

# **DIGITAL VIRTUAL ASSETS AND ITS TAX IMPLICATIONS**

- by Tanu Priya

In this ever changing world, virtual currency has replaced all the various lucrative assets and investment products around the globe. However, this block-chain technology, which claims to be non-regulatory and decentralized, has unfortunately confused the masses. Even with ambiguous regulatory methods implied on the Crypto transactions, middle class investors did not back down from pooling their money in it.

RBI, the national regulation authority, has not recognized VAs (Virtual asset) as a legal tender. This decision of government has directly affected the tax implications on the VAs. Prior to the Finance Bill 2022, income generated from VAs was taxed under the Capital Gains head or business income under Profits and Gains from Business and Profession (PGBP), based on the usage by the assessee. However, the central government has changed their stance by imposing a heavy levy of 30% on income earned from VA trading under the Other Sources head. This move is being praised for being the first step of government towards regulating Virtual Currencies like Crypto. We cannot overlook upon the intention of authorities behind the act. It is primarily to discourage masses from investing in crypto. This was done to decrease the huge number of young investors moving towards the industry.

The position under direct taxation can still be considered as great if we were compare it with the Indirect sector. Cryptomining has still not been recognised by the statues. An effort was made by Central Economic Intelligence Bureau (CEIB) to impose 18% GST on Bitcoin Transaction. The classification of Crypto is the most crucial task for it to fall under the pursuit of GST. The virtual assets need to recognised either as a Good or Service under the statue. Furthermore, a rate of levy needs to be decided. Considering the rates under Income Tax, the government might settle on a GST slab of 18%. Trading Platforms like Wazirx and CoinDX to pay service tax on for facilities they provide in assisting the transactions.

Crypto is highly criticized for the role played by it in black market and funding terrorist activities. Government aims at promoting more reliable investment products like Stocks and securities mainly because they are covered by regulation authorities so any upcoming economic crises could be monitored and prevented. However, the wave of crypto has already hit the cities and staying in denial is not the right recourse. Positive attitude is the key. The volatile Indian

market can be used in a way by authorities to directly help in increasing revenue and which will also help it in becoming a most suitable virtual trading hub.

## **INTRODUCTION**

*“Cryptocurrency is here to stay, so we hear on cryptosphere everyday. But there are some fundamental situations that needs to take place for this speculated ‘store of value’ to really have its foot to stand on, and that is, government’s ability to enforce taxation on businesses and individuals making gains with this currency.*

*So, either we like it or not, crypto taxation needs to be enforced for government to really entertain any form of adoption. Asian countries dominates the cryptocurrency spaces but the governments are finding it a bit hard to really tax crypto transactions.”*

- Olawale Daniel, Founder - TechAtLast International

## **WHAT IS A VIRTUAL DIGITAL ASSET ?**

A virtual asset is a virtual illustration of an item that has price in a specific surroundings. This medium of trade or assets may be digitally traded, transferred or used for price or investment purposes.<sup>1</sup> The Supreme Court, in the case of Internet and Mobile Association of India v. Reserve Bank of India<sup>2</sup> conducted a detailed analysis into the existing literature on the matter. It extensively quoted the Financial Action Task Force (“FATF”) report titled ‘Virtual Currencies Key Definitions and Potential AML/CFT Risks’.<sup>3</sup> The FATF in this report defines 'virtual currency' as a digital representation of value that can be traded digitally and functions as (i) a medium of exchange; (ii) a unit of account; and/or (iii) a store of value, but not having a legal tender status in any jurisdiction. It is not issued, nor guaranteed by any jurisdiction, and fulfils the above functions only by agreement within the community of users of the virtual currency.<sup>19</sup> The report further distinguishes between e-money and virtual currency and defines the former as a digital representation of fiat currency used to electronically transfer value

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<sup>1</sup> Robert Shelon, Virtual Asset, <[www.techtarget.com/whatis/definition/virtual-asset](http://www.techtarget.com/whatis/definition/virtual-asset)>, Whatls.com, accessed 31 October, 2022

<sup>2</sup> Internet and Mobile Association of India v. Reserve Bank of India, Writ Petition (Civil) Nos. 528 and 373 of 2018, Decided On: 04.03.2020, MANU/SC/0264/2020MANU/SC/0264/2020

<sup>3</sup> FATF Report, Virtual Currencies Key Definitions and Potential AML/CFT Risks (June 2014) available at <https://www.fatf-gafi.org/media/fatf/documents/reports/Virtual-currency-key-definitions-and-potential-aml-cft-risks.pdf>, accessed 3 November 2022

denominated in fiat currency.<sup>20</sup> Due to this fundamental distinction between virtual currency and legal tender, many believe that the expression virtual “currency” can be misleading.<sup>21</sup> The expression “payment tokens” is therefore often used to more precisely denote the concept of “virtual currencies” and can usually be interchangeably used.

VAs include things :

A) Cryptocurrencies

B) NFTs – non fungible tokens

Both of these are one-of-a-kind software of blockchain technology. Cryptocurrencies wherein a finite set of ‘currency’ devices, known as cash, are used as an electronic coins machine. This may be connected to an underlying asset or have a few inherent fee.<sup>4</sup>

Non Fungible tokens, which are much like cash, may be sold and offered in a virtual form. Unlike cryptocurrencies where the coins are homogenous, NFTs are non-fungible, i.e., non-interchangeable by using nature such that every token is particular and has a fee this is wonderful from different tokens. NFTs are connected to one or greater underlying assets including artwork or actual estate, which offers it its price<sup>5</sup>

## **TAXES AND THEIR PURPOSE**

Taxes are one of the number one resources of profits for the government through which it fulfils various tasks and tasks. Tax serves numerous functions and is crucial for any nation’s economic development, sustenance and development. Even as the tax cash is utilised for pleasing various initiatives, it’s also the primary supply of funding for numerous important authorities welfare schemes. It enables the authorities in enforcement of legal guidelines and the judicial system. The Indian Constitution under Article 246 enlists different taxations in the country between the Centre and the State.<sup>6</sup>

