

Taxing Ads in Mobile Games: Learnings from India's Equalization Levy

Tributação de Publicidade em Jogos Digitais: Aprendizados a partir da Contribuição de Equalização Indiana

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Abstract

This paper examines the taxation challenges posed by digital advertising in mobile gaming through an analysis of India's Equalization Levy. The mobile gaming industry's reliance on advertising revenue creates significant tax policy challenges, as permanent establishment and other traditional tax concepts prove inadequate for capturing value created through user engagement and data collection in market jurisdictions. India's 2016 Equalization Levy represents a pioneering unilateral approach, imposing a 6% tax on online advertising services to address revenue shifting by non-resident digital companies. However, the levy's uniform structure fails to differentiate between advertising types that rely on different levels of user engagement and creates substantial tax gaps when foreign entities structure transactions through offshore arrangements. The paper concludes that effective digital advertising taxation requires sophisticated, internationally coordinated frameworks incorporating tiered taxation and user-based allocation keys that properly compensate market jurisdictions for user-generated value.

Keywords: digital taxation, Equalization Levy, mobile gaming, digital advertising, user data monetization.

Resumo

Este artigo examina os desafios tributários da publicidade em jogos digitais a partir da análise da Contribuição de Equalização da Índia. A forte dependência do setor em relação à receita publicitária desafia conceitos tributários tradicionais, como o Estabelecimento Permanente, que não capturam adequadamente o valor gerado pelo engajamento dos usuários e pela coleta de dados nas jurisdições de mercado. Instituída em 2016, a Contribuição de Equalização indiana representa uma resposta unilateral pioneira, ao impor uma tributação de 6% sobre serviços de publicidade on-line prestados por empresas

não residentes. Contudo, sua estrutura uniforme não distingue modalidades de publicidade com diferentes níveis de participação do usuário e permite lacunas relevantes quando transações são organizadas por meio de estruturas *offshore*. Conclui-se que a tributação eficaz da publicidade digital exige modelos mais sofisticados, com coordenação internacional, critérios de alocação baseados em usuários e mecanismos proporcionais à criação de valor.

Palavras-chave: tributação digital, Contribuição de Equalização, jogos digitais, publicidade digital, monetização de dados de usuários.

1. Introduction

The digital gaming industry has become one of the most dynamic and profitable segments of the global digital economy, with worldwide revenue surpassing the music, radio, podcasts, and cinema global markets¹. With the rise of mobile technology, game developers have increasingly monetized their platforms through digital advertising – an avenue that captures value from the vast majority of users who do not pay directly for in-game content. While this business model has proven highly effective from an economic standpoint, it presents significant legal and policy challenges, particularly for tax authorities in market jurisdictions operating under frameworks designed for a pre-digital world.

Advertising revenue is a core income stream for mobile games and other digital applications, especially those built on a freemium model. Unlike in-app purchases or subscriptions, which require players to make a direct payment, advertising allows game developers to produce revenue by selling digital space within their game to advertisers with no cost to game players. This enables users to download and use the game application for free – which has a highly positive impact in increasing user base and the penetration of such app in any given market –, in exchange of watching pieces of advertising in various designs such as static images, short videos, banners, and even playable ads that allow users to try out mini interactive versions of other games or apps directly within the ad unit.

Advertising not only monetizes existing players but also fuels user growth across platforms. Game studios deploy performance marketing campaigns across channels (such as Google Ads, TikTok, Instagram, and other applications) to convert users at scale – a process commonly known as user acquisition. With the aid

¹ The video games market is expected to exceed US\$ 320 billion by 2026, while the radio, music, and podcast market worldwide revenue in 2025 is estimated at US\$ 124.83 billion, and cinema market global revenue in the same year is estimated at US\$ 86.10 billion according to STATISTA. (n.d.). *Radio, Music & Podcast – Worldwide*: Statista market forecast. Available at: <https://www.statista.com/outlook/amo/media/music-radio-podcasts/worldwide#analyst-opinion>. Access: May 20, 2025, and STATISTA. (n.d.). *Cinema – Worldwide*: Statista market forecast. Available at: <https://www.statista.com/outlook/amo/media/cinema/worldwide#analyst-opinion>. Access: May 20, 2025, and STATISTA. (n.d.). *Mobile Games – Worldwide*: Statista market forecast. Available at: <https://www.statista.com/outlook/amo/media/games/mobile-games/worldwide#analyst-opinion>. Access: May 20, 2025.

of attribution tools² and data analytics, developers track which ads lead to new installations or long-term engagement, enabling optimized marketing investment. Cross-downloads within game portfolios, retargeting lapsed users, and leveraging ad networks for similar audiences are strategies enhanced by the integration of advertising technologies. This user acquisition process typically occurs through intermediaries such as Google AdMob, Meta Audience Network, Unity Ads, AppLovin, and other ad networks that provide the infrastructure for programmatic advertising, user targeting, and real-time bidding³.

Taxing digital advertising in games challenges traditional international tax concepts in multiple ways. First, because of how technology companies are organized. While revenue is created by user engagement, it is often booked in low-tax jurisdictions where platforms or IP owners are resident. Second, due to the lack of physical presence in the online advertising context. The game studio, the advertiser, and even the ad network do not need to have a physical presence in a market jurisdiction to access its users and produce millions in revenue there, undermining the traditional notion of a permanent establishment (PE). Third, as a result of platform intermediation, advertising revenue is typically routed through tech giants, which serve as both marketplaces and data intermediaries. These additional layers of separation between advertisers, developers, and end-users complicate the identification of where value is created and should be taxed. Last, because user data is an important source of value, advertising profitability is largely driven by user data collected through gameplay, in-app behavior, and demographic tracking. While this data is harvested in source countries, its economic exploitation usually occurs elsewhere, raising concerns about the fair allocation of taxing rights. These dynamics are aggravated in mobile games, where monetization relies on short and frequent user interactions spread across millions of geographically dispersed players.

In response to the challenges described hereinbefore, countries have adopted a combination of unilateral measures, such as the various European Digital Services Taxes (such as the French Digital Services Tax and the Italian Web Tax), and multilateral efforts through the OECD Inclusive Framework, particularly Pillar One and Pillar Two. Among the unilateral measures, India's Equalization Levy employs a pioneering approach to tackling these challenges and serves as a case study for evaluating the taxation of advertising in mobile games and other digital applications producing revenue across jurisdictions. By enacting this mea-

² Attribution tools are technologies, usually provided as software development kits (SDKs) or cloud-based platforms, that help app developers, advertisers, and marketing professionals understand where their users come from and what campaigns or channels led to specific user actions, such as installs, purchases, or ad views.

³ ADMOB, Google. *Mobile ads: the key to monetizing gaming apps*. Available at: <https://admob.google.com/home/resources/monetize-mobile-game-with-ads/>. Access: May 20, 2025.

sure, India has anticipated many of the concerns addressed by the OECD project. It provides a mechanism to capture revenue from non-resident digital companies that derive substantial value from the country's colossal user base. According to estimates, India's internet user base will total 806 million in 2025⁴. However, this arrangement is not without challenges, including the risk of double taxation, legal uncertainty stemming from tax treaties, and the possibility of retaliatory trade measures.

The present study aims to provide a review of India's experience in implementing taxes on digital advertising and to assess the efficacy of this policy within the context of how value is created within mobile games. The following chapter will analyze the economics of advertising in mobile games, as it will delve into the role of advertisements in producing revenue. It will also examine how user data is important in determining where and how value is created. It will then discuss the tax challenges arising from this business model. The final chapter will examine the Indian Equalization Levy on digital advertising, with a special focus on the structure, application, and critiques of the model. Finally, it will address insights that can be gleaned from India's experience. This will be achieved by conducting an analysis of its efficiency in collecting tax revenue and its effectiveness in reaching the digital economy.

2. The economics of digital advertising in the mobile games context

Research indicates that the video gaming market (comprising mobile, console, and PC platforms) is projected to exceed US\$320 billion by 2026, with mobile games contributing approximately 75% of this estimate⁵. Free-to-play games (F2P games) provide players with access to a substantial portion of their functions and assets without paying, and only require payment for additional content (freemium model). This segment accounts for a minimum of 80% of the video gaming market⁶. F2P games, therefore, rely on alternative monetization strategies rather than user payment, with digital advertising being one of the most common models. PwC has estimated that mobile video advertisement alone is set to reach US\$139 billion in 2026⁷. This market is not only relevant but also expanding, as it is contingent upon user engagement (network effect) and the ability to manage

⁴ PETROSYAN, Ani. Countries with the highest number of internet users: 2025. *Statista*. Available at: <https://www.statista.com/statistics/262966/number-of-internet-users-in-selected-countries/>. Access: May 20, 2025.

