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E-Gaming Taxation and Government Recommendations, Shrouded in Self-Defeatism

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ABSTRACT

This article analyses the e-gaming taxation regime of India and points out a few fundamental flaws with the same. It recognizes the government's wish to increase the impetus for the growth of the industry but argues that due to the taxation regime set up by the government itself which imposes huge amounts of tax burden on the industry, the said objective becomes impractical to materialize.

Firstly, it introduces the problem at hand and then builds up to criticize the immense taxation burden that could be induced by the complete implementation of the GST council which states to tax the games based on skill and chance in the same bracket and points out decades of jurisprudence in contravention of the said recommendation of the council.

Secondly, it starts to examine the newly introduced provisions of the Income Tax Act which are sections 115BBJ and section 194BA, and critiques the functional appropriateness of the said provisions, it criticizes section 194BA on the grounds of ambiguity in determining net winnings liable to be taxed from the financial year, thirdly it finds flaws in section 115BBJ on the grounds of its possible faulty application while calculating the gross prize money

The article provides an instance of such over-taxations by giving the example of the DeltaCorp case and then concludes by asserting that due to such huge taxation pressure, the e-gaming industry will not be able to survive properly let alone grow hence the taxation regime being self-defeatist in nature and makes a case for decreased taxation pressure on the industry while simultaneously promoting dialogue as a possible solution for the problem.

Keywords: *E-gaming, Taxation, games of skill v games of chance.*

I. INTRODUCTION

In the contemporary day and age, the online industry has permeated every intricate aspect of both personal and professional lives and its impact is unequivocally undeniable²

¹ Author is a student at Hidayatullah National Law University, Raipur, India.

² Wa'el Hadi and Sahem Nawafleh, 'The Role of E-Business in the e-Government Services Implementation'

The same digital ecosystem when coupled with the gaming industry gives rise to the e-gaming sector which in layman's terms means any digital game that one can play while being connected to the internet³, the one who is playing the game is called the e-gamer, and the one who is organizing such a gaming event is called the gaming intermediary.

According to MeitY (ministry of electronics and information technology) online gaming means "a game that is offered on the Internet and is accessible by a user through a computer resource or an intermediary"⁴

The birth Indian gaming industry is one of the newest developments in the economic ecosystem of India, and the government by various policies and gestures announced its openness for the industry to grow and invite foreign investment for instance a self-regulatory framework has been implemented by the Ministry of Electronics and Information Technology (MeitY) for the online gaming sector, wherein Self-Regulatory Bodies (SRBs)⁵ will validate games that can operate in the country⁶ hence providing the gaming industry with a self-regulation mechanism and enhanced development and on the other hand tightening privacy rules regarding the access to personal information of a gamer in an online game, therefore, inviting more players to join and contribute to the development of the industry freely⁷.

II. THE SUDDEN URGE OF THE GOVERNMENT TO TAX

The E-gaming industry although not the backbone of the economy is still a sizeable industry of around 442 million users⁸ but has made its mark in both staying on top of the news and in monetary terms with expected revenue to touch around 1.6 billion USD by 2028⁹ in valuation due to the much-felt shift toward the digital economy and ecosystem, naturally this industry provides a new-lucrative hotspot for the government to set up taxation regime for raising revenue, consequentially the government has recommended and inserted certain new provisions which when read conjointly with the old provisions formulate the online gaming

(2012) 4 International Journal of Academic Research 230.

³ Claire Milne, 'E-Gaming in the Isle of Man: A Primer' (2010) 14 Gaming Law Review and Economics 371.

⁴ The Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Rules, 2021 Vide G.S.R. 139(E), dated 25.2.2021, published in the Gazette of India, Extra., Pt. II, Sec. 3(i), dated 25.2.2021

⁵ Shouvik Das, 'It's over to Govt Now in Gaming Regulation' (*mint*, 1 January 2024) <<https://www.livemint.com/industry/online-gaming-self-regulation-hits-roadblock-meity-weighs-direct-control-11704104343456.html>> accessed 15 March 2024.