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<sup>4</sup> ibdi

<sup>5</sup> Sharanya Ranga and Farshad Ali, India: Virtual Digital Assets In India: A Sneak Peek Into India's Regulatory Framework, <[www.mondaq.com/india/fin-tech/1164634/virtual-digital-assets-in-india-a-sneak-peek-into-india39s-regulatory-framework](https://www.mondaq.com/india/fin-tech/1164634/virtual-digital-assets-in-india-a-sneak-peek-into-india39s-regulatory-framework)>2022, Mondaq, accessed 8 Novemeber 2022

<sup>6</sup> ABC of Money, Aditya Birla Capital blog, <<https://www.adityabirlacapital.com/abc-of-money/what-is-tax>>, 2019, accessed on 29 October, 2022

## **BLOCKCHAIN AND WORKING OF VDS**

Both cryptocurrencies and NFTs are primarily based on blockchain or different dispensed ledger technology. Oversimplified, blockchain is a way of storage of statistics in a decentralised way such that nobody person (or institution) can exercise absolute control over the records. The term 'blockchain' refers to the manner in which new packets of records (referred to as blocks) whilst delivered are linked to the closing delivered block of facts, as a result forming a sequence of records blocks linked chronologically. A key feature of blockchain era is the way wherein facts blocks are proven and brought. This happens thru a community of computer systems running in parallel,<sup>7</sup> without any one laptop regulating the blockchain or exercise advanced control over the management or storage of the data or the verification processes. Records once added to a blockchain cannot be deleted, modified or tampered with, for this reason a blockchain forms an correct and reliable chronologically organized report of all records that has been introduced to the blockchain. As a end result, despite the fact that there is any human error in the facts being added, the added facts cannot be edited to rectify the error; only a new block can be introduced to well-known and address the mistake.<sup>8</sup>

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<sup>7</sup> FATF Report, Virtual Currencies Key Definitions and Potential AML/CFT Risks (June 2014) available at <https://www.fatf-gafi.org/media/fatf/documents/reports/Virtual-currency-key-definitions-and-potential-aml-cft-risks.pdf>, accessed 3 November 2022

<sup>8</sup> ibidi

## **EVOLUTION OF VDAs IN INDIA**

The crypto story in India started in 2013, when India's primary bank, the Reserve financial institution of India (RBI), has warned residents of the dangers related to buying and selling virtual currencies, and how buying and selling of such currencies in overseas exchanges might also bring about violation of forex regulations (FEMA).

RBI has clarified that digital currencies might not be used as felony gentle in India. In that feel, a cryptocurrency could neither be handled as a foreign foreign money (as recognized under FEMA) or be used in lieu of the Indian Rupee. It may be inferred that the fee of attention with cryptocurrency for buy of goods or services would be handled as an trade in place of an outright sale.

In parallel, reacting to the pointy appreciation in value of Bitcoin and comparable traits with different cryptocurrencies, the income Tax department had in December 2017 issued half a million notices to high internet well worth individuals who personal cryptocurrencies seeking confirmation that there are not any unpaid taxes arising from their buying and selling of cryptocurrencies.

Having realized the underwhelming impact of such warnings, RBI adopted a one of a kind technique issuing a circular in April 2018<sup>9</sup> restricting banks and different economic institutions from facilitating the buying and selling of cryptocurrencies on both Indian and distant places exchanges. These instructions rendered Indian cryptocurrency exchanges efficiently defunct in a single day.

This changed into challenged before the Indian ideally suited court in may also 2018 via the net and cell affiliation of India on the ground that this sort of round would tantamount to a denial of cryptocurrency investors' constitutional proper to carry on any exchange or profession, and might therefore be violative of Article 19(1)(g) of the Indian constitution. In its judgement of March 2020, the splendid court set aside the RBI round staring at that within the absence of any legislative ban at the shopping for or promoting of cryptocurrencies, RBI isn't legal to impose disproportionate restrictions on Indian cryptocurrency exchanges. While maintaining that casual investors or those undertaking buying and selling of cryptocurrencies as a commercial enterprise could now not be entitled to a claim beneath the stated article, the

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<sup>9</sup> Ministry of Finance, Press Release dated 1 February 2022 available at, <https://pib.gov.in/PressReleasePage.aspx?PRID=1794160>, accessed on 17 October 2022

supreme courtroom discovered that the round disconnected the banking area from cryptocurrency exchanges no matter the RBI no longer having located whatever wrong with the functioning of those exchanges. It became also stated that earlier than issuing the round, the RBI did now not discover the availability of alternative less intrusive measures consisting of regulating cryptocurrency buying and selling and cryptocurrency exchanges. The popularity of cryptocurrency in India is clear from the fact that it houses 10.07 crore crypto owners, which is more than every other country in the world.<sup>10</sup>

It is now a long-settled position that the legality of or manner of acquiring income has no bearing on its taxability.<sup>11</sup> Therefore, a lack of clarity with respect to its tax treatment is not only depriving the crypto community of certainty and stability, but it is also robbing the nation's treasury of its fair share of tax revenue.

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<sup>10</sup> Press Trust of India, "India has highest number of crypto owners in the world at 10.07 crore: report", Livemint (13 October 2021) available at <https://www.livemint.com/market/cryptocurrency/india-has-highest-number-of-crypto-owners-in-the-world-at-10-07-crore-report-11634110396397.html>, accessed on November, 2022.