⁵ PWC. *Fault lines and fractures: innovation and growth in a new competitive landscape*. Available at: <https://www.pwc.com/gx/en/industries/entertainment-media/outlook/downloads/pwc-outlook22-v4.pdf>. Access: May 23, 2025, p. 5-8.

⁶ RICHTER, Felix. Cashing in on free-to-play games. *Statista*. Available at: <https://www.statista.com/chart/20395/worldwide-revenue-generated-with-free-to-play-video-games/>. Access: May 23, 2025.

⁷ PWC. *Fault lines and fractures: innovation and growth in a new competitive landscape*, p. 5.

and process user data, which is increasing with technology such as generative artificial intelligence.

Digital game advertising had occasional applications in the 1980s, but became widespread after the 1990s. Some examples are Chupa Chups lollipops advertising in Zool, a video game published by Gremlin Graphics in 1992, and Adidas advertising in FIFA International Soccer Championship Edition, a video game published by EA Sports in 1993 (see Figure 1 below). Since then, a golden rule is that advertising is more efficient when it is directly linked to the game's content⁸, because it helps create deeper engagement with the brand through meaningful player interaction. This means that not any advertising is good advertising. It has to create empathy and engagement with the player, as ads should feel like they belong in the game universe. Like Adidas, a sports brand advertising in the FIFA game in the example hereinbelow.

Figure 1 – Chupa Chups and “Zool” adverggame (Gremlin Graphics, 1992), and Adidas sponsorship in “FIFA International Soccer Championship Edition” (EA Sports, 1993).



Source: Adapted from HERREWIJN, 2015.

When digital game advertising first appeared, pieces of advertising were hard-coded into the game, resulting in static ads that could never be changed or updated once the game was released. However, by 2004, the internet and computing technology had made sufficient progress to reach the ability to dynamically embed advertisements in modern digital games. In this sense, ads do not have to be integrated into games in the form of a static and unchanging image anymore, but can be delivered and updated in-game based on multiple criteria, such as

⁸ HERREWIJN, Laura. *The effectiveness of in-game advertising: the role of ad format, game context and player involvement*. Universiteit Antwerpen, 2015. Available at: <https://www.academia.edu/12104122>. Access: May 23, 2025, p. 26.

players' socio-demographic information and gaming behavior⁹. This allows advertising to be much more precise and efficient in acquiring new users.

Digital advertising involves incorporating a variety of pieces of advertising (ad inventory) in digital spaces and displaying them to software users to increase brand awareness and drive purchase intentions. Moreover, digital ads are also relevant to producing revenue that is not directly linked to purchases. In other words, digital advertising is an independent and profitable business itself. For study purposes, digital advertising can be split into three main types: Around-Game Advertising (AGA), Advergames, and In-Game Advertising (IGA). Each type reflects a different level of brand integration into the gaming experience, and each has distinct strategic, legal, and tax implications.

2.1. Around-Game Advertising (AGA)

Going deeper into the modern types of game advertising listed above, Around-Game Advertising (AGA) is not directly integrated with the gameplay as it typically appears before progressing to a new game level, between rounds or matches when the game is downloading, or even around the game window (anchored on the top or bottom of the screen) during gameplay. Therefore, they do not always have a strict connection to the game's storytelling or its universe, as they are non-intrusive pieces of advertising around game displays, or licensing of game branding with associated third-party products that also do not intrude the gaming environment¹⁰. AGAs commonly appear as banners, interstitials, and rewarded ads (see Figure 2 below), which are usually hyperlinked to advertising websites promoting the product or service associated with the game, or to a platform or store (such as Google Play and Apple App Store) where the user can download that software or application. Interstitials are full-screen video elements also associated with supplementary web pages, which are displayed to the user while navigating from one page to another, like during load screens¹¹.

⁹ HERREWIJN, Laura. *The effectiveness of in-game advertising: the role of ad format, game context and player involvement*, p. 24.

¹⁰ SMITH, Martin W.; SUN, Wei. Game advertising: a systematic literature review. *Proceedings of the LCBR European Marketing Conference*. 2016, p. 2. Available at: https://www.researchgate.net/profile/Martin-Smith-22/publication/307014234_Game_Advertising_A_Systematic_Literature_Review/links/57c1547f08aed246b0fd0af3/Game-Advertising-A-Systematic-Literature-Review.pdf. Access: May 29, 2025.

¹¹ SMITH, Martin et. al. Game advertising: a conceptual framework and exploration of advertising prevalence. *The Computer Games Journal*. 2014, p. 100. Available at: https://www.researchgate.net/publication/264834353_Game_Advertising_A_Conceptual_Framework_and_Exploration_of_Advertising_Prevalence. Access: May 29, 2025.

Figure 2 – Types of Around-Game Advertising: Audible (Amazon) banner in “Angry Birds 2” (Rovio, 2015), Interstitial of “Clash of Clans” (Supercell, 2023), Rewarded advertising in “Candy Crush Saga” (King, 2012).



Source: Adapted from Rovio (2015), Supercell (2023), and King (2012).

AGAs are typically structured as an agreement wherein the publisher receives a fee based on the number of ad units (or pieces of advertisement) displayed or fully viewed. This fee is subject to variation according to the public segmentation, with advertisements refreshing automatically at optimized rates of user conversion. These conversion rates are calculated from historical data concerning user interaction. This suggests that Audible incurs a higher cost for Angry Birds to display the banner exemplified above (see Figure 2) for their adult players compared to children, given that Audible’s public and its marketing target are predominantly composed of adult users. In addition to age, other proxies may be pertinent to defining advertising pricing, including socio-demographic information such as the player’s geographical location, the hardware’s operating system (mobile, PC, videogame console, etc.), and gaming behavior, including expected lifetime spending and average daily time dedicated to the game.

Rewarded ads constitute an additional efficient type of AGA. These ad units take the form of video or interactive content, such as playables, which users can opt in to engage with in exchange for a reward within the game. The nature of the prize is subject to variation, ranging from additional time to play the game to power-ups and features exclusively available through in-app purchases¹². These prizes are often game assets that are useful or desirable, effectively compelling players to engage with the ad unit. For example, in Candy Crush Saga, a match-three game published by King in 2012, a player has the option to view an advertisement in exchange for an additional life and continue playing when they run out of lives (see Figure 2 above). Given its higher effectiveness in engaging and

¹² ADMOB, Google. *Mobile ads: the key to monetizing gaming apps*.

retaining users, rewarded ads pay a larger fee to game developers compared to other types of AGAs¹³.

2.2. *Advergames*

Advergames are downloadable or web-based games developed exclusively for the purpose of facilitating product placement. These games are designed to promote specific brands, products, services, or ideas, integrating them into an engaging and interactive gaming environment. Consequently, they function as a form of advertisement¹⁴. A compelling example of an adverggame is Crazy Taxi, a car race game first published by Sega in 1999. In this game, players encounter billboards and labels from various brands, including KFC, Pizza Hut, and Levi's, within different scenarios. Another notable example is Chester Cheetah: Too Cool to Fool, a side-scroller game (a Super Mario-style game) that features Elma Chip's Cheetah as its protagonist.

Adverggames are distinct from other forms of advertising due to their exclusive marketing objective: to create an immersive brand experience. Consequently, adverggames are typically characterized by their cost-free nature, ease of access, brevity, and swift delivery of rewards. Thus, adverggames are often developed under a software development agreement (a service agreement) between a brand and a software developer. This agreement enables the brand to exercise a high degree of control over the product, with game revenue being of lesser importance than brand awareness.

2.3. *In-Game Advertising (IGA)*

A third type of game advertising is In-Game Advertising (IGA), a more sophisticated form that is intimately connected to gameplay and storytelling. IGAs encompass customization and character modifications, including but not limited to branded skins (outfits or different layouts or designs for a given character or a game asset), branded characters, costumes, and character modifications that players can use to personalize their gaming experience.

