

**Proposed amendment on taxation of
crypto-currencies
- Issues & approaches**

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————— CHARTERED ACCOUNTANTS —————

Cryptocurrency and its Indian Regulatory Journey

Crypto-tech Industry in India

Crypto-tech industry to grow to **\$241 million** in India by 2030

The crypto-tech market in India has the potential to create over **800,000 jobs**

The **economic value-add of \$184 billion** by 2030 in the form of investments and cost savings

Over **230 startups** are already operating in India in the cryptotech space

India has the highest number of crypto owners in the world at **10.07 crore**

What is Cryptocurrency

Digital or Virtual Currency

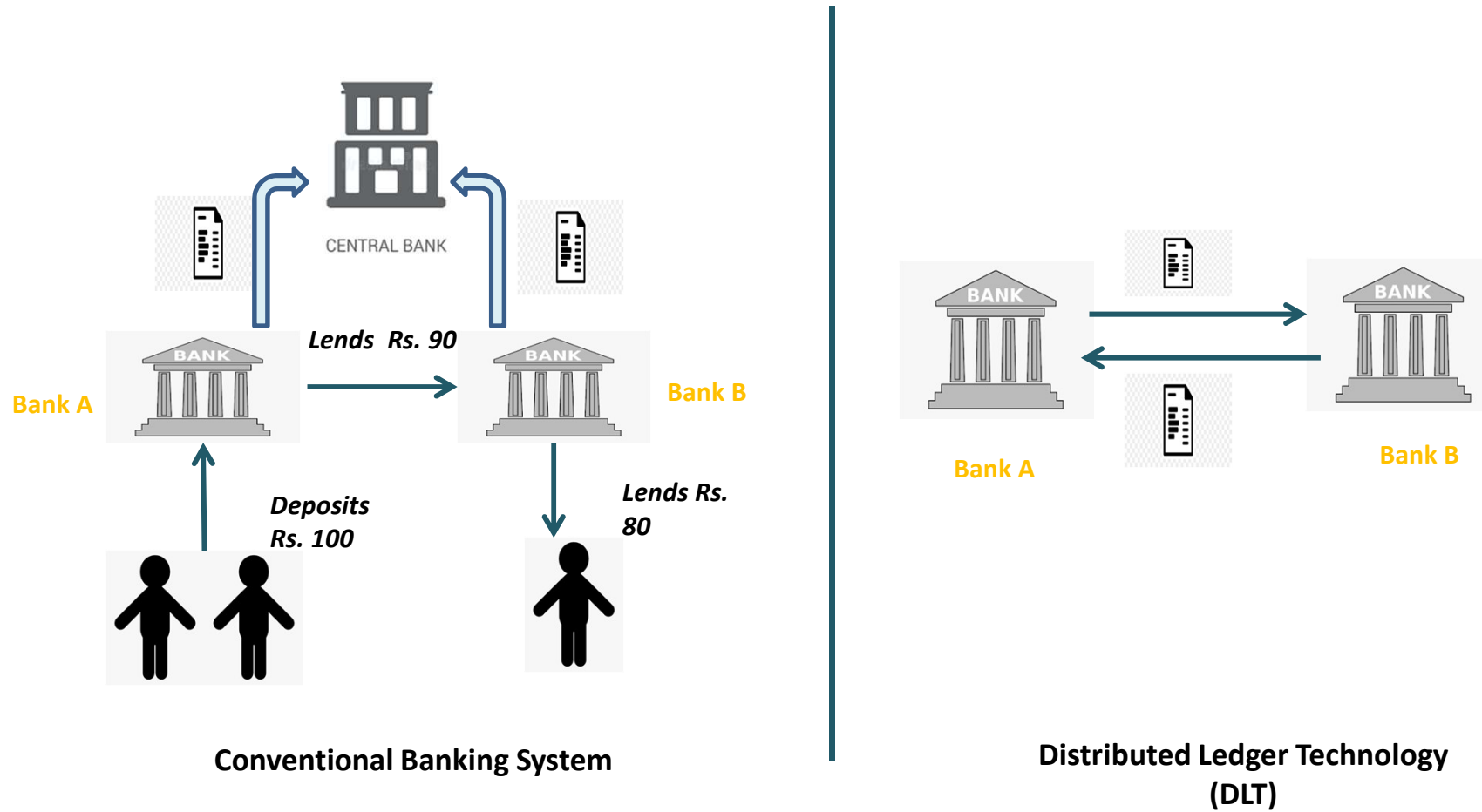
Secured by cryptography means

Based on a network that is distributed across a large number of computers. (Distributed Ledger Technology)