<sup>11</sup> Commissioner of Income-tax v. K. Thangamani [2009] 309 ITR 15 (Madras); V.V. Minerals [100% EOU] v. Commissioner of GST & CE (CESTAT Chennai), Service Tax Appeal Nos. 40343 to 40346 of 2020-DB

## **MONEY LAUNDERING AND TERROR FUNDING CONCERNS**

The Cryptocurrency & regulation of legitimate virtual forex invoice, 2019 launched in December 2019 meant to prohibit and criminalise the maintaining, selling or trading of cryptocurrency, punishable with imprisonment of up to ten years, or a quality, or both. The bill in addition outstanding and accepted the other programs of the underlying disbursed ledger technology for experiments, research, or teaching. It moreover accredited RBI to roll out a government advocated virtual foreign money.

Presently, RBI continues to explicit its apprehensions in legalising cryptocurrency transactions, and its capacity to destabilise the Indian economy, and to pass government efforts to monitor and manipulate the waft of cash by illegal way and for illicit activities. In light of this, RBI indicates a hard-line technique by means of banning and criminalising all decentralised cryptocurrency transactions. This contrasts sharply with the critical government's concept to give digital virtual assets criminal repute. As a result, this differing stance at the legality of virtual virtual property, coupled with the evolving view of courts, simply makes the future of digital virtual belongings unsure.<sup>12</sup>

Virtual assets are at risk of being misused through criminals to launder money and fund terrorism as they allow extra ranges of anonymity, have international reach making it easier for go-border payments, and they can be traded effortlessly.<sup>13</sup>

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<sup>12</sup> Sharanya Ranga and Farshad Ali, India: Virtual Digital Assets In India: A Sneak Peek Into India's Regulatory Framework, <<https://www.mondaq.com/india/fin-tech/1164634/virtual-digital-assets-in-india-a-sneak-peek-into-india39s-regulatory-framework>>2022, Monaq, 8 Novemeber 2022

<sup>13</sup> Te Tari Taiwhenua | Department of Internal Affairs Building, Virtual Asset Service Provider, 2019, <<https://www.dia.govt.nz/AML-CFT-Virtual-Asset-Service-Providers>>, accessed on 29 October, 2022

## **PRE FINANCE BILL 2022 STATUS OF VDAs IN INDIA**

Besides regulatory actions, there have also been concerted efforts to “ban all private cryptocurrency”. Most notably, a bill in this regard was set to be placed before the Parliament in its winter session in late 2021.<sup>14</sup> Though this bill has not been made public yet and was never actually placed before the Parliament, it disrupted the crypto ecosystem in India. In parallel, other disincentives have continued. For instance, the Advertising Standards Council of India which is a self-regulatory organisation of the Indian advertising industry, came out with guidelines to regulate the advertising and promotion of cryptocurrencies.<sup>15</sup> It noted that several crypto advertisements did not adequately disclose the risks associated with such products. The guidelines required all such advertisements to carry the disclaimer that “Crypto products and NFTs are unregulated and can be highly risky. There may be no regulatory recourse for any loss from such transactions.” It also required the disclaimer to be carried in such a manner that it is prominent and unmissable by an average consumer. On the tax front too, there has been an immense lack of clarity. Back in 2021, Minister of State for Finance, Mr. Anurag Singh Thakur had said in response to a question in the Rajya Sabha that “the gains resulting from the transfer of cryptocurrencies/assets are subject to tax under the head of income, depending upon the nature of holding of the same”. However, within a span of a year since this aforementioned statement, the Ministry of Finance took a completely different and classification agnostic approach to taxing cryptocurrencies. In the Budget for the Financial Year 2022-23, the Finance Minister made four key amendments to the Income-tax Act, 1961 (“IT Act”).<sup>16</sup>

The Finance Act 2022 inserted:

- (i) Section 2(47A) to define virtual digital assets;
- (ii) Section 115BBH that specifies the rate at which transfer of these ‘virtual digital assets’ will be liable to income-tax, the rate of tax being 30 percent;

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<sup>14</sup> Asit Ranjan Mishra, Prasad Banerjee, “Govt. to move bill to ban all private cryptocurrencies”, Livemint (24 November 2021), <[www.livemint.com/market/cryptocurrency/govt-to-move-bill-to-ban-all-privatecryptocurrencies-11637693131165.html](http://www.livemint.com/market/cryptocurrency/govt-to-move-bill-to-ban-all-privatecryptocurrencies-11637693131165.html)> accessed on 23 October 2022

<sup>15</sup> Pooja Sitaram Jaiswar, After 30 percent tax rate, cryptocurrency assets to bear 1 percent TDS, <https://www.livemint.com/market/cryptocurrency/after-30-tax-cryptocurrency-assets-to-bear-1-tds-how-taxes-impact-cryptos-11656245759063.html>, Livemint, accessed on 31 October, 2022

<sup>16</sup> Vidushi Gupta, Yeeshya Shriyan, Aashima Sawhney, Taxing Cryptocurrencies: The concept, the challenges and the required changes, 2022, VIDHI Centre For Legal Policy, <[https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527\\_WP\\_Taxing-Cryptocurrencies\\_VCLP.pdf](https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527_WP_Taxing-Cryptocurrencies_VCLP.pdf)>, accessed on 02 November, 2022



(iii) An explanation under clause (x) of section 56(2) to the effect that property would include ‘virtual digital asset’; and (iv) Section 194S that provided for tax deduction at source on payment towards consideration for transfer of virtual digital assets.

