



# DIGITAL TAXATION IN INDIA: AN OVERVIEW OF EQUALISATION LEVY AND SIGNIFICANT ECONOMIC PRESENCE

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## ABSTRACT

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India has emerged as one of the fastest-growing digital economies, driven by rising internet use, smartphone adoption, and expanding e-commerce activities. The growing presence of multinational digital platforms exposed weaknesses in traditional tax rules based on physical presence. To address this, India introduced the Equalization Levy (EL) in 2016, initially imposing a 6 percent tax on online advertising and later expanding it in 2020 to a 2 percent levy on non-resident e-commerce operators. However, in line with global tax reforms under the OECD framework, the 2 percent levy was abolished in 2024 and the 6 percent levy is proposed to be removed in 2025. With the phase-out of the EL, Significant Economic Presence (SEP) now serves as India's primary rule for taxing the digital economy, subject to treaty compatibility and profit attribution clarity.

**KEY WORDS:** Digital Taxation, Equalisation Levy, E-commerce, Advertisement tax (Google Tax) and SEP

## INTRODUCTION

Economic systems have historically evolved alongside major technological innovations such as the telegraph, railways, and modern communication networks. In the contemporary era, the internet stands out as a transformative force due to its global reach, connecting both developed and developing economies. This revolution has led to the emergence of the digital economy, often described as the third wave of capitalism, fundamentally reshaping how businesses and governments create value, exchange services, and generate wealth. India provides a particularly compelling example of this transformation. Over the three decade, the country has emerged as one of the fastest-growing digital economies in the world, supported by rapid smartphone adoption, expanding mobile internet penetration, affordable data services, and policy initiatives promoting digital inclusion. This expansion has been accompanied by significant growth across various digital activities, including e-commerce transactions, digital payments, online education, and platform-based services. India's digital payments ecosystem, notably driven by the Unified Payments Interface (UPI), has positioned the country as a global leader in real-time payment systems. While digitalisation has created immense economic opportunities, it has also introduced complex challenges for traditional taxation systems. Advances in information and communication technologies (ICT), platform-based business models, and remote digital service delivery have fundamentally changed how value is generated. Rapid digitalisation has increased the global use of online platforms for buying goods and services such as google, Facebook, Amazon. This has

allowed businesses to operate from anywhere, often choosing countries with lower taxes. As a result, governments became concerned about tax avoidance and revenue loss. To address this, the Organisation for Economic Co-operation and Development (OECD) introduced the Base Erosion and Profit Shifting (BEPS) framework, suggesting that existing tax rules should be adapted for the digital economy. However, since these guidelines were not legally binding, countries followed different approaches.

India took an early step by introducing the Equalisation Levy in 2016. It first applied a 6 percent tax on online advertising services provided by non-resident companies. In 2020, the levy was expanded to include a 2 percent tax on e-commerce supplies of goods and services by foreign companies without a permanent establishment in India. The levy was designed as a tax on transactions, separate from income tax and GST, and included rules for payment, interest, and penalties. The rise of such digital taxes led to global disagreements, especially because many affected firms were large multinational tech companies. Significant Economic Presence (SEP) was introduced by India through the Finance Act, 2018 to address the taxation challenges of the digital economy. SEP expands the concept of "business connection" by allowing India to tax non-resident enterprises based on their economic engagement rather than physical presence. A foreign entity is considered to have SEP in India if it exceeds prescribed revenue thresholds or maintains significant interaction with Indian users through digital platforms. This provision reflects a shift from traditional

Permanent Establishment (PE) rules and aligns with global efforts, particularly the OECD’s BEPS Action Plan 1, to tax digital businesses based on value creation. Although the Equalisation Levy generated revenue, its planned withdrawal may cause short-term losses. Still, better global tax coordination and increased investment may balance this over time.

**REVIEW OF LITERATURE**

**Jaiswal (2022)** The paper examines the taxation challenges created by the rapid growth of the digital economy, with a focus on India’s Equalization Levy (EL). It clearly explains India’s early adoption of the EL in 2016, initially on online advertising and later expanded in 2020 to e-commerce transactions. The study outlines key objectives, including analysing Digital Public Infrastructure and Platforms (DPIPs), the digital ecosystem in finance, health, and commerce, and the legal provisions related to the EL. Using secondary data, the paper highlights how digitalization has blurred the distinction between digital and traditional economies and altered cross-border business models. Overall, the paper provides a useful overview of India’s digital taxation framework, though it could benefit from deeper empirical analysis and updated discussion of recent reforms.