⁶ Sec 3 Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Rules, 2021

⁷ 'Here's How New Rules Can Give a Big Push to India's Online Gaming Industry - BusinessToday - Issue Date: Feb 05, 2023' <<https://www.businesstoday.in/magazine/corporate/story/heres-how-new-rules-can-give-a-big-push-to-indias-online-gaming-industry-366983-2023-01-21>> accessed 15 March 2024.

⁸ Gaming Industry in India (Invest India) <<https://www.investindia.gov.in/sector/media/gaming>> accessed 22 December 2023

⁹ *ibid*

taxation regime of India¹⁰, which becomes complex due to intricate role play between different provisions and stakeholders in this rapidly developing industry, this article explores the stance taken by the Government and the judiciary in relation to the E-gaming taxation and analyses whether the new and proposed changes to the taxation regime serves as a growth impetus to the industry or acts as a death knell to the growth of the industry¹¹

(A) Games based on skill and chance taxed in the same bracket

As of now the position In Indian jurisprudence regarding the different taxing of E-games based on skill from those based on luck/chance is experiencing a monumental change of events and the set positions of taxing are being changed and the final answer to the question seems to be a puzzle which is being solved differently by different stakeholders but one conclusion remains functional that taxing games based on skill and chance in the same bracket is fundamentally erred due to there being a significant difference between gambling and skilful play

(B) Over-taxing can kill the industry's growth prospects

The accouchement of the view of the GST council regarding the nullification of a distinction factor between games of skill and games of chance can be traced to the 47th GST council meeting¹² wherein the council recommended taxing the e-games at 28% on the total contestant entry amount contributed by the users which was then partially implemented by the GST council in 50th GST council meeting¹³ wherein the council implemented a flat 28% GST for games based in luck(gambling) and reaffirmed the assertion of charging GST on both games based on skill and chance in the same bracket, although not implementing it. This when read conjointly with the newly introduced sections 115BJ and 194BA vide the Finance Act 2023 makes the effective rate of implementation of tax exceedingly high and hence will completely deny the industry of any possible financial goals.

(C) The Council's View is in contravention of decades of jurisprudence

The council's view in regards of taxing both the games based on skill and games based on chance in the same bracket is fundamentally erred and doesn't take into consideration the decades of jurisprudence which surrounds the issue, as far back as in 1957 the issue of games

¹⁰ 'Tax on Online Gaming in India - Tax2win' <<https://tax2win.in/guide/tax-on-gaming-in-india>> accessed 15 March 2024.

¹¹ 'India's Tax on Gaming Industry the Highest - The Hindu BusinessLine' <<https://www.thehindubusinessline.com/data-stories/visually/indias-tax-on-gaming-industry-the-highest/article67107177.ece>> accessed 15 March 2024.

¹² Agenda for 47th meeting (GST Council)< <https://gstcouncil.gov.in/sites/default/files/Agenda/Agenda-Volume-1-for-47th-GSTCM.pdf> > accessed 25 December 2023

¹³ Minutes of the 50th GST Council meeting (GST council) <https://gstcouncil.gov.in/sites/default/files/Minutes/Minutes_of_50th.pdf> accessed 26 December 2023

of skill Vs games of chance came before the SC in the case of *RMD Chamarbaugwala V UOI*¹⁴ wherein the hon'ble court stated that if in the game substantial skill is involved then the game can't be said to be one based on chance and

In furtherance of the same in state of *AP V K satyanarayan*¹⁵- the SC held the game of rummy to be a game of skill and beyond the ambit of gambling hence not liable to be taxed in the higher bracket, the hon'ble court in *MJ Sivani V state of Karnataka*¹⁶ – upheld its view and further laid the preponderance test wherein it held that despite there being certain amount of luck and chance involved in every game then also if the game has skill as a dominant and driving factor in deciding the winner then the game would be considered as a game of skill

The test of preponderance is also internationally prevalent, for instance It was laid down In England in the case of *Rex V Fortier*¹⁷ and in US in *state V Gupton*¹⁸ hence when the government brings in provisions for taxing both the types of online games in the same tax bracket it is not recognizing the fact that the games based on skill are constitutionally protected legitimate source of income under article 19(1)(g) and games based on chance are not protected under article 19(1)(g) as they are '*res extra commercium*'¹⁹, withering away of that distinction is not legally sound as well as undue violation of constitutional protections²⁰.