## **FINANCE BIL 2022 AND 30% TAX IMPOSED**

Profits bobbing up from transactions in cryptocurrencies have become taxable from April 1, 2022, following the Budget announcement to that effect by means of Union Minister of Finance Nirmala Sitharaman in February, 2022. She introduced a scheme of 30% taxation on virtual digital assets (VDAs), other than tax deducted at source (TDS) implications, which got here into effect from July 2022<sup>17</sup>

## **TAX ON INCOME FROM VIRTUAL DIGITAL ASSET**

The IT Act defines the term “income” in a broad manner.<sup>18</sup>It further stipulates “heads of income” under which all income needs to be classified for the purpose of charge of income-tax. <sup>19</sup>This list inter alia includes ‘profits and gains from business or profession’, ‘capital gains’ and ‘income from other sources’.<sup>20</sup>

The Supreme Court in Commissioner of Income-tax v. G.R. Karthikeyan<sup>21</sup> has observed that the idea behind providing an inclusive definition of income under section 2(24) of the IT Act is not to limit its meaning but to widen its net and the word ‘income’ is of widest amplitude, and that it must be given its natural and grammatical meaning. Accordingly, any income earned from cryptocurrency would naturally fall within the ambit of the IT Act.

## **Section 28, Finance Act, 2022 - Intersertion of new sections 115BBH and 115BBI**

After section 115BBG of the Income-tax Act, the following sections shall be inserted with effect from the 1st day of April, 2023, namely:-

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<sup>17</sup> Harsh Kumar, 6 Months After Crypto Taxation, A Look At Its Impact on Industry, Investors, <<https://www.outlookindia.com/business/6-months-after-crypto-taxation-a-look-at-its-impact-on-industry-investors-news-227172>>, 2022, accessed on 23 October, 2022

<sup>18</sup> Section 2, sub-section 29, Income Tax Act, 1961

<sup>19</sup> Section 14, Income Tax Act, 1961

<sup>20</sup> Section 14, Income Tax Act, 1961

<sup>21</sup> CIT v. G.R. Karthikeyan (1993) 112 CTR (SC) 302).

*Section 115BBH, The Income Tax Act, 1961:*

(1) Where the total income of an assessee includes any income from the transfer of any virtual digital asset, notwithstanding anything contained in any other provision of this Act, the income-tax payable shall be the aggregate of,-

(a) the amount of income-tax calculated on the income from transfer of such virtual digital asset at the rate of thirty per cent.; and

(b) the amount of income-tax with which the assessee would have been chargeable, had the total income of the assessee been reduced by the income referred to in clause

(2) Notwithstanding anything contained in any other provision of this Act,-

(a) no deduction in respect of any expenditure (other than cost of acquisition, if any) or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing the income referred to in clause (a) of sub-section (1); and

(b) no set off of loss from transfer of the virtual digital asset computed under clause (a) of sub-section (1) shall be allowed against income computed under any provision of this Act to the assessee and such loss shall not be allowed to be carried forward to succeeding assessment years.

(3) For the purposes of this section, the word “transfer” as defined in clause (47) of section 2, shall apply to any virtual digital asset, whether capital asset or not.

*Specified income of certain institutions Section (115BBI)<sup>22</sup>*

(1) Where the total income of an assessee, being a person in receipt of income on behalf of any fund or institution referred to in sub-clause (iv) or any trust or institution referred to in sub-clause (v) or any university or other educational institution referred to in sub-

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<sup>22</sup> Section 115BBI, Income Tax Act, 1961

clause (vi) or any hospital or other medical institution referred to in sub-clause (via), of clause (23C) of section 10 or any trust or institution referred to in section 11, includes any income by way of any specified income, notwithstanding anything contained in any other provision of this Act, the income-tax payable shall be the aggregate of,-

(i) the amount of income-tax calculated at the rate of thirty per cent. on the aggregate of such specified income; and

(ii) the amount of income-tax with which the assessee would have been chargeable had the total income of the assessee been reduced by the aggregate of specified income referred to in clause (i).

(2) Notwithstanding anything contained in this Act, no deduction in respect of any expenditure or allowance or set off of any loss shall be allowed to the assessee under any provision of this Act in computing the specified income referred to in clause (i) of sub-section (1).

Explanation.-For the purposes of this section, “specified income” means,-

(a) income accumulated or set apart in excess of fifteen per cent. of the income where such accumulation is not allowed under any specific provision of this Act; or

(b) deemed income referred to in Explanation 4 to the third proviso to clause (23C) of section 10, or sub-section (1B) or sub-section (3) of section 11; or

(c) any income, which is not exempt under clause (23C) of section 10 on account of violation of the provisions of clause (b) of the third proviso of clause (23C) of section 10, or not to be excluded from the total income under the provisions of clause (d) of sub-section (1) of section 13; or

(d) any income which is deemed to be income under the twenty-first proviso to clause (23C) of section 10 or which is not excluded from the total income under clause (c) of sub-section (1) of section 13; or

(e) any income which is not excluded from the total income under clause (c) of sub-section (1) of section 11.<sup>23</sup>

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<sup>23</sup> Section 28, Finance Act, 2022

## **THE EFFECT OF INCOME TAX IMPLICATION**

Though there is a lot of doubts and ambiguousness regarding the functionality of the new introduced changes, the crypto investor and the general public should keep in mind that The entire 30% tax on any crypto assets will be deducted from the profits earned via various crypto tokens in an entire financial year. The starting of this 30% tax will be from the Assessment of the FY 2023-24. The following points shall also be kept in mind

- a) Income from the transfer of virtual digital assets such as crypto and NFTs will be taxed at 30% at the end of each financial year.
- b) No deduction, except the cost of acquisition, will be allowed while reporting income from the transfer of digital assets.
- c) Loss from digital assets cannot be set off against any other income.
- d) The gifting of digital assets will attract tax in the hands of the receiver. Losses incurred from one virtual digital currency cannot be set off against income from another digital currency. 1% TDS point should also be mentioned in this list of pointers as it was announced in Budget 2022.<sup>24</sup>

## **ASSETS SUBJECT TO TAX IMPLICATIONS**

The earnings Tax Act turned into amended with effect from April 1, 2022 to provide for the taxation of profits and, or, profits derived from VDAs. Below the earnings Tax Act, VDAs are: Cryptocurrencies not being Indian or foreign foreign money (the proposed virtual Rupee could seemingly be exempt as a end result) – the particular terminology used underneath the income Tax Act is “...any facts or code or range or token (now not being Indian forex or foreign foreign money), generated through cryptographic way or otherwise, through something call referred to as,<sup>25</sup> supplying a digital illustration of fee exchanged with or without attention, with the promise or representation of having inherent fee, or functions as a shop of cost or a unit of account which include its use in any monetary transaction or funding, but no longer restrained to investment scheme; and may be transferred, saved or traded electronically...”