The prevalence of branded characters, or digital clones of actual sportspeople, is increasing as brands can enter into contractual agreements with game developers and receive a percentage of sales generated by these digital assets. However, the scope of use can be more extensive. For instance, the Iron Man skin, which was made available in Fortnite, a video game published by Epic Games in 2017, is a prime example, as it took advantage of Marvel's Iron Man movie to in-

¹³ In June, 2025, Unity, one of the largest ad networks in the globe, paid an average US\$ 10 to US\$ 50 for every 1,000 impressions of a rewarded video app. Available at: <https://developers.is.com/ironsource-mobile/general/rewarded-video/#step-1>. Access: June 2, 2025.

¹⁴ HERREWIJN, Laura. *The effectiveness of in-game advertising: the role of ad format, game context and player involvement*, p. 4.

crease monetization. Another notable instance is the online show by DJ Marshmello in 2019, where the artist performed a virtual show for more than 200,000 online players who were virtually present and interacted with the artist and other users through their avatars. This led to a 1,800% increase in DJ Marshmello's YouTube following count¹⁵. This substantial increase in brand awareness underscores the significant impact of such strategies. These elements enable users to express themselves while engaging with brand content, thereby fostering high user engagement and consequently generating a higher return on investment.

Product placements also represent a prevalent form of in-game advertising, wherein brands meticulously position paid products to influence audiences through strategic integration¹⁶. In the gaming industry, products are deliberately interwoven with the narrative to persuade players and leverage product, brand, or game hype to enhance user conversion and return on sales. These elements are very ubiquitous in the form of in-game vehicles, branded clothing and apparel, food and beverages, and music and sounds. In the context of IGA, a final category of game advertising encompasses brand-related cheat codes and Easter eggs that unlock hidden content such as special game assets, new abilities, or exclusive game content. In *Nascar 2005: Chase for the Cup*, a car race game published by Electronic Arts in 2005, featured several branded cheat codes that unlocked exclusive branded race tracks and race cars when players typed in codes such as "race dodge" or "oldspice venue"¹⁷.

3. How mobile games make money with digital advertising?

The revenue yielded from advertisement is contingent upon two factors: the genre of the application in which it is presented and the advertisement unit employed. The financial transactions involving the digital space licensed to advertising entities are determined by either impressions, defined as the number of times an advertisement is displayed, or by installs, representing the number of downloads originating from that ad unit¹⁸.

Digital advertising, much like the stock market, involves negotiations between demand-side platforms (representing advertisers who bid for ad impres-

¹⁵ BEIN, Kat. *Marshmello's Fortnite Concert: breaking down the social impact*. Billboard, June 02, 2019. Available at: <https://www.billboard.com/music/music-news/marshmello-fornite-concert-social-impact-8496868/>. Access: May 25, 2025.

¹⁶ LÓPEZ, Javier de la Vara; MARCHIS, Giorgio P. de. Redefining in-game advertising: a systematic literature review and an updated definition. *Revista de Comunicación* v. 23, n. 2, 2024, p. 35-52. Available at: http://www.scielo.org.pe/scielo.php?pid=S1684-09332024000200035&script=sci_arttext&tlng=es. Access: May 26, 2025.

¹⁷ HERREWIJN, Laura. *The effectiveness of in-game advertising: the role of ad format, game context and player involvement*, p. 35.

¹⁸ NIEBORG, David B. Free-to-play games and app advertising: the rise of the player commodity. *Explorations in critical studies of advertising*. Routledge, 2016, p. 38-51. Available at: <https://www.academia.edu/download/50835384>. Access: May 23, 2025, p. 3.

sions) and supply-side platforms (operating for ad publishers that offer access to their ad inventory, which is the space available to display ad impressions). These platforms work in real-time biddings (RTB), where programmatic buying technology meticulously assesses the prevailing prices and the quality of the digital space that is available (users, leads, etc.) and then balances it with the ad inventory to ascertain the optimal return on investment. Consequently, RTB advanced behavioral targeting by submitting billions of simultaneous bids on individual advertisements. This transition represents a shift from probabilistic models to deterministic ones, with a concomitant transition from delivering impressions to prompting specific actions from users. In this paradigm, the collection, storage, analysis, and disclosure of data assume pivotal roles¹⁹.

Simpler advertisements, such as banners, are generally priced on a cost-per-mille (CPM) basis, while interactive formats may be priced on a cost-per-click (CPC) or cost-per-install (CPI). These pricing models reflect different levels of user interaction and are relevant for tax purposes because they indicate how closely advertising revenue is connected to user engagement and conversion. In addition to the ad format (AGA, Advergames, and IGA as described above), the price of advertising can also be influenced by the type of platform, the users' socio-geographic characteristics, and user behavior. It is evident that mobile platforms generally have rates different from consoles and PC, but even among mobile applications, CPM can vary depending on the operating system, following the advertisers' preferences²⁰.

User location also affects advertising prices because it operates as a proxy for purchasing power, conversion probability, language, and cultural relevance. For tax purposes, this reinforces the importance of revenue sourcing rules and user-based allocation keys in digital advertising markets. In the same sense, user behavior data affects pricing because it allows ad networks and advertisers to segment players according to engagement and conversion probability. The more an ad format depends on behavioral targeting and user interaction, the stronger the connection between advertising revenue and local user-generated value. Modern games can track granular in-game behavior, including movements, purchases, session duration, and interactions with advertising units. This technical capacity matters for tax purposes because it turns local user activity into monetizable data used to improve ad targeting and pricing.

¹⁹ NIEBORG, David B. Free-to-play games and app advertising: the rise of the player commodity. *Explorations in critical studies of advertising*. Routledge, 2016, p. 4.

²⁰ Recent researches show that between 2020 and 2021, CPM for rewarded video ads was slightly higher (around 2%) for iOS (Apple's operational system) versus Android (Google's operational system), while interstitials and banner ads are generally more expensive for Android (around 15% and 122% respectively). See more at KNEZOVIC, Andrea. *ECPMs for rewarded video, interstitial & banner ads*. Udonis. Available at: <https://www.blog.udonis.co/mobile-marketing/mobile-apps/ecpms>. Access: June 3, 2025.

3.1. Tax challenges arising from this business model

Mobile advertising poses challenges that are analogous to those presented by other digital businesses, such as the scale without physical presence and the heavy reliance on intangible assets²¹. However, it is relevant to acknowledge the unique challenges arising from the intricacies of the gaming market, particularly with regard to the generation and utilization of the value derived from data and user participation. The nexus challenge is of particular interest in this context. The traditional tax rules that rely on physical presence are not applicable to mobile advertising and other digital services that can reach users with no local infrastructure.

As previously discussed, mobile advertising occurs through real-time bidding, performed by automated digital services within the framework of an ad network, and none of these operators needs physical presence in a given market to have access to their users and infrastructure²². Conversely, the operation is conducted through cloud-based platforms and applications, with numerous layers of separation between the game player (end user, customer) and the companies that monetize their data, engagement, and attention. The initial challenge is to ascertain how market jurisdictions can effectively enforce taxation on mobile advertising. Given that these activities primarily occur outside their jurisdiction they, therefore, lack control or access to profits, money remittances, and relevant information deriving from these transactions to properly assess and enforce tax charges.

Considering the debate hereinbefore, it is evident that user data and engagement, and interaction are pivotal for ad monetization. Consequently, companies deliver in-game and around-game advertisements that achieve user attention, enhance brand recognition, and influence purchasing decisions, with these advertisements being meticulously customized and targeted to local players. So, unquestionably, a significant economic presence exists, even in the absence of physical operations.

Another challenge lies in understanding how and where value is created in digital advertising. A thorough analysis of the business model reveals that the

²¹ OCDE. *Addressing the tax challenges of the digital economy: Action 1 – 2015 final report*. Available at: https://www.oecd.org/en/publications/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report_9789264241046-en.html.