In the recent case of Goods & Services Tax Intelligence (HQS) v. Gameskraft Technologies (P) Ltd²¹, the Karnataka HC succinctly held that actionable claim based on an amount due is neither classified as a supply of goods and services not as gambling hence going beyond the GST act therefore giving a breather to the industry.

III. STAYING OF KARNATAKA HC ORDER OF GAMESKRAFT TECHNOLOGIES BY THE SUPREME COURT

The Supreme court stayed the order²² of the Karnataka HC in the case of *Gameskraft Technologies Private Limited V directorate general of Goods services Tax Intelligence council*²³ the show-cause notice of 21000 Crore rupees which was earlier quashed by the

¹⁴ [1957] AIR 628; [1957]SCR 930

¹⁵ [1968] AIR 825; [1968] SCR (2) 387

¹⁶ [1995] 6 SCC 289

¹⁷ [13] Que K.B. 308

¹⁸ [30] N.C. 271

¹⁹ The State Of Bombay vs R. M. D. Chamarbaugwala; [1957] AIR 699 ; [1957] SCR 874

²⁰ Datar, Arvind P. (2009) "Privilege, Police Power and res Extra Commercium - Glaring Conceptual Errors," *National Law School of India Review*: Vol. 21: Iss. 1, Article 5. Available at: <https://repository.nls.ac.in/nlsir/vol21/iss1/5>

²¹ [2023] SCC OnLine Kar 18

²² Goods & Services Tax Intelligence (HQS) v. Gameskraft Technologies (P) Ltd.;[2023] SCC OnLine SC 1254

²³ *supra* note 21

Karnataka HC now stands to be valid, therefore it tells a taxpayer that the SC is aligning its view with the view of the GST council regarding the nullification of a distinction factor between games of skill and games of chance.

The SC's decision of staying the order of the Karnataka HC and refusing to thwart the further claim of the tax authorities can be argued as an act by which it is aligning itself with the view of the GST council which presents a picture where the lines between games of skill and chance are blurred and consequentially can act a final nail in the coffin for the already sunrise industry facing multiple challenges from different issues and policy concerns²⁴.

IV. THE INDIAN E GAMING TAXING MODEL – IN CONTRAVENTION OF THE GLOBALLY SET MODELS OF TAXATION

There are 2 major models of taxing the income generated by the e-gaming industry worldwide namely the **GGR model**²⁵ and the **turnover tax model**²⁶, while analysing the Indian taxing regime on E-gaming one can quickly understand that the taxation model in India is in contravention of both the industry set and globally prevalent modes of taxation for the E-gaming industry.

The GGR model or the Gross Gaming revenue model imposes moderate rates of taxation on the E-gaming sector as the entry amount of the game gross revenue is taxed in consequence the rates are kept high because the amount deducted is on the lower side, in contrast in the turnover tax model the entire amount is taxed rather than deductions from the prize pool but the tax rates are kept significantly lower. A closer look at both the tax models will clarify that the maximum taxation in the GGR model is 25% and the maximum taxation in the turnover model is 5.3%²⁷. It portrays a negative image of the country's FDI investment prospects in the gaming industry as any gaming intermediary would be averse to tax rates higher than globally prevalent rates.

FINANCE AMENDMENT 2023 –INCREASED TAX PRESSURE

The Finance Amendment Act 2023 inserts new provisions to the Income Tax Act namely

²⁴ NEXGENO, 'SC Stay on Karnataka HC Judgment' (<https://www.ahlawatassociates.com>) <<https://www.ahlawatassociates.com/news/supreme-court-imposes-an-ad-interim-stay-on-the-karnataka-high-court-judgment-against-gameskraft>> accessed 28 March 2024.