**Shrey and Mahi (2024)** The paper provides a clear overview of India’s Equalisation Levy (EL), outlining its objectives, expansion, criticisms, and eventual abolition. It effectively

links India’s experience with broader global debates, particularly US opposition and the OECD’s Two-Pillar Solution. The discussion appropriately highlights key policy tensions—revenue protection, double taxation risks, compliance burdens, and innovation concerns. The conclusion is balanced, noting that while abolishing the EL aligns India with global reforms, implementation challenges under Pillar One and Pillar Two remain. The paper is conceptually strong, though it would benefit from tighter language, removal of repetitions, and deeper empirical evidence to strengthen its arguments.

**OBJECTIVE OF THE STUDY**

1. To Examine the trends Digital Taxation in Indian Economy.
2. To Study the key components of the Equalisation Levy in India.

**METHODOLOGY**

This is a descriptive based study. The data were sourced from the RBI, National Payments Corporation of India, Statista, Rajya Sabha OLTA, budget from 2014-2024.

**RESULT AND DISCUSSION**

Digital revenue is the income generated from digital activities such as online advertising, e-commerce, digital services, and platform-based business operations.

**Table 1: The Expansion of India Digital System from 2016 to 2024**

Year	Internet user (in percentage)	UPI value (Rs in crore)	E-Commerce (US \$ billion )
2016	16.5	707.93	14
2017	18.2	13,174.24	20
2018	20.8	1,02,594.82	39
2019	29.52	2,02,520.76	21.9
2020	43.40	4,16,176.21	30
2021	48	8,26,848.22	67
2022	52	12,82,055.01	84
2023	55	18,41,083.97	102
2024	58	23,24,699.91	125

Source: IBEF,RBI, IAMAI, NPCI

The data presented in Table 1 highlight the rapid expansion of India’s digital economy over the period 2016–2024. Internet usage increased significantly from 16.5 per cent in 2016 to 58 per cent in 2024. During the same period, the value of UPI transactions rose markedly from ₹70,793 crore to ₹23,24,699 crore. Parallel to this growth, the e-commerce market expanded substantially, reaching US\$125 billion in 2024. The expansion of internet access has significantly accelerated digital transactions and online commerce, thereby highlighting the need for adaptive digital taxation policies.

**Equalisation Levy in India**

The rapid growth of digital technology has transformed the global economy and created major challenges for traditional tax systems (WTO, 2019). A leading institution in addressing these issues is the Organisation for Economic Co-operation and Development (OECD), established in 1961 and headquartered in Paris. The OECD plays a central role in global tax policy and digital economy regulation. Although India is not an OECD

member, it is a key partner and actively participates in OECD-led tax initiatives. At the OECD Ottawa Ministerial Conference (1998), framework conditions for taxing electronic commerce were introduced. The OECD’s Committee on Fiscal Affairs (CFA) issued guiding principles based on neutrality, efficiency, certainty, simplicity, effectiveness, fairness, and flexibility. The framework also covered taxpayer services, administration, tax collection, control, consumption taxes, international tax treaties, and cooperation. Concerns grew as multinational enterprises (MNEs), especially digital firms, shifted profits to low-tax jurisdictions. To address this, the OECD launched the Base Erosion and Profit Shifting (BEPS) Project (2013). India actively engaged in BEPS discussions because digital companies were generating profits from the Indian market without a physical presence, thereby escaping taxation under Permanent Establishment (PE) rules. Tax systems also struggled to capture value created through digital activities such as user participation and data.

The OECD's 2015 report, "Addressing the Tax Challenges of the Digital Economy," proposed three measures: a new nexus based on Significant Economic Presence (SEP), a withholding tax on digital transactions, and an equalization levy. Later, the OECD introduced the Two-Pillar Framework (2021). Pillar One reallocates taxing rights to market countries, while Pillar Two establishes a global minimum tax to reduce profit shifting. In line with these developments, India introduced the Equalization Levy (Finance Act, 2016) to create a level playing field between domestic and foreign digital enterprises. The levy applied to non-resident entities without a PE in India, allowing taxation of revenues linked to Indian users, IP addresses, and digital advertising. Under the 2016 provisions, the levy mainly targeted online advertising, imposing a 6 per cent tax on payments to non-resident service providers. This functioned like a withholding tax. Although concerns arose regarding double taxation, the levy operates outside the DTAA framework. To prevent domestic double taxation, Section 10(50) of the Income Tax Act, 1961 exempts income subject to the levy from regular income tax. The Finance Act, 2020 expanded the levy to non-resident e-commerce operators, imposing a 2 per cent tax on gross consideration from online sales of goods or services to Indian customers, subject to the turnover threshold.