²² A treaty-based alternative can be found in article 12B of the UN Model, which allows source taxation of automated digital services on a gross basis, subject to treaty negotiation. Báez Moreno's critique of article 12B is relevant because it highlights a recurring difficulty in digital tax design: the more a rule attempts to define a specific category of digital services, the more it creates boundary problems with adjacent categories, such as technical services, advertising services, data transmission, and platform intermediation. This concern also applies to mobile game advertising, where the same transaction may combine access to ad inventory, behavioral targeting, data analytics, software infrastructure, and user acquisition services. See: BÁEZ-MORENO, Andres. Because not always B comes after A: critical reflections on the new article 12B of the UN Model on automated digital services. *World tax journal*. Amsterdam., 2021, p. 501-532. Available at: <https://ssrn.com/abstract=4223012>. Access: June 7, 2026.

value generated from advertising is contingent on the user context, rather than merely displaying an ad unit. A nuanced understanding of player behavior is essential to producing such value and ad-related income. However, at the same time, the presence of a brand in a story-rich game does not guarantee measurable economic value for that brand. For example, many billboards pass unnoticed in high-involvement scenarios of a car race game. Value may arise when there is an effective association of the brand with the game and the player (not just cognitive attention). This makes it more difficult to define and measure value creation for purposes of profit attribution or nexus definition. So the second challenge is: how to differentiate and measure the value created by different types of advertising? Is there a one-size-fits-all solution for taxing digital ad revenue, or should it balance how much value is created by the user, who produces data to improve ad targeting? Or even, would user engagement and interaction produce no or less value for ads that are not negotiated in RTB or placed in styles that are less sensitive to user data, such as AGAs?

Finally, a third challenge pertains to profit attribution, which involves balancing the value created across the value chain and allocating taxable income to participating jurisdictions according to the value produced. This undertaking is particularly challenging, as it requires the delineation of player interactions that engender quantifiable advertising impact and the discernment of how factors such as narrative, game environment (e.g., controller type, co-play vs. single-play, etc.), and other user-related variables influence ad visibility, engagement, and effectiveness. This is critical for estimating how much economic value was created by ads shown to users in a specific location or under specific conditions. To illustrate this point, consider the following example: if advertisements in multiplayer games in Brazil were found to elicit a heightened emotional response and enhance brand preference among consumers, would this substantiate the allocation of a greater proportion of profits to Brazil under formulary apportionment or user-based allocation keys (as delineated in OECD Pillar 1)? Or even, how much value is derived from the ability of ad networks, game studios, and platforms to collect, store, and analyze user data for advertising purposes?

In an effort to address this challenge, various jurisdictions and organizations worldwide have proposed solutions to tax digital advertising. In the next chapter, an analysis will be conducted on one of these proposals, namely, the Equalization Levy introduced by India, with a subsequent review of the effectiveness of this proposal for the taxation of advertising in mobile games.

4. The Indian tax policy regarding digital advertising

4.1. Motivation and overview

In response to the challenges described above, market jurisdictions have proposed a variety of alternatives for taxing the digital economy. These alterna-

tives include joining a multilateral arrangement such as the OECD Pillar One, or proposing unilateral frameworks, including the various models of Digital Services Taxes (DSTs) and Equalization Levies. India represents a unique case study for taxing digital revenue, particularly for digital advertising. With a vast and growing mobile user base, India creates significant value for global gaming platforms. However, this value rarely corresponds with tax collections in India, as most of these platforms are not based in the country.

With nearly one billion mobile users²³, India represents a substantial market with considerable potential, drawing the attention of major mobile platforms and gaming companies. In this regard, the mobile game turnover in India is expected to be US\$405 million in 2025, and the number of game players is projected to reach 270 million by 2030²⁴. The tricky aspect is that most of the platforms exploring Indian users, either game developers or ad networks, are not based in India but rather in the US, Europe, and other regions like Singapore and Israel²⁵. Consequently, the revenue generated by digital advertisements displayed in India, which is significantly increased by the processing and commercialization of Indian users' data, will hardly be captured by the local income tax or other taxes on sales.

Prior to 2016, India faced significant challenges in taxing digital advertising revenue, particularly concerning payments made to foreign technology companies. The primary issue under consideration was whether the payments in question could be tipified as royalties, thereby becoming subject to taxation under Indian law and relevant tax treaties, particularly Article 12 of the OECD Model Convention. The situation was further complicated by prolonged disputes involving major technology companies such as Google and Yahoo, which led to inconsistent Court interpretations and challenges in tax administration.

A landmark case in this context was the Yahoo case (ITA No. 6181/Mum/2011)²⁶, which involved payments made by Yahoo India to Yahoo Holdings (Hong Kong) for online advertisement services. In this case, the Department of Tourism of India had hired Yahoo India's services for uploading, displaying, and

²³ PETROSYAN, Ani. *Countries with the highest number of internet users*: 2025.

²⁴ STATISTA. (n.d.). *Mobile games*: India. Available at: <https://www.statista.com/outlook/amo/media/games/mobile-games/india#analyst-opinion>. Access: June 18, 2025.

²⁵ In January 2025, none of the top ten gaming app publishers in Google Play was based in India. They were based in the US (Scopely and Roblox), Singapore (Funfly, Century Games, and Cognosphere), Turkey (Dream Games), Ireland (Playrix), Israel (Moon Active), Sweden (King), and Finland (Supercell). See more in CLEMENT, Jessica. *Leading Android Gaming App Publishers Worldwide 2025*, by Revenue. *Statista*. Available at: <https://www.statista.com/statistics/692559/leading-mobile-games-publishers-google-play-world-revenue/>. Access: June 18, 2025.

²⁶ Available at: <https://indiankanoon.org/doc/61437390/>. Access: June 20, 2025. Other relevant cases are Right Florist Pvt. Ltd (2013), available at: <https://indiankanoon.org/doc/98785989/>, and Pinstorm Technologies Pvt. Ltd. (2015), available at: <https://indiankanoon.org/doc/131633874/>.

hosting banner advertisements on the Yahoo portal operated by Yahoo Hong Kong. Yahoo India acted as an intermediary, receiving payment from the Department of Tourism and remitting the balance to Yahoo Hong Kong after retaining its margin. The Court ruled in favor of Yahoo, holding that banner advertisement hosting services did not involve the use or right to use any industrial, commercial, or scientific property, and therefore the payments could not be qualified as royalties. As a conclusion, the income was classified according to Article 7 of the Tax Convention and taxed as business profits, which are due to the residence country (Hong Kong) unless a permanent establishment exists in the source state, which was not the case.

In contrast, the Google case (ITA No. 1190/Bang/2014)²⁷ presented a more complex scenario, wherein Google India made payments to Google Limited under the Google AdWords Program Distribution Agreement²⁸. The tax administration initially characterized these payments as royalties, arguing that they involved the use of Google's intellectual property and software. However, the Court ultimately ruled that the payments for online advertisement space could not be characterized as royalties under the India-Ireland Double Tax Agreement. This ruling was particularly significant as it aligned with previous rulings in cases like Yahoo India and emphasized that distribution rights for online advertising should not be classified as intellectual property rights.

The contrasting outcomes of these cases underscore the difficulties in applying conventional tax principles to digital business models. The results of both cases culminated in decisions that were favorable to the taxpayers: payments in compensation for digital advertising are not subject to withholding tax from India, as they are typified as business profits rather than royalties. However, they followed different reasoning paths and caused opposing effects on taxpayers in preliminary decisions. For the Indian Courts, these cases shed light on the inefficiency of traditional statutory approaches to taxing digital services.

4.2. A new nexus based on a significant economic presence and the Equalization Levy on digital advertising

Contemporaneously with the case law described above, the OECD published its Final Report on Action 1 (the 2015 Report), which provided guidance on how the challenges of the digital economy should be addressed. Key recommendations were a new nexus based on significant economic presence, the enforcement of withholding tax on digital transactions, and the imposition of equalization

²⁷ Available at: <https://indiankanoon.org/doc/43943938/>. Access: June 20, 2025.

²⁸ Google AdWords, also now known as Google Ads, is a digital advertising platform that allows businesses to promote their products and services on Google's search engine results pages and other websites and apps within the Google network. It enables businesses to reach a target audience by bidding on keywords and displaying ads to users searching for relevant terms.

levies to equal treatment between foreign and domestic suppliers. As a member state of the OECD, India has also implemented an internal Committee on Taxation of e-Commerce (the Committee) that addressed the challenges faced by its Courts and the recommendations provided by the OECD to tax the digital economy. The purpose of the Committee was to draft a proposal that was adequate to India's internal and international tax framework, which resulted in the 2016 Proposal for Equalization Levy on Specified Transactions.