²⁵ Corporate finance institute 'Gross Gaming revenue Overview, Formula, Financial statements' <<https://corporatefinanceinstitute.com/resources/valuation/gross-gaming-revenue-ggr/>> accessed 28 December 2023

²⁶ Fang Wei 'The Optimal Turnover threshold and Tax rate' (7 May 2019) IMF working papers volume 2019 Issue 098(2019) <<https://www.elibrary.imf.org/view/journals/001/2019/098/article-A001-en.xml>> Accessed 28 December 2023

²⁷ Lakshmikumaran & Sridharan 'white paper on Taxability of Online Gaming Income' <<https://www.lakshmisri.com/MediaTypes/Documents/LKS-White-Paper-on-Taxability-of-Online-Gaming-Income.pdf>> Accessed 29 December 2023

sections 194BA and 115BBJ which mandates the flat taxation of income from online games at 30%. This provides a picture of the grim situation because the flat tax virtually makes it impossible for the gaming intermediaries and businesses to conduct their operations without receiving significant harm in their method of conducting business.

This can lead to setbacks in industry gains and losses in jobs furthermore the government also needs to understand that now the E-gaming industry is not working in isolation hence the death of one industry by over-taxation can act as a domino effect for negative chain of events to follow, moreover such high flat-tax rates will hurt the smaller and medium gaming intermediaries the most and as most of the small and medium gaming intermediaries which will be unable to adjust with such a high tax rate are mostly domestic operators, such a high tax rate will definitely unjustly harm the domestic industries and also harm the FDI prospects made possible by the larger gaming intermediaries

V. LOWER LIMIT FOR THE NEWLY ADDED SECTION 194BA – FUNCTIONAL?

The relevant portion of section 194BA of the Income Tax Act²⁸ reads as follows-

“194BA. (1) Notwithstanding anything contained in any other provisions of this Act, any person responsible for paying to any person any income by way of winnings from any online game during the financial year shall deduct income tax on the net winnings in his user account, computed in the manner as may be prescribed, at the end of the financial year at the rates in force”

Earlier there was no lower limit of the taxation under section 194BA(unlike sections 194B and 194BB which have a lower baseline limit of 10000 Rupees)which proposed a peculiar situation for both the player engaging in the gaming activity and the gaming service provider as both of them faced the exposure of petty and minuscule tax-deductions which were proved to be a further negative impetus for the industry as players will be reluctant to participate in the games anymore since more than 99% of players participate in amounts less than 100 rupees

Consequently to stop such a huge decline in available revenue the CBDT had recently issued guidelines for minuscule payments under the newly introduced rule 133²⁹ according to which the tax for the payments will not be deducted subject to the conditions that the withdrawal by the individual from his gaming wallet should not exceed 100 rupees a month

This leads to an ambiguity in interpretation rather than clarifying the position of law as to what

²⁸ Income Tax Act 1961 [43 of 1961]

²⁹ Central board of direct taxes ‘Vide the circular 5 of 2023’ (dated:22 May 2023) <<https://incometaxindia.gov.in/communications/circular/circular-5-2023.pdf>>

constitutes net winnings or in other words at what amount will the Tax be deducted whether, in the difference between the aggregate winning amount and 100 rupees or the entire of the winnings, an illustration can be further utilized to understand this discrepancy better

Suppose a person opens his e-gaming account and deposits Rs 100 then wins Rs 50 then withdraws Rs 90 in the same month a question arises that when is the tax liable to be deducted, at the total of 140 rupees or the difference between the aggregate and 100 i.e. 40 rupees would be considered as the base for the 30% deduction

Therefore, this provision can expose online gaming intermediaries to significantly more harm when considering the tax liabilities and a possible decline in revenue due to the loss of customers as will be natural when high tax liabilities are mechanically imposed without considering the nature of minuscule payments in mind.