NFTs or similar tokens as the critical government may additionally notify; and

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<sup>24</sup> Budget 2022 Crypto Tax Update <<https://coindcx.com/blog/cryptocurrency/crypto-tax-guide-india/>>, accessed 9 November 2022

<sup>25</sup> Shehnaz Ahmed and Swarna Sengupta, “Blueprint of a Law regulating for regulating Cryptoassets” (January 2022) available at <https://vidhilegalpolicy.in/research/blueprint-of-a-law-regulating-cryptoassets/>, accessed on 3November 2022

Such other virtual property as the crucial government may additionally notify.

Interestingly, the income Tax Act does no longer point out either blockchain or DLT within the definition of VDAs. The relevant government has but to notify the NFTs, tokens or different VDAs to which the provisions of the profits Tax Act will observe. While it can, therefore, be argued that no NFTs are currently protected via the brand new tax regime, there is a opportunity that the tax authorities will select to tax NFTs under the cryptocurrency head as the definition consists of tokens and can be considered wide enough to consist of NFTs. It'd, therefore, be prudent for taxpayers to count on that the NFTs they accumulate, sell, and, or, otherwise address are in all likelihood to be taxable under the regime.

Under the Income Tax, there could be three scenarios. First, where if someone gets a VDA without attention and the fair market value of that VDA exceeds INR 50,000 – the entire truthful marketplace fee of the asset is taken into consideration taxable profits in the fingers of the individual that obtained the VDA. The applicable price of tax will depend upon the income tax bracket within that man or woman in most cases falls. Second, when someone gets a VDA for consideration lower than the fair marketplace price, and the truthful market price exceeds the consideration by using extra than INR 50,000 – the difference between the honest marketplace fee and the consideration paid is considered taxable earnings within the hands of the individual that obtained the VDA. The relevant rate of tax will rely on the profits tax bracket within that person by and large falls. Third, in which a person earns earnings from the switch of a VDA – the profits earned by using that character less the price of acquisition, if any, is problem to tax on the fee of 30%. Moreover, an equalization levy of 2% will be levied on the non-resident proprietor of the blockchain on which NFTs are traded.<sup>26</sup>

### **1% TDS DEDUCTION AND SECTION 206AB**

The earnings Tax Act in addition complicates subjects through requiring that, where a resident transfers a VDA for attention, the person liable for paying that attention must deduct 1% of the consideration at supply as earnings tax. The requirement to deduct 1% of the attention applies regardless of whether or not the consideration is in cash, in part in cash and in part in attention for another VDA, or in attention for only some other VDA.

The duty to withhold tax may also be imposed on the proprietor of the blockchain on which NFTs are traded (whether or not they're resident in India) as they will be taken into consideration e-trade operators facilitating the trading of NFTs.

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<sup>26</sup> Shehnaz Ahmed and Swarna Sengupta, "Blueprint of a Law regulating for regulating Cryptoassets" (January 2022) available at <https://vidhilegalpolicy.in/research/blueprint-of-a-law-regulating-cryptoassets/>, accessed on 3November 2022

Tax does not need to be deducted where:

1. The consideration is paid by a “specified person” and the aggregate value of the consideration being paid does not exceed INR 50,000 during the financial year; or
2. The consideration is paid by a person other than a “specified person” and the aggregate value of the consideration being paid does not exceed INR 10,000 during the financial year. A “specified person” is defined as an individual or Hindu undivided family:
3. whose total sales, gross receipts or turnover from the business carried on by him or profession exercised by him does not exceed INR 1 crore in case of business or INR 50 lakhs in case of profession, during the financial year immediately preceding the financial year in which such VDA is transferred;
4. that does not have any income under the head “profits and gains of business or profession”.

As a consequence, tax will generally need to be deducted at source by most persons acquiring VDAs unless they fit the criteria of “specified persons” or only make purchases of VDAs infrequently and for small amounts.

Section 206AB, Income Tax Act, 1961:

1. If any user has not filed their Income Tax Return in the last two years and the amount of TDS is ₹ 50,000 or more in each of these two previous years, then the tax (TDS) to be deducted for Crypto related transactions will be at 5%.<sup>27</sup>
2. If an order is placed before 1st July 2022, but the trade is executed on or after 1st July 2022, TDS provisions will apply.<sup>28</sup>

Regarding the 1% TDS reduction on crypto assets According to the revised Income Tax regulations, it will be applicable on all sell transactions of the crypto assets. This will be effective for 1 July, 2022. Whether there is any profit earned or not, TDS will be deducted irrespective of that.