The first recommendation of the OECD Report acknowledges that the traditional permanent establishment concept is not sufficient to deal with the business arrangements of the digital economy, as evidenced in the previous chapter in the context of digital gaming and advertising. The Report thus discusses the possibility of introducing a new nexus approach based on a significant economic presence (SEP) in the market state of the non-resident corporation. In this regard, the company's economic presence can be ascertained through digital factors such as localized digital platforms, local payment options, and customer accounts, or user-based factors associated with data collection and user interactions²⁹. This assertion holds particular relevance in the context of advertising within mobile games, wherein the value of the ad is predominantly determined by the efficacy with which user data is collected and processed, as evidenced previously.

The concept of SEP was introduced in India by the 2018 Finance Bill, which modified the 1961 Indian Income Tax Act so that a SEP would build a nexus of the foreign company in India and trigger taxation. According to the Indian Bill³⁰, there would be a SEP when a non-resident carries out transactions involving goods, services, or property in India over a threshold (INR 20 million, approximately US\$ 250,000.00), including downloading data or software. There would also be a SEP when a non-resident systematically and continuously solicits business activities or interacts with a prescribed number of users (at least 300 thousand) in India through digital means – treaty countries would have a privileged regime³¹.

So with this innovation, profits attributed to these transactions would be taxed in India. Considering that the most value in digital advertising is created via user interaction, the concept of SEP could capture the value created by exploring user data in India. However, the administration challenges associated with monitoring foreign companies and with processing and auditing tax returns could jeopardize its application on a large scale for developing countries. Moreover, although SEP has been incorporated into the Indian Income Tax Act, its

²⁹ OCDE. *Addressing the tax challenges of the digital economy: Action 1 – 2015 final report*, p. 111.

³⁰ GOVERNMENT OF INDIA. *The Finance Bill*, 2018. Chapter 3, Section 9, Subsection 1, Explanation 2A. Available at: https://dea.gov.in/sites/default/files/frbm_amendment_acts_2018_1.pdf.

³¹ HORTA, Nereida de Miranda Finamore. *Tributação da economia digital na Índia e no Brasil: proximidades, diferenças e oportunidades*. São Paulo: IBDT, 2024, p. 112-113.

practical application continues to be largely dormant due to treaty override. Most Indian tax treaties are based on OECD or UN Model Conventions and require a physical presence for business profits to be taxed in the source state, and under Section 90(2) of the Indian Income Tax Act, the provisions of the treaty override domestic law if they are more beneficial to the taxpayer. Therefore, unless treaties are renegotiated to review Article 5 to include the SEP approach, non-residents can rely on the PE definition in the treaty, rendering SEP ineffective³².

The second recommendation, withholding tax on digital transactions, was deemed feasible by the Indian Committee on the condition that it be incorporated into tax treaties. However, by 2016, India had approximately 100 double tax agreements in force, which would make it impossible to ensure a systematic and consistent application, and a minimum level of policy effectiveness, therefore this option was abandoned. However, the third recommendation, which pertains to the implementation of an equalization levy to ensure fair treatment between foreign and domestic suppliers, garnered substantial support from the Committee. The Committee acknowledged that the Equalization Levy (EL) could be implemented under domestic laws, without violating the tax treaty obligations, as it would not be imposed on income, but on the gross amount of transactions³³. The Committee further reasoned that the EL provides greater clarity and predictability regarding the characterization of payments for digital transactions, and that it could be imposed as an interim measure until international taxation rules are modified³⁴.

The Indian choice to adopt an Equalization Levy rather than a treaty-based withholding tax can be better understood against the broader academic debate on withholding taxes as a response to BEPS Action 1. Báez Moreno and Brauner argue that withholding mechanisms may serve either as a primary response to digital economy taxation or as an ancillary enforcement device supporting a new nexus rule³⁵. India's model reflects this logic only partially: it avoids the treaty obstacles of a traditional income-tax withholding system by designing the levy as

³² A similar concept was introduced by the Delhi High Court in a civil case – Case World Wrestling Entertainment, Inc. vs. M/S Reshma Collection & Ors on 15 October, 2014, FAO(OS) 506/2013 & CM Nos. 17627/2013, 18606/2013. The Court decided that transactions carried out in a website are equivalent to the ones performed by a salesperson at a physical store for its civil implications.

³³ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. 2016. Available at: <http://incometaxindia.gov.in/news/report-of-committee-on-taxation-of-e-commerce-feb-2016.pdf>. Section 129.

³⁴ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. 2016. Section 125.

³⁵ BRAUNER, Yariv; BÁEZ-MORENO, Andres. Withholding taxes in the service of BEPS Action 1: address the tax challenges of the digital economy (February 2, 2015). *WU International Taxation Research Paper Series* No. 2015 – 14. Available at: <https://ssrn.com/abstract=2591830>. Access: June 7, 2026, p. 6.

a separate gross-basis charge, but it preserves the administrative appeal of collecting tax at the payment level through the resident payer.

Hence, following the Committee's recommendation, India's Equalization Levy was introduced in 2016³⁶ as a targeted measure to address tax challenges arising from the digital economy. At its core, the levy imposes a 6% tax on gross payments made by Indian businesses to non-resident enterprises for online advertising and related services. The tax specifically applies to payments for online advertising, licensing of digital advertising space, and any other facility or service related to online advertising.

The levy is imposed on business-to-business (B2B) transactions where the payment is made by an Indian resident business or a permanent establishment of a non-resident in India to a non-resident enterprise for specific digital services. Conversely, if the non-resident service provider has a permanent establishment in India and the services are effectively connected to such PE, the levy does not apply. This structure ensures that the levy targets only those foreign digital businesses that operate in India without establishing a traditional taxable presence.

In terms of its nature, the Equalization Levy was deliberately structured as a distinct tax, independent of the income tax. This tax is imposed on the gross amount of transactions rather than on income, distinguishing it from income tax, tax on income, or any identical or substantially similar tax³⁷. This classification is of paramount importance because it ensures that the levy remains outside the scope typically covered by double taxation avoidance agreements.

The levy is also subject to specific payment thresholds and statutory requirements. A *de minimis* rule establishes that the aggregate consideration for services between each service provider and recipient must exceed INR 100,000.00 (approximately US\$ 1,500.00) in a year for the levy to apply. This is an important aspect of the EL as the low threshold ensures equal treatment across large multinational groups and smaller offshore enterprises doing business in India with no physical presence. Therefore, what is being equalized is not the treatment of digital companies versus their brick-and-mortar rivals, but the treatment of resident taxpayers and those with PEs versus nonresidents that lack a PE in India³⁸. The administration and governance implications of this legislative choice will be discussed later in this chapter.

The tax collection mechanism operates through a withholding system, whereby the Indian business payer is responsible for deducting the levy from pay-

³⁶ GOVERNMENT OF INDIA. *The Finance Bill*, 2016. Chapter VIII, Section 160-177. Available at: <https://www.indiabudget.gov.in/budget2016-2017/ub2016-17/fb/bill.pdf>.

³⁷ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. Section 127.

³⁸ GOULDER, Robert. India reinvents its Equalization Levy. *Tax Notes International*, [S.l.], v. 99, n. 13, jul. 2020. Available at: <http://www.taxnotes.com/lr/resolve/tax-notes-international/india-reinvents-its-equalization-levy/2cpt1>. Access: May 12, 2025.

ments made to non-resident service providers. The withholding obligation is a requirement for businesses seeking to claim the payment as a deductible expense in determining their taxable profits in India. This linking of deductibility with levy compliance serves as an effective enforcement mechanism.

In order to circumvent the possibility of double taxation within the Indian tax system, any income arising from transactions subject to the equalization levy is exempt from income tax under the Indian Income Tax Act. This exemption ensures that the same transaction is not taxed twice under different provisions of Indian tax law. However, it does not preclude the possibility of double taxation at the international level.

The EL's implementation framework includes specific reporting and compliance requirements. Businesses must maintain proper records of transactions subject to the levy, and those required to have their accounts audited must obtain an auditor's certificate regarding the equalization levy compliance. However, smaller businesses, not required to maintain books of accounts or have their accounts audited, are exempted from these additional compliance requirements³⁹.

In contrast to the significant economic presence alternative, the equalization levy could be implemented unilaterally without requiring treaty modifications. The rationale underlying this phenomenon is that the EL is not codified within the framework of income tax legislation, thereby obviating the necessity for harmonization with the extensive and complex Indian international tax framework. This approach enabled India to swiftly address the challenges associated with taxation in the digital economy while circumventing the intricacies of treaty renegotiations.