(A) Section 194BA should be out of the ambit of section 206AB

The relevant portion of section 206AB³⁰ of the act reads as follows

“Notwithstanding anything contained in any other provisions of this Act, where tax is required to be deducted at source under the provisions of Chapter XVIIB, other than section 192, 192A, 194B, 194BB, 194LBC or 194N on any sum or income or amount paid, or payable or credited, by a person (hereafter referred to as deductee) to a specified person, the tax shall be deducted at the higher of the following rates, namely: —

- (i) at twice the rate specified in the relevant provision of the Act; or*
- (ii) at twice the rate or rates in force;”*

The non-exclusion of section 194BA of the Income Tax Act from section 206AB of the same poses a further impending challenge for the industry as it can inculcate tax liabilities as high as 60% which will be completely impractical as their income is already being taxed under the highest flat tax slab of 30% keeping this in mind the section 194B and 194BB was kept out of the purview of the section 206AB and hence the same for the section 194BA is the need of the hour

(B) TDS under section 115BBJ – the deciding factor?

The relevant part of Section 115BBJ³¹ of the Income Tax Act reads as follows –

“115BBJ. Notwithstanding anything contained in any other provisions of this Act, where the total income of an assessee includes any income by way of winnings from any online game, the

³⁰ N (19)

³¹ *ibid*

income tax payable shall be the aggregate of— (i) the amount of income tax calculated on net winnings from such online games during the previous year, computed in the manner as may be prescribed, at the rate of thirty percent;”

Although the provision seems to be legally sound, one problem with regards to the same is still persistent that the deduction of the TDS from the ‘online winnings’ as u/s 115BBJ should be made while calculating the winnings and not the gross prize money as under numerous circumstances the gross prize money can be mistakenly held to be the net winnings.

For instance, the amount credited to the gaming intermediaries during an E-sports tournament which is to be refunded later cannot be called a net-winning but if the same happens during the period of the tax cycle and the intermediary is not able to complete the E-tournament cycle and consequently not able to return the contribution money to the gamers then according to the language of this provision they will be held liable to be taxed on the entire amount including the money to be refunded later hence the expenditures like the losses in contributions should be off-set to the gaming intermediary and while the deduction of the TDS on the winnings only the income available at hand should be liable to be deducted, the situation becomes even more complicated when the same wallet is mostly used by the individuals for both paying the contribution fee to the gaming intermediary and receiving the rewards from the online intermediary

An illustration of the same can help in proving the point -

At the beginning of the financial assessment year an individual -A puts 11000 rupees in his game wallet and now has lost 6000 rupees in the in-game tournaments but won 9000 with the in-game tournaments so will the TDS be deducted at Rs 14000(11000-6000+9000) or at 20000 because if the recommended change is not implemented in the code the individual will be liable to pay an extra 1800 on TDS tax liabilities which are not part of his income hence putting more pressure on the industry collectively as both the intermediary and the customer will face the loss of income due to the deductions on TDS amount being under clear ambiguity

VI. DELTA CORP CASE – AN INSTANCE OF OVER-TAXING

The minister of the state for finance Mr. Pankaj Chaudhary mentioned in his Rajya Sabha speech³² that 71 show-cause notices have been sent to the online gaming intermediaries amounting to 1,12,332 Cr rupees for alleged income-tax evasion, this instance is the perfect

³² A to Z Taxcorp LLP ‘71 show cause notices issued to online gaming firms involving GST demand of Rs 1.12 Lakh crore’ <<https://www.a2ztaxcorp.com/71-show-cause-notices-issued-to-online-gaming-firms-involving-gst-demand-of-rs-1-12-lakh-cr-finance-ministry/>> Accessed 31 December 2023

example of the harm done to the industry due to over-taxation, the most highlighted instance out of all of them is that of Delta Corp

The casino company Delta Corp. has been sent a direct-tax notice of 11,140 crore rupees and its subsidiaries (Casino Deltin Denzong, Highstreet Cruises, and Delta Pleasure Cruises) have also been issued show cause notices.

