



Impact of GST on online marketplaces

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Abstract

E-commerce is fast gaining traction in today's world. In simple terms, e-commerce can be described as the conduct of any commercial activity using the Internet as a medium. The scope of e-commerce is dynamic and consistently expanding. The online marketplace business model has been the most successful model in India, given the foreign direct investment (FDI) and regulatory norms currently in existence. Therefore, this study focusses more on online marketplaces while studying the e-commerce sector in India. Multiple indirect taxes are currently levied on transactions in India. Some taxes are levied and collected by the central government, while others are collected by state governments. Furthermore, due to the dynamic and complex business models in which e-commerce players operate, the treatment of various e-commerce transactions under indirect taxes is fraught with ambiguity and disputes.

Considering the issues plaguing the current indirect tax regime, India is gearing up to introduce a comprehensive indirect tax regime under the Goods and Services Tax (GST). Introduction of the GST regime will affect the very fundamentals of how business is carried out in India, it is essential to reflect upon the impact on online marketplaces. This paper starts with a brief overview of the conditions under the existing indirect tax regime. It then goes on to discuss the outline of the GST proposal based on the available information. Next, the paper attempts to identify the key factors that might prove to be important for online marketplaces under the proposed GST regime. Finally, certain recommendations are offered on the basis of our detailed study.

Keywords: e-commerce, marketplaces, waybill, issues in the current regime, VAT

Introduction

Goods and Service Tax (GST) will roll out nationwide on 1st July 2017, marking a revolutionary change in the Indian taxation system. Businesses operating both online and offline are already gearing up to migrate to the new tax system and figuring out how to be compliant in the GST era.

While GST is surely going to bring about much required standardization in the commerce landscape; in line with the motto 'one nation, one tax', there are several aspects of GST that will change how businesses operate.

In the last decade, e-commerce has seen an unprecedented growth and India is pegged as the second largest market for e-commerce. The e-commerce market in the country is expected to breach the \$100- billion mark by 2020. The explosive growth in the sector has given rise to multiple tax issues along with other challenges such as rising competition, shrinking profit margins etc. They are also facing litigation owing to their innovative business models.

The Government is trying to simplify the tax structure by introducing GST and promoting trade, while keeping a check on tax evasion. Let's see how implementation of GST will impact e-commerce marketplaces (operators).

Issues in the current regime

Given that online marketplaces are a relatively new phenomenon, the conventional indirect tax regime in India is unsuccessful in providing complete clarity on the appropriate tax treatment of e-commerce transactions. To ensure that the GST regime takes into account the existing anomalies and

suitably addresses them, an overview of the current indirect tax regime and some of the key issues being faced by e-commerce players is provided below.

1. Person liable to pay tax

Background and relevant provisions in a conventional sale transaction, the seller of the goods is the 'dealer' liable to deposit value added tax (VAT) with the authorities. A dealer, as broadly defined under the VAT legislation in various states, is liable to register under VAT and undertake all compliances such as payment of VAT/central sales tax (CST) and filing of returns. In online marketplace transactions, given that each transaction involves multiple parties, tax authorities are often confused about the identity of the actual seller who is liable to pay taxes.