In fact, the relationship between the equalization levy and the concept of significant economic presence is complementary rather than harmonized. While both aim to address digital economy taxation, they operate independently. The equalization levy provides immediate tax revenue from digital transactions, while significant economic presence serves as a longer-term framework for establishing taxable nexus in the digital economy.

After all, the equalization levy represents India's response to the BEPS Action 1 recommendations, and was designed as an interim measure that could be modified or replaced once international taxation rules are updated to address digital economy challenges more comprehensively⁴⁰. Its structural design enables adaptability in response to evolving circumstances, a topic that will be further elaborated upon in the subsequent sections of this chapter.

³⁹ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. Section 163.

⁴⁰ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. Section 125.

4.3. Critiques of The Equalization Levy and its effectiveness in taxing digital advertising in the mobile games context

A critical assessment of the Equalization Levy must be grounded in the fundamental principles of sound tax policy, namely neutrality, efficiency, simplicity, equity, and administrability. From a neutrality standpoint, the EL distorts market dynamics by applying only to non-resident suppliers of digital services, potentially favoring domestic competitors and undermining competition. In terms of efficiency, while the levy seeks to correct mismatches between value creation and taxation, its flat rate and broad scope may lead to economic deviations. The design also raises concerns about simplicity and administrability, as the lack of clear definitions and the low application threshold create high compliance burdens for taxpayers and enforcement challenges for tax authorities. Finally, regarding equity, the EL does not adequately account for the varying degrees of user engagement and data-driven value creation, thereby applying the same rate to fundamentally different economic contributions. These aspects will be more deeply analyzed as follows.

The Equalization Levy has been the subject of considerable criticism regarding its efficiency in revenue collection relative to the compliance burden it imposes on businesses. Despite the absence of explicit data regarding tax revenue derived from the levy within the Indian Finance Bills and its Annual Financial Statements, pronouncements of the Indian Minister of State for Commerce and Industry estimate a sum of around US\$1.7 billion between 2016 and 2025⁴¹. This is a modest amount considering the disproportionate administrative cost imposed on the tax authorities and the taxpayers, particularly the foreign companies that must navigate India's complex tax system.

Although the precise cost of administration of the Equalization Levy is also not publicly available, the low threshold of the levy (approximately US\$ 1,500) means that it captures numerous smaller transactions, creating blanket coverage that may not be cost-effective from an administrative perspective. In this sense, the tax administration is required to oversee a significant number of transactions and to audit an increasing number of companies operating digital advertising either on the demand side (game studios or other digital applications licensing

⁴¹ While gross tax revenue collected by the Indian Government in 2023-2024 was 3.5 million crore (around US\$ 420 billion), estimated tax revenue derived from the Equalization Levy for 2016 to 2021 is estimated at 4,496 crore (approximately US\$ 540,000, and 9,800 crore (roughly US\$ 1.2 billion). See: SUNEJA, Kirtika. Rs 1,492 cr worth equalisation levy collected in last 10 months: Govt to Parliament. *The Economic Times*. February 12, 2021. Available at: <https://economictimes.indiatimes.com/news/economy/finance/govt-collects-rs-1492-crore-equalisation-levy-between-apr-2020-jan-2021/articleshow/80879675.cms?> Accessed on June 24, 2025. And KHAN, M. Zakariya. India to scrap 6% equalisation levy on digital ads, leading to revenue loss. *Business Standard*. Available at: https://www.business-standard.com/industry/news/india-equalisation-levy-removed-tax-impact-2025-125040100810_1.html? Accessed on June 24, 2025.

their digital space for advertising) or the supply side (ad networks and other companies providing their ad inventory).

In this context, the Indian policy choice between significant economic presence, withholding taxes, and equalization levies should not be assessed only by reference to revenue potential, but also by administrability, treaty compatibility, and the capacity to approximate the location of value creation. Báez Moreno and Brauner's comparative analysis is useful because it shows that gross-basis instruments may be attractive precisely when traditional profit attribution is impracticable⁴². However, the Indian Equalization Levy also reveals the limits of this approach: a gross-basis charge may be administratively simpler, but if designed with a very low threshold and a broad scope, it may generate disproportionate compliance costs while still failing to capture offshore-to-offshore transactions targeting local users.

By contrast, the European Digital Services Taxes (DSTs) have a significant structural difference as they specifically target large digital businesses. France, for instance, has enacted a 3% DST on digital advertising revenue for companies with worldwide revenues exceeding EUR 750 million, and EU-sourced revenues exceeding EUR 25 million. They also differ in scope, while the EL targets specific digital services like advertising and e-commerce, the DST applies to multiple digital services. The French DST, for example, targets advertising services based on users' data, the provision of a digital interface, and streaming. Additionally, the vastly different thresholds reflect diverse policy objectives – while the EU explicitly targeted large tech companies, India's approach was more broadly applicable to all non-resident digital service providers. The DST approach seems to be smarter as it reduces compliance and administration efforts while capturing the largest portion of the tax revenue concentrated in the largest taxpayers. In this respect, Mason's comparative analysis of digital tax litigation in the United States and Europe suggests that the legal sustainability of a digital advertising tax depends heavily on its design. Taxes that apply only to very large companies or to narrow digital revenue streams may be vulnerable to claims of discrimination, particularly when they disproportionately burden foreign or out-of-state businesses⁴³.

Furthermore, the rushed legislative process carried out by India while enforcing the EL in 2016 resulted in practical compliance challenges, as detailed regulations and guidance were not available when the levy took effect. Companies faced immediate deadlines without adequate time to obtain necessary local

⁴² BÁEZ-MORENO, Andrés; BRAUNER, Yariv. *Policy options regarding tax challenges of the digitalized economy: making a case for withholding taxes*. Available at: <https://ssrn.com/abstract=3167124>. Access: June 7, 2026.

⁴³ MASON, Ruth. *Legal problems with digital taxes in the United States and Europe*. 2023. Available at: <https://ssrn.com/abstract=4346279>. Access: June 7, 2026, p. 17-18.

tax registration numbers or clearly understand their obligations. They also had to comply with tax payments by the last day of the same reference month, which creates impossible compliance scenarios as online operations happen twenty-four-seven. In this regard, the equalization levy has also been criticized for creating significant legal uncertainty due to ambiguous language and unclear implementation. Numerous ambiguities have been identified, including the scope of taxable services, the universe of liable companies, the applicability to intra-group transactions, and proper calculation methods⁴⁴.

Other critics of this framework, like the US government⁴⁵, argue that the levy undermines investment neutrality and creates distortions in international trade. Grounded in the fact that the levy explicitly exempts Indian companies while targeting non-resident firms, the US argues it would create an uneven playing field that violates fundamental principles of trade neutrality⁴⁶. Additionally, the broad definition of nexus based merely on IP addresses or customer location creates enforcement challenges and jurisdictional conflicts, particularly given how easy digital presence can be manipulated through VPNs and proxy servers. In this sense, the levy's extraterritorial application entails companies facing taxation even without a permanent establishment in India, contradicting international norms that typically require a territorial nexus for corporate taxation (the traditional PE concept established as reflected in OECD and UN model conventions). This additional tax burden can ultimately discourage foreign investment and create barriers to international trade.

In the same sense, there is an interpretation that the EL is discriminatory because it targets digital services while exempting similar non-digital services. This could lead to a ring-fencing approach that has been repeatedly criticized by

⁴⁴ GOVIND, Sriram. Unilateralism in taxing the digitalized economy: comparing the EU digital services tax proposal and the Indian Equalization Levy. In: PISTONE, Pasquale (ed.). *Taxing the digital economy: the EU proposals and other insights*. IBFD, 2019, p. 4-5.

⁴⁵ The US trade authority published in January 2021 the Report on India's Digital Services Tax analyzing whether the Equalization Levy is discriminatory, consistent to international tax principles, and burdensome or restrictive to the US commerce. See more in OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE. Report on India's digital services tax: Section 301 Investigation. January 6, 2021. Available at: <https://ustr.gov/sites/default/files/enforcement/301Investigations/Report%20on%20India%E2%80%99s%20Digital%20Services%20Tax.pdf>. Access: June 25, 2025.