Firstly Income tax notices worth 5682 crore rupees were sent, later on the same firm was issued a new GST tax notice which then coupled the entire amount claimed to be 23,206 rupees against the market capitalization of the company which is only 3749 rupees which can be unequivocally said to be an instance of distress to the industry due to over-taxation as the gaming intermediaries are receiving tax notices of an amount which is several times their generated revenue and a major reason for this tax burden comes due to the GST councils decision to impose a flat 28% tax on wagers and gambling³³ as now a player will only receive 72 rupees for a 100 rupees of chips acquired and since demand for the GST amount was made on the gross revenue rather than the rake amount (net profit made by the gaming intermediary)³⁴

Moreover, the consequences of these actions are not only limited to Delta Corp. or the players associated with the e-gaming industry but have wider implications, after the show-cause notice of the direct and indirect tax the company stock price took a massive hit and went down as low as 12% and took some time to recover, later Delta Corp had to put a halt to the IPO of one of its subsidiaries (delta tech gaming) because of the pressure felt from the tax notices.³⁵

Among this unfortunate chain of action was one event which seemed to provide a glimmer of hope to the industry which was the staying of the Tax notice by Sikkim HC³⁶

But very soon that glimmer of hope was seriously limited by the SC when it declined to put a halt on the tax-enforcement authorities' actions and later listed the matter to the 8th of January³⁷ but the court however indicated that it will take the issue of the constitutional validity of the 28% GST taxation into consideration

³³ After the 50th meeting of GST council on 11th July 2023 <https://gstcouncil.gov.in/sites/default/files/Minutes/Minutes_of_50th.pdf> accessed 31 December 2023

³⁴ Business today 'Delta Corp's tax liability soars to Rs 23,206 crore as Deltatech Gaming hit with second GST notice' <<https://www.businesstoday.in/latest/corporate/story/delta-corps-tax-liability-soars-to-rs-23206-crore-as-deltatech-gaming-hit-with-second-gst-notice-402028-2023-10-14>> accessed 1 January 2024

³⁵ Business Today 'Delta Corp shares crash 12% to hit 52-week low after co gets another tax notice' <<https://www.businesstoday.in/markets/company-stock/story/delta-corp-shares-dive-9-after-co-gets-another-tax-notice-heres-what-tech-charts-indicate-402098-2023-10-16>> accessed 2 January 2024

³⁶ W.P. (C) No. 41 of 2023 (Sikkim HC)

³⁷ Writ Petition(s)(Civil) No(s).1384/2023 (SC)

VII. CONCLUSION

In summation, the author humbly submits that the whole scheme of taxation of e-gaming companies is self-defeatist as firstly the industry is unjustly harmed in both monetary aspects and a lack of potential FDI in the industry due to the general aversion of industry investment in jurisdictions with high taxation rates, and secondly, if the current scheme of events continues then the industry will automatically shrink in size therefore the amount of tax collected will naturally reduce

Consequently the current scheme of taxation fails on both ends i.e. – it fails to provide the government with enough revenue in the long run due to the potential shrinking of the industry and secondly unjustly harms the current revenue produced by the industry by taxing on non-justifiable grounds therefore not fitting right with the overall policy of promoting the growth of the sector, hence self-defeatist.

To avoid such negative consequences from materializing the taxing authorities need to step down their taxing rampage and provide some breathing space to the industry as the industry is not only connected to gambling which is viewed in a bad light in the country but also contains in its umbrella, the games of skill and the employees who earn their livelihood which is directly proportional to the growth of the industry i.e. the more the industry has to pay unjustified taxes the more people are prone to be removed out of a livelihood accordingly the tax authorities also need to take into consideration that it's not just the industry that their actions are not limited to the few gaming intermediaries and their respective gaming units but its implications permeate into the lives of an honest worker too.

Finally, the tax authorities need to consider that the tax which they tend to increase is on the games based on skill and will practically eliminate the difference between “*res Extra commercium*” and protected trades under article 19(1)(g) therefore being fundamentally erred in law.

But the onus is also on the e-gaming intermediaries and the gamers to not pursue a vituperative criticism and non-cooperation of the government policies and instead pursue a path of mutual understanding and fruitful dialogue as they are the primary stakeholders in their business and if their business takes a jibe due to their own harmful conduct then blaming the tax code for it would be a futile exercise.