Not issued by Central Authority

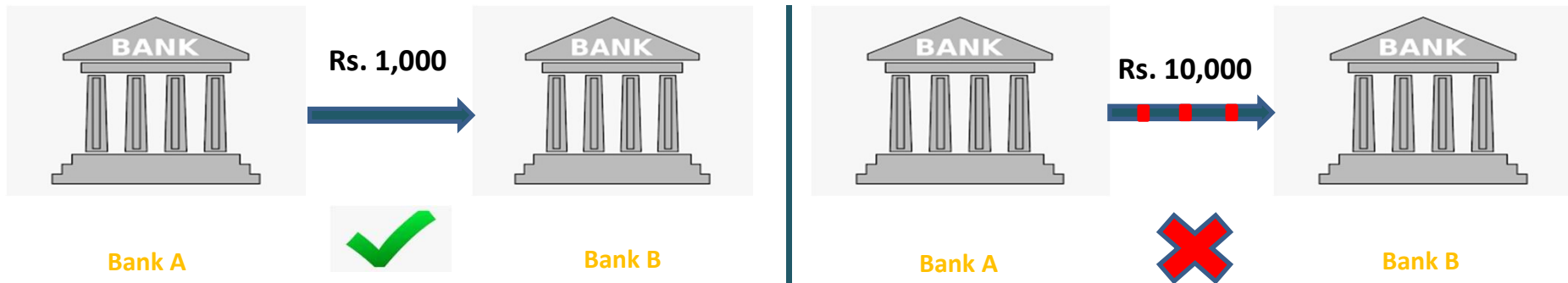
Based on block chain technology

Overview : Distributed Ledger Technology



Cryptography

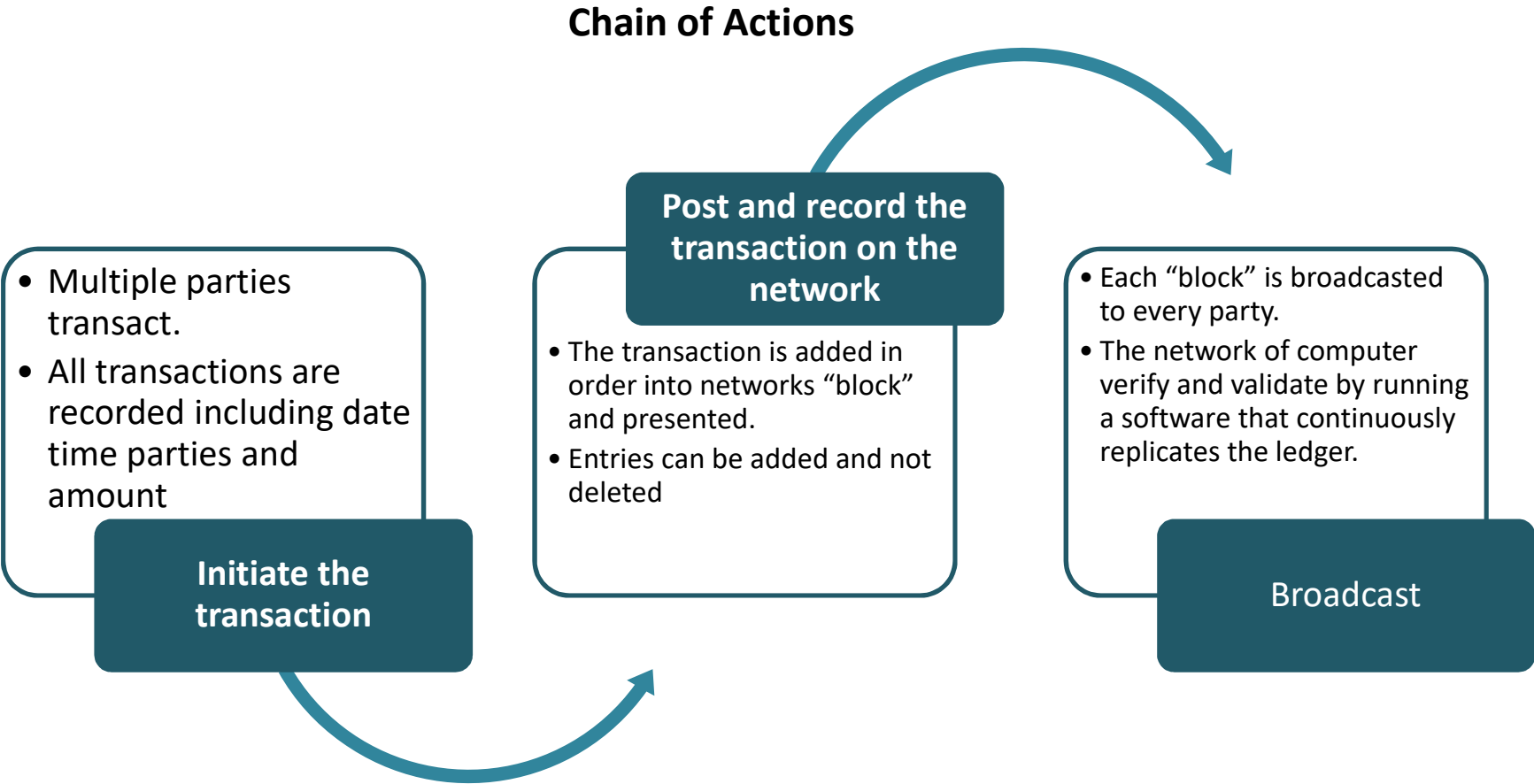
Bank A intends to transfer Rs. 1,000 to Bank B