**Table 2 : Equalisation levy in India from 2016-2017 to 2024-2025**

Year	Equalisation Levy (Rs in Core)
2016-2017	338.6
2017-2018	589
2018-2019	938.9
2019-2020	1,136
2020-2021	1492.7
2021-2022	-
2022-2023	4000
2023-2024	3,500
2024-2025	3,300

**Source:** Rajya Sabha OLTAS, Time of India, business today

Table 2 explain about the Equalisation levy in India from 2016-2017 to 2024-2025. Revenue increase from 338.6 from 2016-2017 to 3,300 from 2024-2025. This trend underscores the growing importance of digital taxation in revenue mobilisation.

### Equalisation levy charged

The Equalisation Levy is imposed on specified digital transactions involving non-resident entities deriving income from the Indian market. The levy applies where a foreign e-commerce operator provides, facilitates, or supplies goods and services to persons resident in India, users accessing services through an Indian IP address, or transactions linked to Indian users, including targeted advertising and data monetisation. This provision reflects India's effort to establish a tax nexus based on significant economic presence rather than physical presence.

The Equalisation Levy applies to online advertisement and digital advertising services provided by non-resident entities. The Indian resident or a non-resident with a Permanent Establishment (PE) in India receiving the service is responsible for deducting the levy. This mechanism ensures that advertising

revenues earned by foreign digital platforms from India are subject to tax.

### Exemptions Equalisation levy

The Equalisation Levy is not applicable under certain defined conditions. It does not apply where the aggregate consideration from relevant digital transactions falls below the prescribed threshold (₹2 crore for e-commerce supply or services). Additionally, the levy is excluded where the non-resident entity maintains a Permanent Establishment (PE) in India, and the income is effectively connected with such PE, thereby falling within the scope of regular income taxation. The levy is also designed to prevent duplication in cases where transactions are otherwise taxable under existing provisions of domestic tax law.

The levy is not imposed where the non-resident service provider has a PE in India and the advertising service is effectively connected with that PE. Further, transactions involving consideration below the statutory threshold (₹1 lakh annually) are excluded. Services obtained for personal, non-commercial purposes are likewise exempt, ensuring that the levy primarily targets commercial digital transactions.

### Significant Economic Presence (SEP)

The abolition of the Equalization Levy (EL), the taxation of digital services now relies on the Income Tax Act, 1961. Section 9 defines when income is deemed to accrue or arise in India, and under Section 9(1)(i), a non-resident's income may be taxed if it is connected to a "business connection" in India, including economic transactions with Indian customers or agents. Recognizing the limitations of traditional tax rules in addressing digital business models, the Finance Act, 2018 introduced the concept of Significant Economic Presence (SEP). SEP expanded the "business connection" principle by establishing a taxable nexus based on revenue or user thresholds, even without physical presence, reflecting the OECD's BEPS Action Plan 1, which emphasizes taxation based on economic participation rather than physical location. For several years, SEP and the EL coexisted, with SEP operating within the income tax framework and the EL functioning as a separate levy. The Finance Act, 2024 abolished the 2% levy (effective August 1, 2024), and the Finance Act, 2025 proposed the removal of the 6% levy (effective April 1, 2025). India's SEP provisions apply when a foreign enterprise exceeds prescribed thresholds, namely a revenue-based threshold of more than ₹2 crore (INR 20 million) from Indian transactions in a financial year, or a user-based threshold involving systematic and continuous business activities or engagement with 300,000 or more Indian users through digital platforms. Unlike the traditional Permanent Establishment (PE) rule, SEP allows taxation based purely on economic engagement, even in the absence of physical presence.

### CONCLUSION

India has become one of the world's fastest-growing digital economies, with nearly 58 percent of its population using the internet and increasing engagement in e-commerce. This digital expansion led India to introduce the Equalization Levy (EL) to tax foreign enterprises that generate income from the Indian market without maintaining a physical presence. Introduced in 2016, the EL initially imposed a 6% levy on online advertising

and was later expanded in 2020 to include a 2% levy on non-resident e-commerce operators. With the gradual phase-out of the EL, Significant Economic Presence (SEP) has emerged as India's primary domestic nexus rule for taxing the digital economy, although its effectiveness depends on treaty alignment and clear profit attribution rules.

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