⁴⁶ In this regard, the controversy surrounding digital services taxes also has a geopolitical dimension. As Mason observes, digital taxes have often operated as a proxy for broader disputes over the taxation of large U.S.-based technology companies. This helps explain why measures such as India's Equalization Levy cannot be assessed only as domestic tax instruments: they also interact with trade policy, treaty negotiations, and the political economy of allocating taxing rights between residence and market jurisdictions. See: MASON, Ruth. *Legal problems with digital taxes in the United States and Europe*. 2023. Available at: <https://ssrn.com/abstract=4346279>. Access: June 7, 2026.

the OECD⁴⁷. Therefore, under the traditional approach existing in the international tax framework, it could negatively affect companies from countries that lead in digital services, creating trade distortions that favor traditional business models over innovative digital approaches. Although this argument is valid, digital advertising and traditional advertising services are not exactly comparable, as they have very different purposes and operations. Digital ads has a strong dependency on user data and online infrastructure, which is not compatible with advertising published in a newspaper or a magazine.

Regarding EL's potential to unlevel the international trade, critics note that payers and beneficial owners, particularly when they are associated enterprises, can potentially avoid the levy by relabeling payments to fall outside the specified categories. Therefore, the equalization levy's structure can create perverse incentives for tax avoidance and artificial restructuring of business arrangements.

Another common criticism of the EL, also acknowledged by the Indian Committee on Taxation of e-Commerce, is its potential to create double taxation without treaty protection. Since the levy is structured outside India's Income Tax Act and explicitly designed to fall outside tax treaty coverage, companies paying the levy cannot claim foreign tax credits in their residence jurisdictions. This creates a scenario where the same income may be subject to both the equalization levy in India and corporate income tax in the company's residence country⁴⁸. In this sense, the US investigation also found that companies could face not just double but potentially multiple taxation when subsidiaries in multiple jurisdictions with digital service taxes are involved⁴⁹. This would violate the fundamental principle of avoiding double taxation that underlies the international tax system, as reflected in numerous bilateral tax treaties and OECD model conventions, the so-called "single tax principle".

While all these arguments are valid, the equalization levy is not unique in this respect. The European DSTs were also designed to fall outside the scope of income tax and, therefore, outside existing tax treaties. This was achieved by structuring them as transaction-based taxes rather than income taxes, allowing jurisdictions to implement these measures unilaterally without needing to renegotiate their existing tax treaties. So, although these measures can create double taxation, both the EL and the DST were conceived as interim solutions while

⁴⁷ The OECD states that because the digital economy is increasingly becoming the economy itself it would be difficult, if not impossible, to ring-fence it from the rest of the economy for tax purposes, and that attempting to do so would require arbitrary lines between what is digital and what is not. See: OECD. *Addressing the tax challenges of the digital economy: Action 1 – 2015 final report*. Paris: OECD Publishing, 2015, p. 12 and p. 54-55.

⁴⁸ COMMITTEE ON TAXATION OF E-COMMERCE. *Proposal for Equalization Levy on specified transactions*. Section 10.16.

⁴⁹ OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE. *Report on India's digital services tax*: Section 301 Investigation, p. 27.

awaiting (or pushing) for more comprehensive international consensus on digital economy taxation.

On the other hand, the Indian EL deviates from the principles underlying Pillar One, particularly regarding nexus concepts and profit allocation methodologies. Under the OECD/G20 Inclusive Framework's Pillar One Blueprint, Amount A was designed as a new taxing right for market jurisdictions, operating independently from the traditional permanent establishment threshold and reallocating a portion of residual profits of large multinational groups by reference to market-based revenue sourcing rules. Pillar One seeks to reallocate taxing rights to market jurisdictions based on a comprehensive framework involving Amount A (a portion of residual profits allocated to market jurisdictions) and Amount B (a simplified approach for baseline marketing and distribution activities). The nexus concepts underlying each approach reveal fundamental philosophical differences about digital taxation. Pillar One attempts to establish a nexus based on comprehensive economic engagement metrics, including revenue thresholds, user bases, and digital presence indicators that reflect purposeful and sustained interaction with the economy of a country via technology and other automated tools⁵⁰. The BEPS framework recognizes that user data and network effects create value that should be captured through sophisticated profit allocation mechanisms rather than crude gross revenue taxes. India's Equalization Levy, by contrast, establishes a nexus through simple payment flows and basic territorial connections subject to a low threshold. This approach leads to taxing any non-resident entity providing digital services to Indian residents, regardless of their level of economic engagement or value creation in India. This prioritizes immediate revenue generation over the complex value attribution mechanisms that Pillar One seeks to develop.

Finally, from the domestic law perspective, critiques also extend to constitutional concerns about India's legislative competence to enact such a tax. Under India's Constitution, the taxation of "advertisements other than advertisements published in newspapers and advertisements broadcast by radio or television" falls under the exclusive power of state legislatures, not the Parliament⁵¹. Critics argue that since the Equalization Levy deals primarily with advertisement services, the Parliament may lack constitutional authority to legislate in this area. The broad wording of the levy's regulation creates additional constitutional challenges.

Concerning India's Equalization Levy's ability to tax digital advertising in the mobile games context, the framework acknowledges that mobile advertising

⁵⁰ OECD. *Tax challenges arising from digitalisation: report on Pillar One Blueprint*. Paris: OECD Publishing. Available at: <https://doi.org/10.1787/beba0634-en>. Access: June 7, 2026.

⁵¹ GOVIND, Sriram. *Unilateralism in taxing the digitalized economy: comparing the EU digital services tax proposal and the Indian Equalization Levy*, p. 4.

operates through real-time bidding systems where game studios, advertisers, and ad networks can access millions of users in different countries and generate substantial revenue without establishing any physical presence in market jurisdictions. This approach aligns with the OECD's recommendation for a new nexus based on significant economic presence, which considers digital factors such as localized platforms, customer accounts, and user-based factors associated with data collection and interactions. The traditional permanent establishment concept proves inadequate for digital gaming and advertising, where value creation is driven by user engagement rather than physical assets.

However, the design of India's Equalization Levy fails to differentiate various types of digital advertising based on their level of market presence and user engagement intensity. The levy applies a uniform 6% rate across all online advertising services without distinguishing Around-Game Advertising or In-Game Advertising. This one-size-fits-all approach overlooks the fundamental differences in how these advertising types create value and engage with users. AGAs, which appear as banners or interstitials around game displays with minimal connection to gameplay, should arguably face lower taxation in market jurisdictions compared to IGAs, which involve sophisticated integration with gameplay through branded characters, customized skins, and product placements. The EL's structure fails to recognize that IGAs create deeper user engagement and derive more substantial value from local user data and interactions, warranting higher taxation in source countries.

This is particularly problematic when considering the varying degrees of user data utilization and market presence. User data creates disproportional value in digital advertising by enabling better audience targeting and maximizing return on investment, with this data being particularly crucial for RTB systems that evaluate billions of simultaneous bids. IGAs and rewarded advertisements rely heavily on user behavior analysis, demographic tracking, and engagement scoring to optimize pricing and effectiveness. In contrast, simpler AGAs like static banners may require less sophisticated user data processing. The levy's structure ignores these distinctions, applying the same tax rate regardless of whether the advertising model extensively monetizes local user data or operates with minimal data dependency.

While the Equalization Levy's withholding tax mechanism operates efficiently by placing collection responsibility on Indian business payers rather than requiring foreign companies to register and comply with Indian tax obligations, this design creates a significant tax gap when foreign advertisers purchase advertising space from non-resident platforms to target Indian users. Since neither party has to be present in India to operate, substantial economic value extraction remains unaddressed by the EL. For instance, when a US-based game developer purchases user acquisition campaigns from Google or Facebook (also resident in

the US) to specifically target Indian mobile users, the substantial economic value created by Indian user engagement, data collection, and conversion activities remains completely untaxed by India. This structural flaw undermines the levy's fundamental objective of ensuring that market jurisdictions receive fair compensation for the value created by their users, as the most valuable advertising transactions – those specifically designed to monetize Indian users' engagement and data – often escape taxation entirely when structured through offshore entities. Also, the EL's focus on the payer's residence rather than the user's location creates perverse incentives for tax avoidance through restructuring business arrangements to avoid Indian business presence while continuing to extract substantial value from the Indian market.

Wei Cui's conceptual defense of digital services taxes provides a useful theoretical foundation for treating user-based advertising revenue as more than a mere destination-market proxy. If digital platforms earn location-specific rents from the interaction, data, and attention of users located in a given jurisdiction, that jurisdiction may have a principled claim to tax part of such rent⁵². In mobile games, this claim is particularly strong where advertising revenue depends on behavioral targeting, engagement metrics, rewarded ads, and real-time bidding systems that transform local user activity into monetizable advertising value.