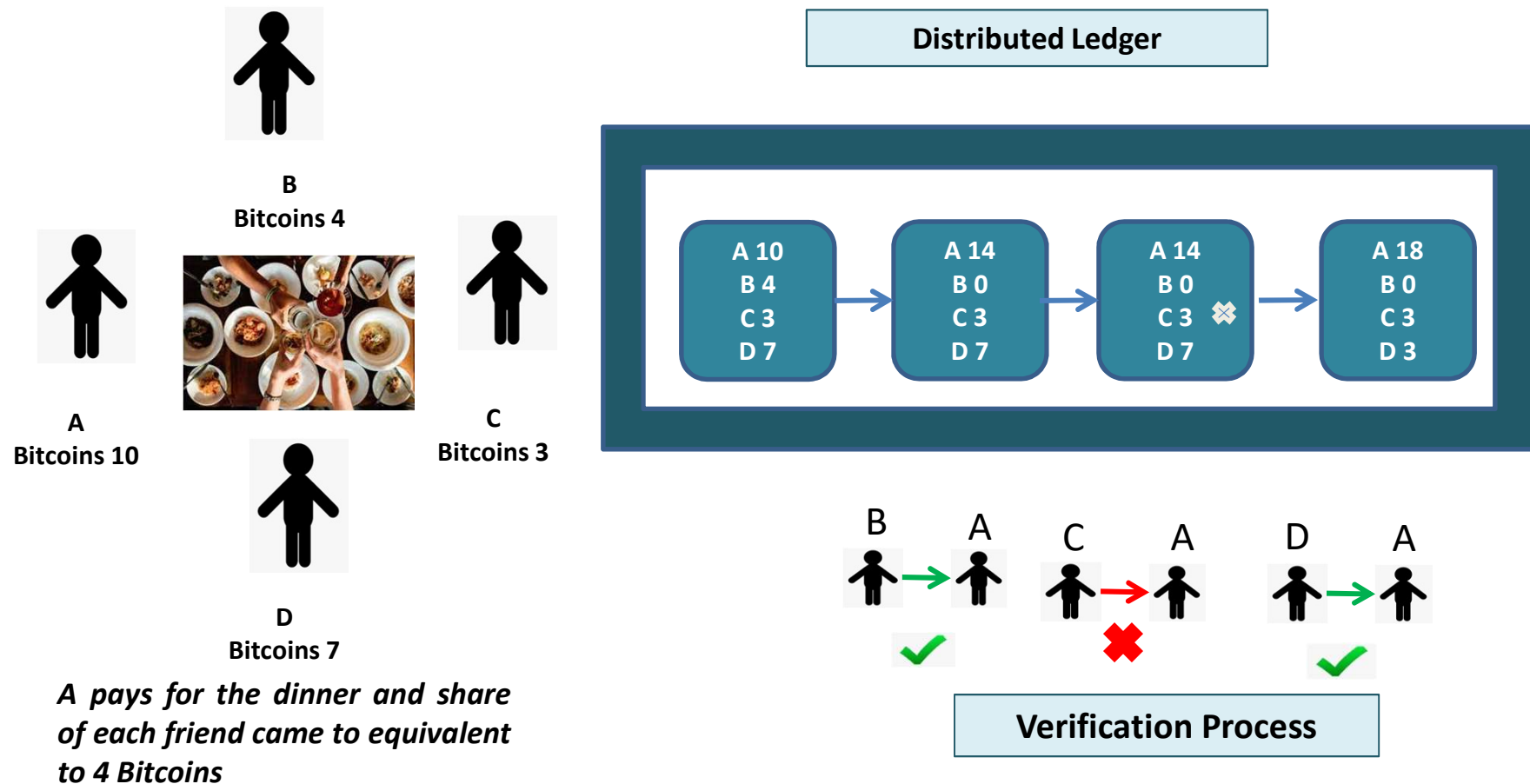
Bank A : Public Key : <<yxbxjwjw8192n>>
Bank B : Public Key : <<klnsksnlknkiwik>>
Private Key generated by Bank B :
<<janjnnlnceiiej>>

Bank A : Public Key : <<2632@@@xjbj>>
Bank B : Public Key : <<hbwxh87182gbs>>
Private Key generated by Bank B :
<<vhxvhw42633o0>>