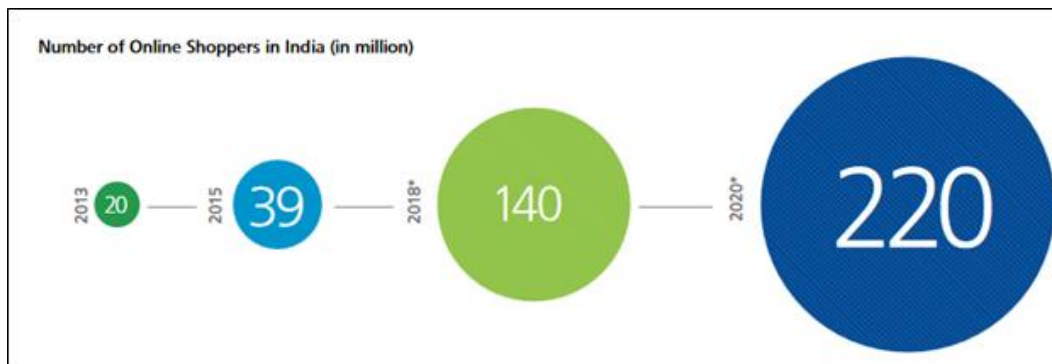
Key Concerns

The activities of online marketplaces have often been misconstrued as the activities of a 'seller' by local tax agencies. It is imperative to have consistent guidelines under different VAT legislation, affixing the liability to deposit VAT/CST, obtain registration and undertake related compliance. Key concerns Requirements Even if the online marketplace's involvement in the transaction is limited to packing, repacking and forwarding the consignment to the buyer, the authorities often insist that the e-commerce player is the 'dealer' that is liable to pay taxes and undertake all related compliance. Thus, the intermediary role played by online marketplaces needs to be acknowledged.

2. Waybill Compliances

Background and relevant provisions VAT legislation under various states prescribes the manner in which inward and outward movement of goods is to be undertaken. Generally, a dealer in the state is required to obtain waybills from VAT authorities (either manually or by online generation). The Gujarat authorities issued a clarification

allowing e-commerce consignments to carry manual waybills in case it is practically challenging to generate online waybills for each consignment (especially in the case of low-value goods). In Uttar Pradesh, the customer is required to obtain, fill and send Form 39 to the shipper to authorize the movement of goods into the state. Similar issues are being faced in Uttarakhand.



(Source: <http://italiaindia.com/images/uploads/pdf/april-2016-e-commerce-in-india.pdf>)

Fig. 1: Number of Online Shoppers in India (in millions)

Key Concerns

The person liable to undertake waybill compliance, i.e. whether the online marketplace or the vendor is liable to undertake waybill compliances While under a federal structure, each state has the authority to track inward and outward movement, this setup goes against the essence of 'free Key concerns Requirements Even though the online marketplace player is not the dealer, given that there are a number of interstate movements (procurement from vendors, supply to customers), the compliance requirements need to be tracked properly and movement should be facilitated with appropriate documentation. E-tail transactions are generally of low value. Accordingly, it is not practical to undertake protracted compliance for each consignment of low-value items. Recognizing this predicament of e-commerce players, Gujarat VAT authorities have issued a specific clarification. However, other states have not yet addressed this issue and it continues to remain a compliance nightmare for online marketplaces.

3. Furnishing of information as prescribed under VAT legislation

Background and relevant provisions Several states have recently started making provisions for furnishing of information by e-commerce players: • Kerala has introduced section 54A to the Kerala VAT Act, 2003, which provides that e-commerce companies have to obtain registration and file returns. There are no provisions under most VAT legislations that correctly identify online transactions. Rationalized and consistent compliance is required by e-commerce players across different states to simplify the process of doing business.

Key Concerns

Requirements VAT authorities have started to demand a vast amount of information under the assumption that this information will help to avoid tax leakage. The fluctuating statutory obligations in each state lead to a high compliance cost and time for online marketplaces. • Tamil Nadu VAT

authorities have issued a press release seeking to tax various transactions undertaken by online portals. • Delhi has prescribed a return format for the filing of information for e-commerce players on a quarterly basis. • UP VAT authorities have also issued instructions to their field officers for scrutiny of the transactions of e-commerce players and ascertaining whether or not tax is duly discharged. • Maharashtra VAT authorities have proposed the introduction of an amendment to track all sales and purchases by online portals for ensuring that VAT/CST is duly paid.

4. Valuation in case of 'discount funding'

Background and relevant provisions VAT/CST is required to be paid on the sale of goods. The 'sale price' on which such VAT/ CST is payable is defined under different VAT legislation. Generally, sale price refers to the amount of valuable consideration paid or payable to a dealer for any sale made, including any sum charged for anything done by the seller in respect of the goods prior to delivery (transportation, installation, etc.).