## **SET-OFF OR CARRY FORWARD OF LOSSES NOT ALLOWED**

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<sup>27</sup> Section 206AB of the Income-Tax Act, 1961

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The Income Tax Act expressly prohibits the set-off of losses from transfers of VDAs against profits or gains derived from other VDAs. Illustratively, if someone were to promote an NFT and incur a loss, the loss can't be set-off against a benefit made on the transfer of another VDA. Illustratively, if A sells an NFT paintings for a loss of INR 10,000 after which sells units of Ethereum for a profit of INR 50,000, A could be prone to tax on the whole income of INR 50,000 from the sale of Ethereum and could not be able to set-off the lack of INR 10,000 at the NFT. Basically, beneath the earnings Tax Act, gains and profits from VDAs are taxable however no comfort is furnished within the event losses are incurred, and, to that extent VDAs are taxed otherwise than most different belongings in India.<sup>29</sup>

## **CRYPTO AND THE CAPITAL ASSETS**

Any earnings or profits springing up from the sale of capital property together with equity stocks, mutual finances, bonds, and different commodities are problems for short-term and long-term capital gains taxation. Capital assets that might be held for more than 36 months are called short-time period capital assets. In some cases, belongings like fairness or choice shares in a listed corporation, different listed securities, UTI gadgets, fairness-oriented budget gadgets, or 0-coupon bonds - held now for not more than one year also are categorized as short-term belongings. Within the case of unlisted shares and immovable belongings, those belongings held no longer extra than 24 months are also said to be short-time periods. In the meantime, capital belongings held for greater than 26 months or 24 months, or twelve months inside the above-cited cases - are referred to as long-term capital belongings.<sup>30</sup>

Underneath short-term capital profits tax, if Securities Transaction Tax (STT) is not applicable - then the fast-term capital gains grow to be other earnings tax go back gadgets, and the taxpayer is taxed in step with the profits tax slab quotes. However, if STT is relevant then the short-term capital gains tax is 15%. With regard to long-term capital gains tax, a ten% tax rate is levied on the sale of equity stocks/devices of fairness-orientated budget on amounts above

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<sup>29</sup> Justin M Bharucha, Aashika Jain, How Cryptocurrencies Are Taxed In India, <<https://www.forbes.com/advisor/in/investing/cryptocurrency/cryptocurrency-tax-in-india>>, Forbers Advisors, 2022, accessed 9 November 2022

<sup>30</sup> Pooja Sitaram Jaiswar, After 30 perecent tax rate, cryptocurrency assets to bear 1 percent TDS, <https://www.livemint.com/market/cryptocurrency/after-30-tax-cryptocurrency-assets-to-bear-1-tds-how-taxes-impact-cryptos-11656245759063.html>>, Livemint, accessed on 31 October, 2022

₹ 1 lakh. The tax rate is 20% on belongings besides fairness stocks/equity-oriented price range. Presently, there are not any TDS relevant to domestic buyers on their capital gains. However, NRIs are a problem to 30% TDS on short-time period capital profits and 20% over a long time. Form 15G /15H anyplace relevant is to be had and needed to be submitted to the IT branch to avoid TDS.<sup>31</sup>

From the above, it can be said that cryptocurrency gains or losses still have higher tax rates as compared to the quick term and long term capital profits taxation. Also, TDS is limited to NRIs in capital assets in contrast to the 1% on crypto belongings to be had for citizens.<sup>32</sup>

Problems can also arise in figuring out a taxpayer's taxable profits or profits from the receipt or switch of a VDA:

- a) Where a VDA is received without attention or for a attention decrease than the fair market value, difficulties can also stand up in determining the character's taxable earnings in recognize of the asset. Cryptocurrencies and NFTs are commonly extremely risky with valuations fluctuating on a ordinary foundation. Consequently, it could be difficult to pinpoint the honest market fee of the asset.
- b) Where cryptocurrency is purchased on a crypto-change or an NFT is bought on a market, it is able to normally be argued that the truthful marketplace fee is the price winning on that change or marketplace on the time of the purchase.

However, this may no longer preserve water with the profits tax government as fair marketplace price under the profits Tax Act is to be determined in accordance with the income Tax regulations, 1962 (regulations). At the same time as the policies do prescribe mechanisms for determining the truthful market cost of numerous assets, they do no longer especially cope with the valuation of VDAs, as a consequence creating a lacuna.

Troubles might also stand up where someone is vulnerable to tax on transfer of a VDA. The handiest deduction permitted at the profits earned from the switch of a VDA is the fee of

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<sup>31</sup> Pooja Sitaram Jaiswar, After 30 perecent tax rate, cryptocurrency assets to bear 1 percent TDS, <https://www.livemint.com/market/cryptocurrency/after-30-tax-cryptocurrency-assets-to-bear-1-tds-how-taxes-impact-cryptos-11656245759063.html>, Livemint, accessed on 31 October, 2022

<sup>32</sup> ibdi

acquisition. In which a VDA is bought and offered for an recognized amount in INR or in a foreign forex, the income and the cost of acquisition are easily identifiable. However, if a VDA is acquired using, or offered in exchange for, another VDA (example an NFT is purchased using Bitcoin), the price of acquisition and, or, consideration for the switch of the VDA may be difficult to envision as a selected INR fee for the purchase and, or, switch will no longer be comfortably to be had.

The problems in valuing VDAs for the purpose of taxation may want to result in disputes with the tax authorities. The authorities have additionally confirmed that expenditure incurred in mining cryptocurrency is taken into consideration capital expenditure and no longer a cost of acquisition. Consequently, the full-size expenditure on the hardware required to mine cryptocurrency can't be deducted from any earnings derived from the transfer of cryptocurrency. Whilst no rationalization is to be had in admire of the deduction of costs incurred to mint NFTs, those costs will probable be handled in the identical way as mining charges for cryptocurrencies.<sup>33</sup>

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<sup>33</sup> Justin M Bharucha, Aashika Jain, How Cryptocurrencies Are Taxed In India, <<https://www.forbes.com/advisor/in/investing/cryptocurrency/cryptocurrency-tax-in-india>>, Forbers Advisors, 2022, accessed 9 November 2022

## **IMPACT ON THE INDUSTRY- ECONOMICALLY AND SOCIALLY**

Taxation has definitely made the enthusiasm of Indian crypto investors, cold. Trading volumes on WazirX and CoinDCX dropped by using as a minimum 80 in line with cent. According to data received from facts aggregator nomics.Com, change volumes on Indian cryptocurrency exchanges have considerably decreased after the 1 in keeping with cent TDS came into effect from July 1, 2022.<sup>34</sup>