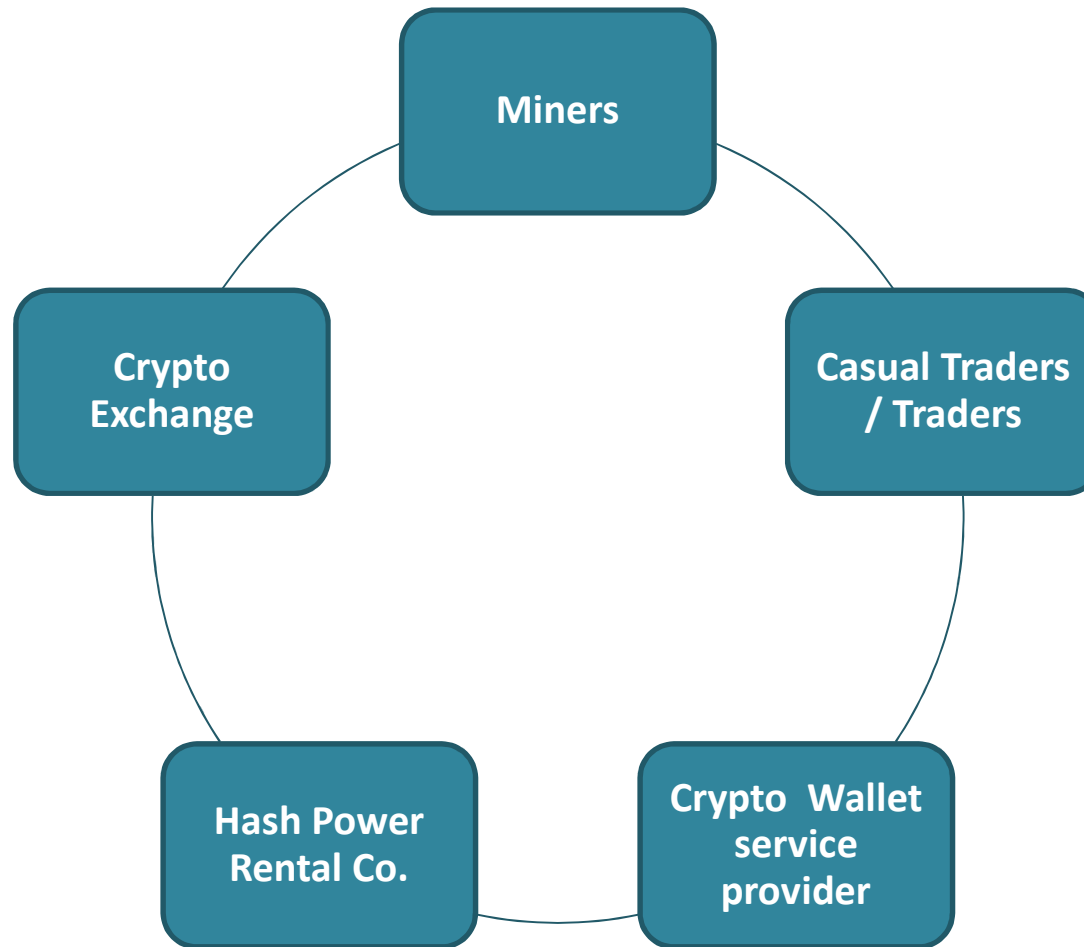
Brief on Blockchain Technology



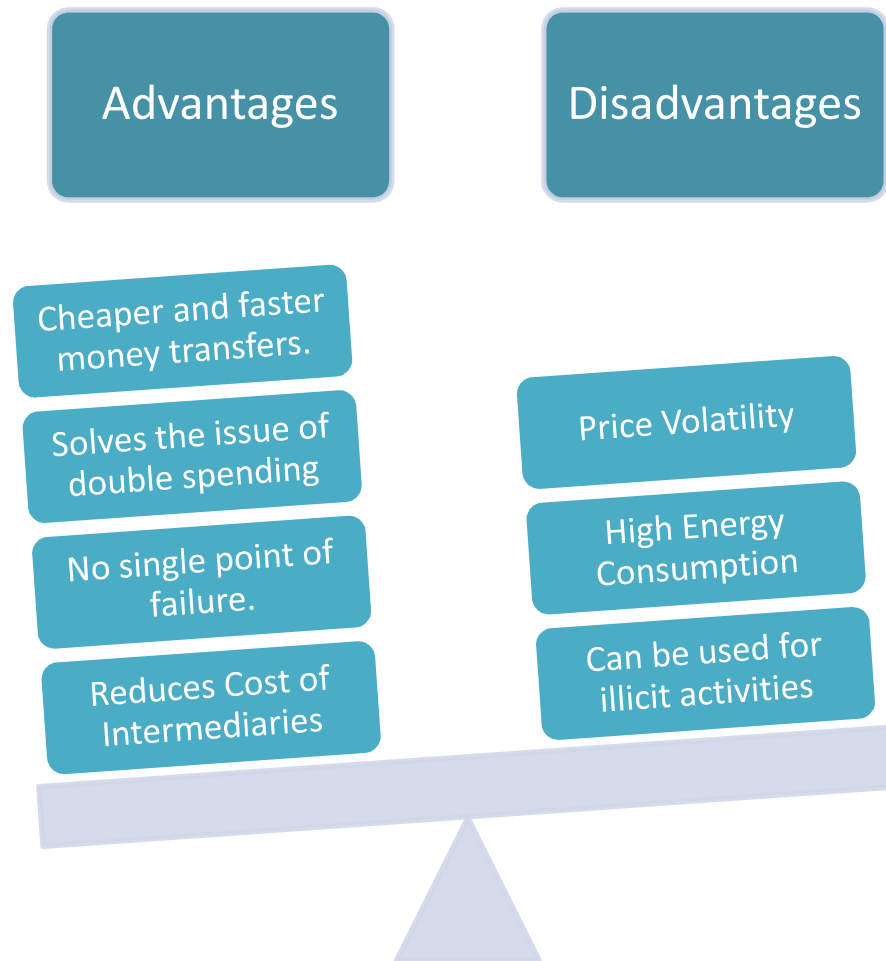
Blockchain Technology – Example



The Participants in the Crypto-Currency Ecosystem



Pros and Cons of Cryptocurrency



What is Non-Fungible Token

Non Fungible Tokens

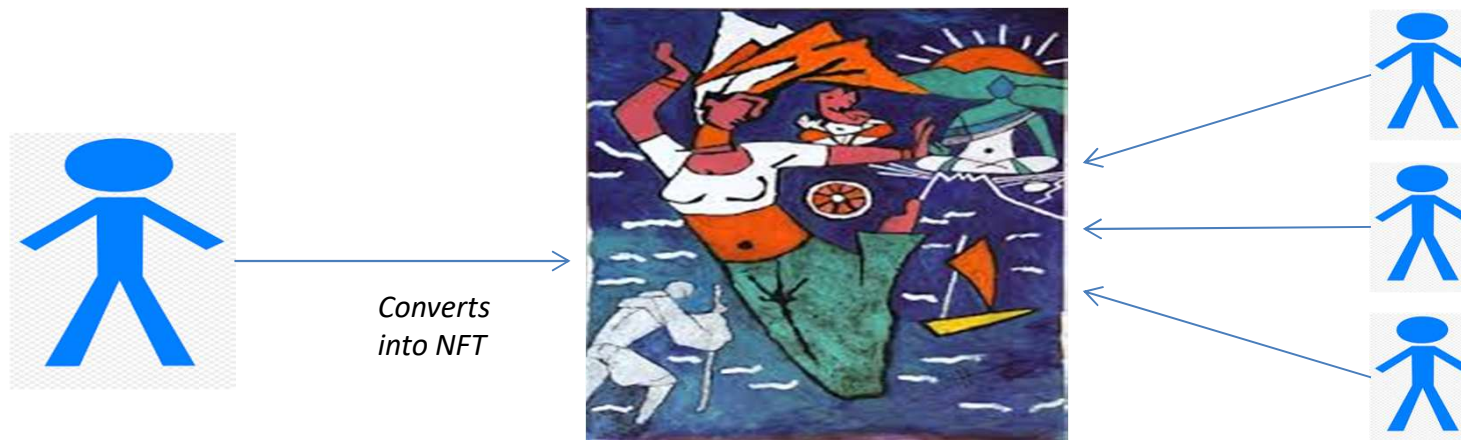
NFTs are **unique cryptographic tokens** that exist on a blockchain and cannot be replicated.

NFTs can represent real-world items like artwork and real estate. NFT can **digitally represent any asset**, including online-only assets like digital artwork and real assets such as real estate.

"Tokenizing" these real-world tangible assets makes buying, selling, and trading them more efficient while reducing the probability of fraud.

NFTs can also function to represent individuals' identities, **property rights**, and more.

Example of NFT



- Suppose, painting by MF Husain is converted in the NFT
- Desirous people buys NFT of the Painting
- May get access rights and / or excess profits in the painting

Digital Assets, *technically..*

Cryptocurrency

- The word “Cryptocurrency” is derived from encryption techniques which is used to secure network. It is a digital currency used over internet to purchase goods or services or traded for profit. It is created using technology called Blockchain. Blockchain is a decentralized technology spread across many computers that manage and records transactions.
- It started in 2009 with introduction of Bitcoin.

Non Fungible Token (NFT)

- NFT is a digital certificate representing the ownership or rights with respect to an indivisible asset (either in the physical or intangible form). NFTs can act as a digital twin to a physical asset. Digital offering of the products with limited editions drive demand due to scarcity.
- NFT works on block chain as it gives users complete ownership of a digital asset. For instance, if you’re a sketch artist, and if you convert your digital asset to an NFT, what you get is proof of ownership, powered by Blockchain

Cryptocurrencies – Indian Experience

(1/2)