Therefore, a more sophisticated approach to taxing digital advertising should incorporate tiered taxation based on the level of market presence and user data utilization, distinguishing low-engagement ad formats from interactive and data-intensive advertising models. AGAs, which operate with minimal connection to local gameplay and user engagement, should face lower taxation rates in market jurisdictions, reflecting their limited value creation from local user interactions. Conversely, IGAs that extensively utilize user data for sophisticated targeting, create deep user engagement through branded content integration, and derive substantial value from local user behavior should face higher taxation rates. Rewarded advertisements, which achieve the highest effectiveness in engaging and retaining users and consequently pay the largest fees to game developers, should be subject to higher taxation rates reflecting their intensive use of user data and engagement metrics⁵³.

⁵² CUI, Wei. The digital services tax: a conceptual defense. *Tax Law Review*, 2019. Available at: <https://ssrn.com/abstract=3273641>. Access: June 7, 2026, p. 11-14.

⁵³ The case for higher taxation is particularly strong where advertising is targeted at users in a specific jurisdiction and monetizes their expected conversion behavior. Cui illustrates this through the example of a German car manufacturer purchasing Google advertising to target UK consumers: the resulting advertising revenue is more closely traceable to the UK, where the targeted audience is located, than to Germany, where the advertiser pays, or to the jurisdictions where Google's servers or R&D may be located. The same reasoning applies to mobile games where rewarded ads, behavioral targeting, or predictive bidding systems monetize the attention and interaction of users located in a specific market. See: CUI, Wei. The digital services tax: a conceptual

In this sense, a first tier, taxed at a reduced tax rate, could be formed of advertising that derives limited value from local user engagement patterns. The minimal engagement could be qualified by the type of ad unit (such as static banner ads, pop-ups, or interstitials that appear outside the core gameplay experience – considering there is no gameplay integration and that ad units can be easily skipped or ignored) or by the level of user data utilization, considering for this tier only basic demographic targeting, such as age, gender, and location. A second tier, taxed at a standard (or intermediary) tax rate, could be composed of advertising that rely on moderate user engagement, either by the type of ad unit (such as billboard placements, branded vehicles, and other environmental advertising within the game) or by the deeper reliance on user data, when the advertiser leverages behavioral targeting based on gaming preferences, session duration, and purchase history of users. Finally, a last tier could be taxed at a maximum rate and encompass interactive in-game advertising, such as branded content that players can meaningfully interact with, affecting gameplay mechanics, and rewarded videos where users voluntarily engage with advertisements in exchange for in-game benefits, and other types of advertising that rely on advanced targeting using gameplay analytics, social connections or other cross-platform user tracking, and predictive modeling for real-time optimization. These ads create substantial value through deep user interaction and sophisticated data utilization, justifying higher taxation reflecting enhanced local value creation.

This tiered approach also responds to a structural weakness of India's Equalization Levy: the levy focuses on the residence of the payer rather than the location and intensity of the targeted user base. Cui distinguishes between taxes on advertising revenue based on where the advertising purchaser is located and taxes based on where the targeted audience is located. For mobile games, the latter approach is more coherent, because the value of digital advertising depends not merely on who pays for the campaign, but on where users view, interact with, and generate data for the ad. However, it provides significant compliance and administration challenges as it depends on complex technical information at a very granular level, which can be particularly problematic for developing countries that would most benefit from it. An alternative solution that prioritizes compliance simplicity would be to define such tiers based on revenue thresholds, assuming that advertisements that are more reliant on user data and interaction produce more revenue. This alternative would be simpler to implement and, while it provides a certain level of fairness by implementing a progressive tax system, it does not properly capture the value created by user interaction, which is core to online advertising.

defense. *Tax Law Review*, 2019. Available at: <https://ssrn.com/abstract=3273641>. Access: June 7, 2026, p. 15-16.

The path forward for efficiently taxing digital advertising requires a nuanced framework that properly compensates market jurisdictions for user-generated value while recognizing the varying degrees of economic presence across different advertising types. Market jurisdictions like India, with substantial user bases that create significant value for global digital platforms, deserve fair compensation through taxation systems that reflect the true economic contribution of their users to digital advertising ecosystems. This would not only improve revenue collection efficiency but also create appropriate incentives for digital platforms to fairly compensate the jurisdictions where their users generate substantial economic value.

Finally, in the 2025-2026 Finance Bill, the Indian Finance Minister announced the revocation of the Equalization Levy on Digital Advertising effective from April 2025. Besides being a clear response to several critiques posed upon its design and regulations, the repeal of the EL also addresses concerns raised by the US reciprocal tariffs crisis that also happened in April 2025⁵⁴. This aligns with the EL's intention as an interim measure that should be replaced by a multi-lateral solution.

5. Conclusion

The taxation of digital advertising in mobile gaming is a pressing challenge in contemporary international tax law, highlighting the fundamental disconnection between traditional tax frameworks and the realities of the digital economy. This paper's examination of India's Equalization Levy provides relevant insights into both the promise and limitations of unilateral approaches to taxing digital services, while demonstrating the urgent need for more sophisticated and internationally coordinated solutions.

India's Equalization Levy was a pioneering unilateral response to the limitations of traditional nexus rules. Its main advantage was administrative: by taxing gross payments for online advertising outside the income tax system, India could collect revenue without renegotiating tax treaties. However, this same design also explains many of its weaknesses, including overbreadth, double taxation risks, and an insufficient connection between the tax burden and the actual intensity of user-generated value. Its low threshold and broad scope also raised proportionality concerns, as the compliance burden may have exceeded the revenue benefits in smaller transactions.

In this context, there are also serious concerns about double taxation arising from the levy's interaction with residence-based taxation systems. Companies

⁵⁴ AHMED, Aftab; KUMAR, Manoj. *India to scrap digital ad tax, easing US concerns*. Thomson Reuters. March 25, 2025. Available at: <https://www.reuters.com/world/india/india-proposes-remove-equalisation-levy-digital-services-government-source-says-2025-03-25/>. Access: June 28, 2025.

may face not only the Equalization Levy in India but also corporate income tax in their residence countries, with some potentially facing triple taxation when subsidiaries in multiple jurisdictions with digital service taxes are involved. This violates fundamental principles of international tax law embodied in bilateral tax treaties and OECD model conventions.

The Indian experience with the Equalization Levy offers valuable lessons for other jurisdictions grappling with digital economy taxation. While unilateral measures can provide immediate policy responses to tax challenges, their effectiveness is ultimately limited by design flaws, administrative complexities, and international coordination failures. The introduction of a Multilateral Convention to Implement Amount A in 2023 confirms that the international tax debate has moved from the mere recognition of digital nexus to the design of administrable mechanisms for reallocating taxing rights to market jurisdictions. However, the Convention also illustrates the trade-off inherent in multilateral solutions: in order to achieve administrability and political consensus, Amount A applies only to covered multinational groups and reallocates a portion of residual profits through standardized rules. As a result, it does not directly solve the more granular problem examined in this article: how to distinguish, within digital advertising, the different degrees of value generated by local user attention, interaction, data collection, and behavioral targeting.

The mobile gaming industry's global nature and sophisticated advertising mechanisms demand equally sophisticated tax responses that can only be achieved through coordinated international efforts that properly account for value creation in digital ecosystems. Therefore, this analysis concludes that effective taxation of digital advertising requires a more nuanced framework that properly compensates market jurisdictions for user-generated value while recognizing varying degrees of economic presence across different advertising types. The proposed tiered taxation system, with lower rates for AGAs and higher rates for IGAs and rewarded advertisements, would better reflect the actual value creation from local user interactions.

Such a system should incorporate user-based allocation keys that account for the number of active users, depth of engagement, volume of data processed, and sophistication of targeting mechanisms. This approach would create appropriate incentives for digital platforms to fairly compensate jurisdictions where users generate substantial economic value, while improving revenue collection efficiency.

The future of digital advertising taxation lies not in blanket unilateral measures but in nuanced, internationally coordinated frameworks that recognize the complex realities of digital value creation while ensuring fair compensation for market jurisdictions. Only through such comprehensive approaches can tax systems effectively address the challenges posed by the digital economy while maintaining the fundamental principles of international tax law.

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