

F. No. 370142/11/2018-TPL
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes

New Delhi, dated the 13th of July, 2018

Subject: Framing of Income-tax rules relating to Significant Economic Presence as per Section 9(1)(i) of the Income-tax Act, 1961, Comments and suggestions reg.

As per the allocation of taxing rules under Article 7 of Double Taxation Avoidance Agreements, business profit of an enterprise is taxable in the country in which the taxpayer is a resident. However, if an enterprise carries on its business in another country through a 'Permanent Establishment' situated therein, such other country may also tax the business profits attributable to the 'Permanent Establishment'. For this purpose, 'Permanent Establishment' means a 'fixed place of business' through which the business of an enterprise is wholly or partly carried out provided that the business activities are not of preparatory or auxiliary in nature and such business activities are not carried out by a dependent agent.

2. For a long time, nexus based on physical presence was used as a proxy to regular economic allegiance of a non-resident. However, with the advancement in information and communication technology in the last few decades, new business models operating remotely through digital medium have emerged. Under these new business models, the non-resident enterprises can carry on business and interact with customers in another country without having any physical presence in that country resulting in avoidance of taxation in the source country. Therefore, the existing nexus rule based on physical presence no longer holds good for taxation of business profits in source country. As a result, the rights of the source country to tax business profits that are derived from its economy are unfairly and unreasonably eroded.

3. In view of the above, Finance Act, 2018 introduced the concept of 'Significant Economic Presence' (SEP) in the Income-tax Act, 1961 ('the Act') for taxation of non-residents in India by amplifying the scope of the definition of "business connection" through Explanation 2A to section 9(1)(i) of the Act. The definition of 'business connection', was clarified to provide that a non-resident's significant economic presence in India shall constitute "business connection" of the non-resident in India and the "significant economic presence" for this purpose shall mean-

- (i) any transaction in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India if the aggregate of payments arising from such transaction or transactions during the previous year exceeds the amount as may be prescribed; or
- (ii) systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed, in India through digital means.

3.1 It is further provided that the transactions or activities shall constitute significant economic presence in India, whether or not the agreement for such transactions or activities is entered into in India or the non-resident has a residence or place of business in India or renders services in India. Moreover, it is also provided that only so much of income as is attributable to the transactions or activities referred above shall be deemed to accrue or arise in India..

4. Accordingly, for the purpose of determining significant economic presence of a non-resident in India, the threshold for the aggregate amount of payments arising from the specified transactions and for the number of users requires to be prescribed.

5. In this regard, suggestions/comments of stakeholders and the general public are invited on the following:

- (i) Revenue threshold of transaction in respect of physical goods or services carried out by a non-resident in India;
- (ii) Revenue threshold of transaction in respect of digital goods or services or property including provision of download of data or software carried out by a non-resident in India;
- (iii) Threshold for number of ‘users’ with whom a non-resident engages in interaction or carries out systematic and continuous soliciting of business activities in India through digital means.

6. Comments and suggestions may be sent electronically by 10th August, 2018 at the email address ustpl3@nic.in.

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