Some crypto finance experts consider that the big step by the government has been precise for traders, as it has reduced hypothesis and price manipulation inside the unsupervised cryptocurrency industry. The Industry expert, Mr. Gaurav Mehta, founder of Catax – a blockchain auditing and taxation start-up, in an interview had explained in great details the positive impact of the action. People at the moment are buying and maintaining virtual belongings, inclusive of Bitcoin and Ethereum for longer durations of time, with the intention to be high-quality for the crypto financial system in the end. Crypto investors appear to have widely widespread the imposition of a 30 percentage without a loss offset and made peace with it. Due to taxation on each transaction, pump-and-unload activities that prey on unsuspecting traders, are now not viable. Traders may also acquire a clean image of market participation, trading volume, and adaption, which changed into what formerly claimed to be billions at the greenback on a day basis and became normally driven by way of buying and selling bots and phony quantity that dazzled and enticed new traders into the unregulated and risky crypto asset elegance.<sup>35</sup>

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<sup>34</sup> Explained: Why was bitcoin trading cheaper in India today compared to global prices?, <https://www.cnbctv18.com/cryptocurrency/explained-why-was-bitcoin-trading-cheaper-in-india-today-compared-to-global-prices-11578612.htm>, CNBCTV18.com (November 24, 2021) 19 October, 2022

<sup>35</sup> ibdi

## **GST IMPLICATIONS ON CRYPTO**

As for now, there is not GST implication on VDAs however; it is being predicted by the people of the industry that the government might soon move towards this direction. It can be deciphered from the steps the government had taken recently. Recently, The Central Economic Intelligence Bureau (CEIB), proposed to impose 18% GST on Bitcoin transactions. The CEIB told CBIC that Government could potentially gain ₹ 7,200 crores annually on bitcoin trading. CEIB has also suggested that Bitcoin be categorized as an 'intangible assets' by which GST could be imposed on all the transactions. It was also added that cryptocurrency could be treated as current assets and GST be charged on the margins made when traded. The CBIC is still reflecting upon a proposal that is yet to be put forth the GST Council. The key points presented included definition of Cryptocurrency 'mining' and how it will be treated as a supply of service since it generates cryptocurrency and involves rewards and transaction fees. Tax will be collected from the miner on transaction fees or reward. If the value of the reward exceeds ₹ 20 lakh, individual miners will need to register themselves under the Goods and Services Tax (GST). The proposal also considers 'wallets' storing keys taxable. Wallet service providers should be registered under GST. Cryptocurrency exchanges need to register and pay tax on their earning. Trading may attract 18 percent GST. Buying and selling of crypto currencies will be considered under the category of supply of goods. Other related facilitating transactions will be counted under services and these would include supply, transfer, storage, accounting, among others. The transaction value in rupees or the equivalent of any freely convertible foreign currency will be used to determine the value of cryptocurrency. In a scenario where both buyer and seller are in India, a transaction would be treated, as a supply of software and the buyer's location will be the place of supply. For transfer and sale, the location of the registered person will be the place of supply. However, in a scenario where sale has to be made to non-registered persons, the location of the supplier would be considered as the place of supply. Integrated GST would be applicable for transactions conducted beyond the Indian territory and would be considered as import or export of goods. IGST will be levied on cross-border supplies.<sup>36</sup>

There is a debate regarding the classification of VDAs as a good or services however, it can be concluded there is a good chance that GST would become applicable on cryptocurrency and

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<sup>36</sup> Aporna Dasgupta, GST on Cryptocurrency< [https://www.taxmanagementindia.com/visitor/detail\\_article](https://www.taxmanagementindia.com/visitor/detail_article)>, Tax Management India, 2021, accessed 7 November 2022

perhaps also on the mining services. But no stated rules and regulations with regard to cryptocurrency and the precipitous speed at which the blockchain technology is growing, it is high time taxation and regulatory principles are brought in to stabilize the current situation and clear off all the grey areas.<sup>37</sup>

With the proliferation of cryptocurrencies, the concept of money is evolving at a rapid speed. While this evolution poses several pertinent threats, it also offers many valuable opportunities. Most of the challenges associated with cryptocurrencies can be effectively addressed by designing an appropriate regulatory framework. The taxation framework should thus be designed such that taxes do not factor into investment or business decisions. They should not be designed to disproportionately encourage or deter activity in this space. Their sole aim should be to earn revenue, without stifling innovation and development of the ecosystem. With this aim in mind, it is suggested that an assessment should be conducted on whether cryptocurrencies qualify as “goods” or “money” under the GST framework and the issue should be clarified. If it is concluded that they constitute “goods”, then an amendment should be made to the GST law specifically including cryptocurrencies to the definition of goods.

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## **VDA TAXATION POLICIES AROUND THE GLOBE**

Cryptocurrency transactions defined and taxed differently in many countries like Canada, USA, Germany, UK, and Australia. In June 2014, Canada is the first country in the world to establish a tax on virtual currencies. The Bank of Canada has expressed a willingness to acknowledge the developing virtual currency market, but currently recognizes cryptocurrencies as investments. Other countries, specifically, within the developed world, have adopted various tactics to the taxation of VDA. Their method seems to be predicated on how they classify VDAs.

Certain nations consisting of the U.S. Recall cryptocurrencies to be assets and tax profits derived from transfers. The fair price for the purposes of figuring out such profits is the fee at which the cryptocurrency turned into buying and selling on the trade while the transaction was finished. In Canada and the United Kingdom, despite the fact that the two countries classify cryptocurrencies in a different way (as commodities and capital assets, respectively), they'll be challenge to both income tax and capital profits tax relying on the relevant statistics and circumstances – example, whether the cryptocurrency changed into obtained through professional mining or interest mining).<sup>38</sup>

As NFTs are nonetheless a fairly new concept, many developed countries have not begun to formulate unique coverage for his or her taxation. At present, maximum evolved international locations, apart from Malta, appear to tax NFTs inside the equal way as cryptocurrencies. Malta has created a framework for DLT belongings — which it categorizes as coins and tokens — and taxes cash within the same way as fiat currencies and levies profits tax on returns earned from monetary tokens.