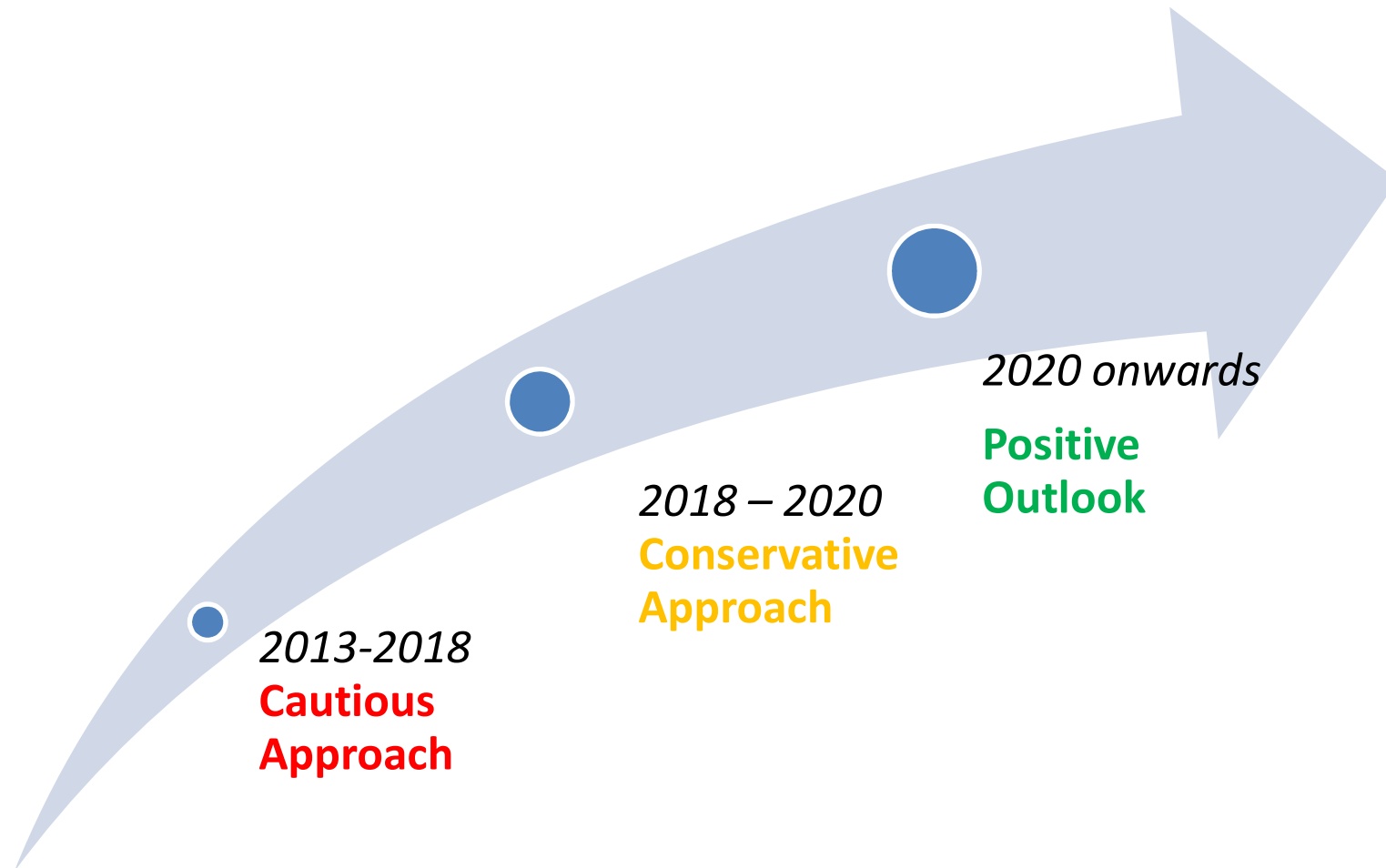
Year	Regulatory Framework
2013	The RBI vide Press Release dated 24 December 2013 cautioned the users about the risks associated with virtual currencies, including money laundering, consumer protection, market integrity, cybersecurity and volatility.
2017	Two cautionary press releases were made on February 1, 2017 and December 5, 2017, respectively, through which RBI reiterated the risks and clarified that it has not given any license or authorization to any entity or company to operate schemes or deal with Bitcoin or any other VCs.
2018	The RBI issued Circular which prohibited entities regulated by RBI from dealing in virtual currency.
2019	In February 2019 the committee proposed a fresh draft bill that recommended a blanket ban.

Cryptocurrencies – Indian Experience

(2/2)

Year	Regulatory Framework
2020	Hon'ble Supreme Court on March 4, 2020 in Internet and Mobile Association of India V. Reserve Bank of India , lifted the ban imposed by the RBI Circular. The court predominantly examined the matter from the perspective of Article 19(1)(g) of the Indian Constitution, which is the freedom to practice any profession, or to carry on any occupation, trade or business, and the doctrine of proportionality.
2021	On March 24, 2021, the Ministry of Corporate Affairs released a notification ('MCA Notification') mandating companies to inter-alia make certain disclosures with respect to the virtual currency/ cryptocurrency transactions undertaken by them during a financial year.
Present	Parliament has intention of introducing the Cryptocurrency and Regulation of Official Digital Currency Bill, 2021 for deliberations. The objective of the Bill is to create an enabling framework for the official digital currency to be issued by the RBI, and to prohibit all private cryptocurrencies available in India.

Approach of Government towards Crypto Assets



Taxation of Digital Assets

Taxable Events

Creation of Cryptocurrencies

- ***Mining***

It refers to confirming and verifying the transaction that takes place on block chain and for such verification / confirmation, cryptocurrency is issued to the miners as an incentive.

- ***Initial token / coin offering***

Tokens / Coins issued by companies developing new block chain protocols to raise money or funds for their project. These tokens / coins are issued in exchange of cash or any other existing cryptocurrency.

- ***Airdrops***

Distribution of tokens / coins free by new companies in crypto space. These are usually distributed to famous people so that more awareness is generated about new token / coin.