Key Concerns

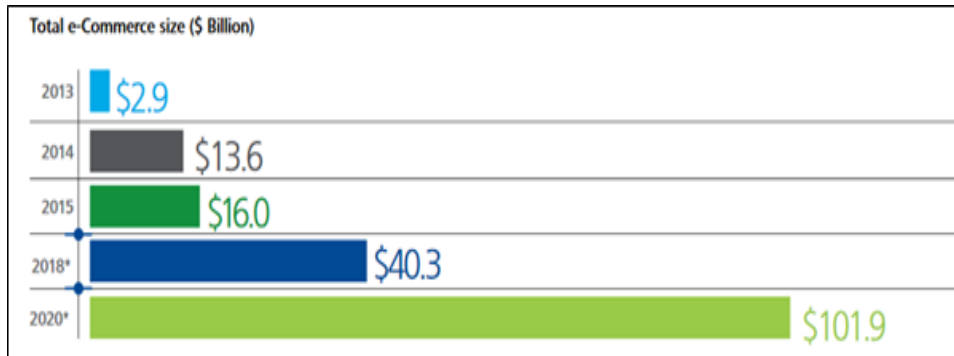
In practical terms, the cost of the sizable discounts offered by vendors on e-commerce sites is borne by the e-commerce players. Given the peculiar nature of e-commerce transactions, VAT/CST laws should provide clarity on the treatment of such situations to ensure minimal litigation. Key concerns Requirements For example, products priced at 100 INR per unit are sold by the dealer on the website at a discounted price of 70 INR per unit. While the end consumer ends up paying the discounted price, the balance 30 INR is paid by the e-commerce player to the vendor for promoting its own business. In e-commerce trade parlance, this is commonly known as 'burning cash for promotion'. VAT authorities are demanding tax on the discount funding by treating the amount being paid by the e-commerce players as part of the sale price for goods on behalf of the buyers. Thus, the authorities intend

to tax the loss incurred on trading of goods.

5. VAT/CST treatment in the case of sales returns, cancellations and replacements

Background and relevant provisions generally, there are specific provisions under state VAT legislation for adjustments to be made in taxable turnover on account of sales returns, cancellations, etc. For instance, VAT is chargeable on

‘turnover of sales’ under the Maharashtra VAT Act, 2002. The definition of turnover under section 2(33) of the Maharashtra VAT Act, 2002, specifically excludes the turnover pertaining to sales returns which has been refunded to customers. This deduction is subject to the condition that the sales returns are made within six months of the sale. Appropriate disclosures pertaining to the sales returns are required to be made in the periodic returns.



(Source: <http://italiaindia.com/images/uploads/pdf/april-2016-e-commerce-in-india.pdf>)

Fig. 2: Total e-Commerce size (\$ Billion)

Key Concerns

E-commerce players routinely offer products on cash on delivery (CoD) terms to customers. According to the CoD terms, a customer is liable to pay cash only when the goods are physically in his/her hands. Robust systems are required, keeping in mind the peculiarities of the e-commerce sector, to ensure that sales returns, cancellations, etc., are duly tracked and all requisite compliance, such as maintenance of documents, disclosure of returns, payment of taxes and availing of deductions, is done accurately. Key concerns Requirements and he/she is satisfied with the delivered product. There are also piecemeal returns and cancellations rather than bulk ones, as in the case of conventional sellers. In such situations, it is difficult to keep the paper trail intact for each case in each state as well as to appropriately claim adjustment for such returns from the VAT authorities.

6. Sale of digital content

Background and relevant provisions Sale of goods attracts VAT/CST and ‘goods’, as defined under various VAT legislations, include tangibles as well as intangibles. Some states have specific entries for taxing intangibles. While the taxing of intangibles that are supplied over a medium is relatively easier, there are no specific provisions for the download of digital content online.

Key Concerns

Digital content such as software, e-books and music albums is often sold over the Internet. Generally, once this content is purchased from the portal, it can be accessed by the customer from any with the increase in transactions relating to digital content, it is vital that clear laws are formulated with regard to taxability, along with related compliance. Key concerns Requirements device by simply downloading after entering the login credentials.