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<sup>38</sup> Shehnaz Ahmed and Swarna Sengupta, “Blueprint of a Law regulating for regulating Cryptoassets” (January 2022) available at <https://vidhilegalpolicy.in/research/blueprint-of-a-law-regulating-cryptoassets/>, accessed on 3November 2022

## **WAY FORWARD**

The authorities has brought a simplified regime of levying a excessive, but widespread fee of tax on all kinds of transactions. Within the brief time period, a simple tax mechanism will probably assist in lowering ambiguity and providing fact to taxpayers. However, inside the longer run adopting a widespread price may additionally disrupt the cryptocurrency industry as a high tax rate could be relevant on every switch thereby substantially increasing the tax price.<sup>39</sup>

Additionally, from 01 July 2022 onwards, any man or woman paying consideration to a resident of India in change for Cryptocurrency will be obligated to withhold tax on the charge of one per cent at the consideration so paid, issue to positive financial thresholds. The applicability of such withholding tax on every transaction will have a sizable unfavorable impact on the liquidity within the cryptocurrency ecosystem and discourage innovation in that space. In which the consideration payable is absolutely or partially in-kind, the payer ought to make certain that tax is paid in recognize of such transaction, before paying the consideration. Implementing this will be tough and might result in the payer being held in default. Hence, from a withholding tax compliance attitude, there may be positive practical challenges, in particular for investors of cryptocurrency, which includes maintaining a report of the identification or tax residence of sellers and so on. A withholding tax mechanism also does not serve any significant reason for the tax government because it does not add to the treasury's sales, as an alternative it most effective will increase administrative fee. Such an hard requirement could be argued to theoretically help the authorities with obtaining statistics approximately transfers of cryptocurrencies but given that any such mechanism is almost not possible to implement at a peer-to-peer degree.<sup>40</sup>

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<sup>39</sup> Vidushi Gupta, Yeeshya Shriyan, Aashima Sawhney, Taxing Cryptocurrencies: The concept, the challenges and the required changes, 2022, VIDHI Centre For Legal Policy, <[https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527\\_WP\\_Taxing-Cryptocurrencies\\_VCLP.pdf](https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527_WP_Taxing-Cryptocurrencies_VCLP.pdf)>, accessed on 02 November, 2022

<sup>40</sup> Vidushi Gupta, Yeeshya Shriyan, Aashima Sawhney, Taxing Cryptocurrencies: The concept, the challenges and the required changes, 2022, VIDHI Centre For Legal Policy, <[https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527\\_WP\\_Taxing-Cryptocurrencies\\_VCLP.pdf](https://vidhilegalpolicy.in/wp-content/uploads/2022/05/20220527_WP_Taxing-Cryptocurrencies_VCLP.pdf)>, accessed on 02 November, 2022





## **CONCLUSION**

The brand new taxation regime delivered by using the authorities does not appear to recollect the nuances of cryptocurrencies and NFTs. Prior to the modification of the earnings Tax Act, experts in India and someplace else had raised questions as to how cryptocurrencies and NFTs have to be categorized – capital property, foreign money, securities, etc. An analysis of the character of every class of VDAs is vital to the formula of a clear and powerful tax regime.

At present, the earnings Tax Act treats cryptocurrencies, NFTs and other VDAs homogeneously. Whilst both cryptocurrencies and NFTs use DLT and blockchain technology, the similarities cease there. Cryptocurrencies are, through their very nature, fungible whilst NFTs aren't. Cryptocurrencies have restrained utility. NFTs, then again, can be deployed in some of approaches – as artwork, instruments, certificate of possession, and so on.

The fact that the income Tax Act does no longer deal with the traits of VDAs and how they may be acquired and utilized could lead to confusion. Illustratively, if cryptocurrency is acquired thru mining, is it considered to had been transferred to the recipient and, therefore, situation to the 30% tax? Instead, is it considered a receipt of a VDA without attention making the honest marketplace cost of that VDA taxable within the hands of the miner? At the same time as experts have differing views on how the receipt of VDAs pursuant to mining may be taxed, the fact remains that the law does no longer deal with or make clear the placement.<sup>41</sup>

The brand new taxes imposed on VDAs appear like geared toward discouraging funding in such belongings. The tax price of 30% – relevant no matter the income bracket of the taxpayer – is similar to that imposed on different belongings of which the authorities seems to disapprove consisting of lottery winnings. The refusal to permit any deductions other than fee of acquisition, or to permit the set-off of losses, and the requirement to deduct tax are in addition evidence of the purpose to deter investments in VDAs.

The government has not prescribed the way wherein VDAs should be valued regardless of linking the imposition of tax in positive cases to the truthful marketplace price of the applicable

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<sup>41</sup> Shehnaz Ahmed and Swarna Sengupta, “Blueprint of a Law regulating for regulating Cryptoassets” (January 2022) available at <https://vidhilegalpolicy.in/research/blueprint-of-a-law-regulating-cryptoassets/>, accessed on 3November 2022

asset. This may invariably cause disputes and further lessen religion inside the Indian tax regime.

In the end, the choice to tax VDAs isn't indicative of the legalization of cryptocurrencies or NFTs in India. In India, assets acquired via the proceeds of crime are problem to tax. In addition, belongings received in an unlawful style (benami assets or undisclosed overseas assets) also are taxed. The mere incidence of taxation can't be interpreted as legitimization or legalization of VDAs.

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