Secondary Sale of Cryptocurrencies

- ***Trading***

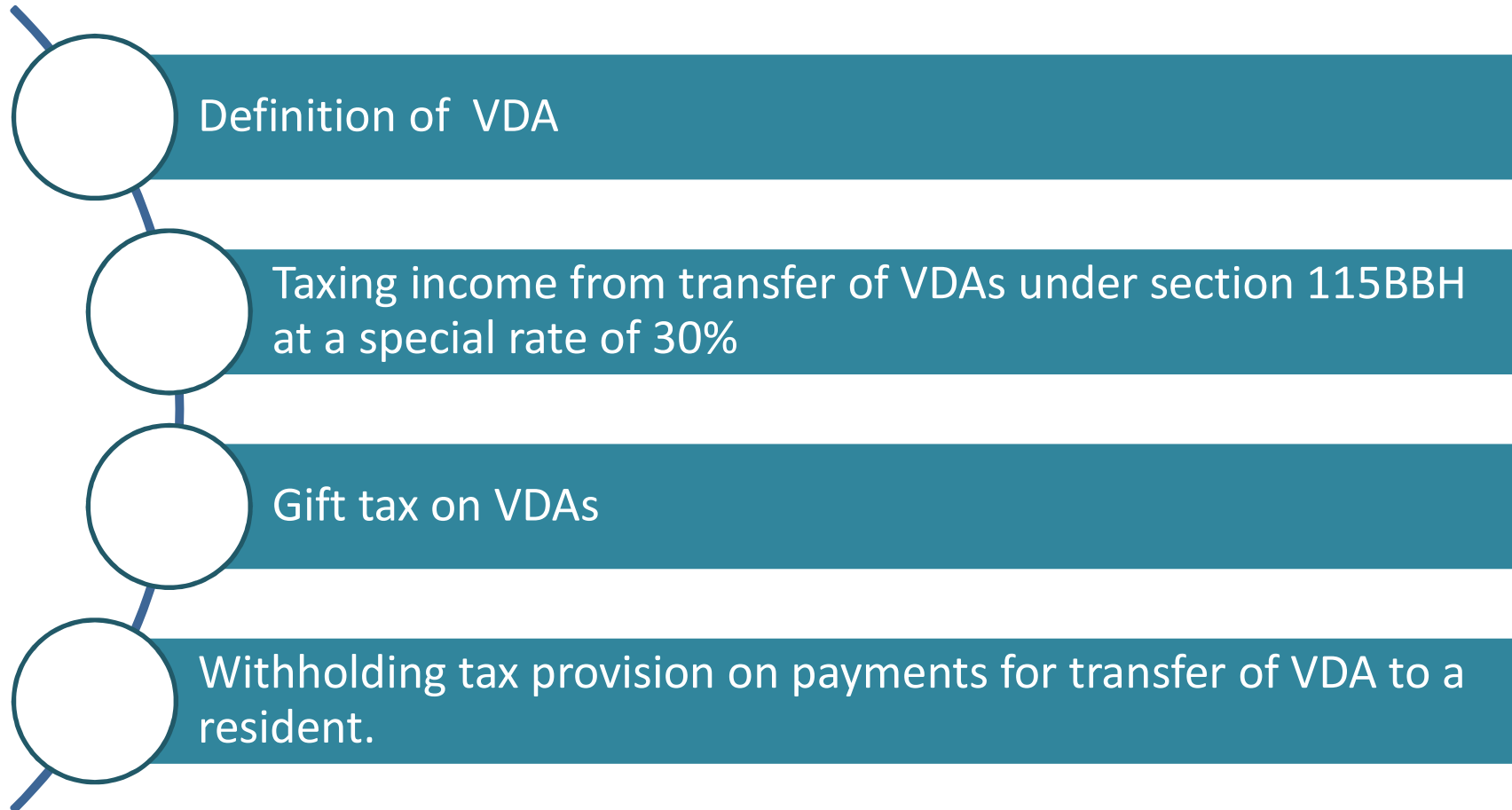
Acquiring cryptocurrencies online through cryptocurrency exchange or in a wallet.

- ***Exchange of goods / services***

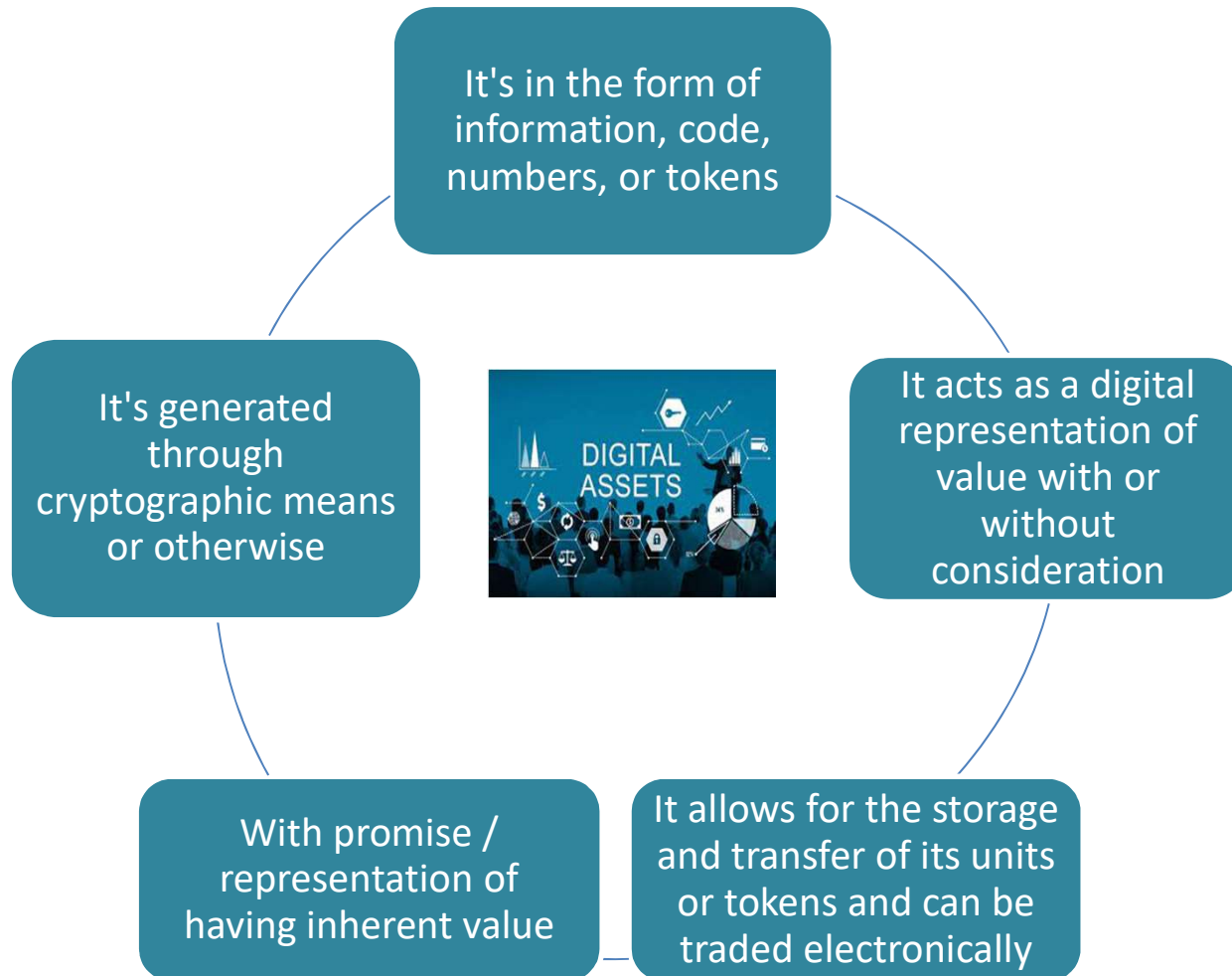
Where goods and services are exchanged for cryptocurrencies.