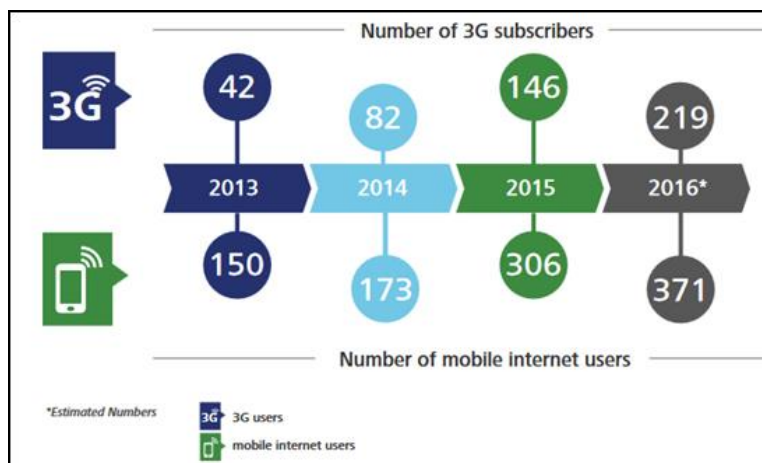


Fig. 3: Number of 3G and mobile Internet Users in India (Source: Mobile Internet in India IAMAN)

7. Combo offers

Background and relevant provisions VAT/CST is payable at the applicable rate on the sale of goods. The applicable rate is based on the exact nature and description of the goods sold. Further, composite supplies of both goods and services may qualify as 'works contracts' which entail specific tax treatment under indirect taxes.

Key concerns

Similar to traditional retail sales, a bundle of two or more related goods (or goods plus services) is offered as a combo offer for a single consideration by sellers over online marketplaces. Clear and concise guidelines regarding classification and valuation in the case of e-commerce

transactions should be laid down to avoid placing an excessive burden on end users as well as high litigation costs for both e-commerce players as well as the authorities. Key concerns Requirements In case the goods bundled together under the combo offer attract VAT/CST at different rates, the authorities may levy tax at the higher rate, thereby leading to an increase in the overall cost of the product. In the absence of any reasonable basis of bifurcation of the consideration, in many cases, tax is being paid at the highest applicable rate to avoid litigation, leading to an increased cost. Further, if goods and services are being combined under these combo offers, such offers should be clearly analysed to ascertain whether they qualify as works contracts.

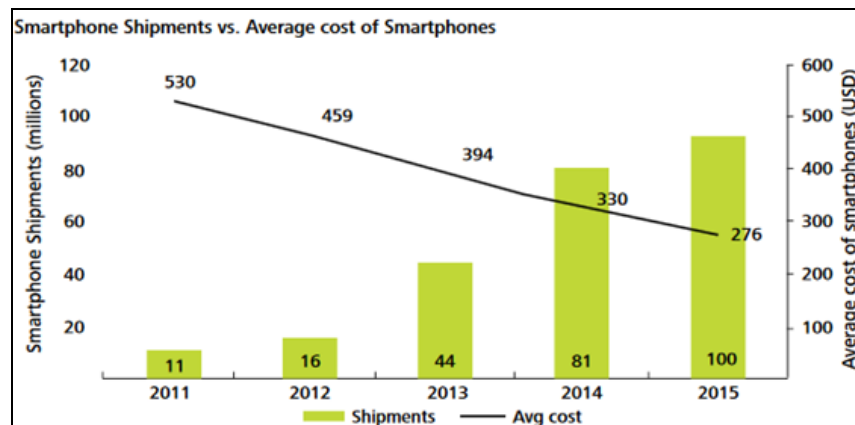


Fig 4: Smartphone shipments and change in average cost of high-end smartphone in India (source: Statista.com)

Conclusion

While there were certain issues that were addressed by the Model GST Law, many issues that prevailed in the existing tax regime still remain. E-Commerce entities are still worried about how combo offers will be taxed, or what will be the taxable amount in case these entities bear the cost of discount provided by them, also known as "burn cost".

While, the negative impact in respect to compliance cost is far rigorous than the benefits provided by the new law, it is true only in the short term. In the long term, GST will prove to be very beneficial to e-commerce sector as it is expected to end the feud between tax authorities and e-commerce operators like Amazon and Flipkart qua the levy of tax, which has been the most litigated aspect in the sector. Along with clarity in levy of tax, seamless tax credit will add to positive growth of the e-commerce sector.

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