Proposals by Finance Bill, 2022 (Virtual Digital Asset)

Taxation of VDA



Meaning of Virtual Digital Asset (“VDA”)



Meaning of Virtual Digital Asset (“VDA”)

Government issued digital currencies, both Indian and foreign, have been specifically excluded from the scope of virtual digital assets

NFTs have been included within the scope of virtual digital assets and it means such digital asset as the Government in the Official Gazette specifies.

Government is empowered to identify digital assets that would be included within the scope of the term ‘virtual digital assets’

Issues in relation to definition of VDA

Broad Definition of VDA

- Whether the choice of wide term is intentional to cover other assets like digital gift cards, loyalty cards etc. or it is just an interpretational doubt.
- NFTs are included in the definition VDA and shall be treated at par with cryptocurrency. NFTs are collectible and have notional value. This asset class requires nuanced tax structure as they are unique.

Taxation of Cryptocurrency

Classification of Virtual Digital Asset

Nature of VDA

- It has not been clarified if VDA will be currency, commodity or security
- In the absence of any such clarification, the VDA should be classified as a capital asset.

S. 2(14)

- In view of Section 2(14) of the Income-tax Act, a capital asset means property of any kind held by a person, whether or not connected with his business or profession
- The term 'property' has no statutory meaning, yet it signifies every possible interest that a person can acquire, hold, or enjoy.

Capital Gains /Business Income

- Cryptocurrencies or NFTs should be deemed capital assets, if purchased for investments by the taxpayers. Gain arising on the transfer of such assets shall be taxable as capital gains.
- However, if the transactions in such assets are substantial and frequent, it should be held that the taxpayer is trading in such assets. In this case, income from the sale of such assets should be taxable as business income.

Taxation under the Head Capital Gains

Provisions under Section 115BBH

<p>Nature of VDA</p>	<p>If gains arising from the transfer of virtual digital assets are treated as capital gains, their further classification into short-term or long-term gains would depend upon the period of holding of such assets. If a virtual asset is held for more than 36 months from the date of purchase, it will be considered a long-term capital asset; otherwise a short-term capital asset.</p>
<p>No deduction to be allowed</p>	<p>While computing the short-term or long-term capital gains, except the cost of acquisition, if any no other deduction or exemption shall be allowed. Thus, the following items shall be ignored while computing the capital gains from the transfer of virtual digital assets:</p> <ul style="list-style-type: none"> • Expenditure incurred in connection with the transfer of a virtual digital asset; • Cost of improvement relating to a virtual digital asset; • Indexation of cost of acquisition of a virtual digital asset; • Exemption under Section 54F
<p>Tax Rate</p>	<p>The income arising from the transfer of virtual digital assets shall be taxed at the rate of 30%. Thus, short-term and long-term capital gains both shall be taxed at a flat rate of 30%. Further, no deduction under Chapter VI-A or an exemption under Section 54F shall be allowed from such capital gains. However, relief under Section 87A can be claimed.</p> <p>Now, Section 115BBH contains a non-obstante clause (The Finance Bill as passed by Lok Sabha on 25.03.2022) . Thus, it overrides all other provisions of this Act. However, the non-obstante clause was missing could lead to an argument that it does not override other provisions of the Act. The tax rate (30%) provided under section 115BBH(1) may not apply in the case where the lower tax rate is provided under any other section of the Act</p>

Computation of capital gains

The capital gains from the sale of virtual digital assets shall be computed in the following manner:

Particulars	Amount
Full value of consideration	XXX
Less : Cost of Acquisition, if any	(XXX)
Long-term capital gains/Short-term capital gains	XXX

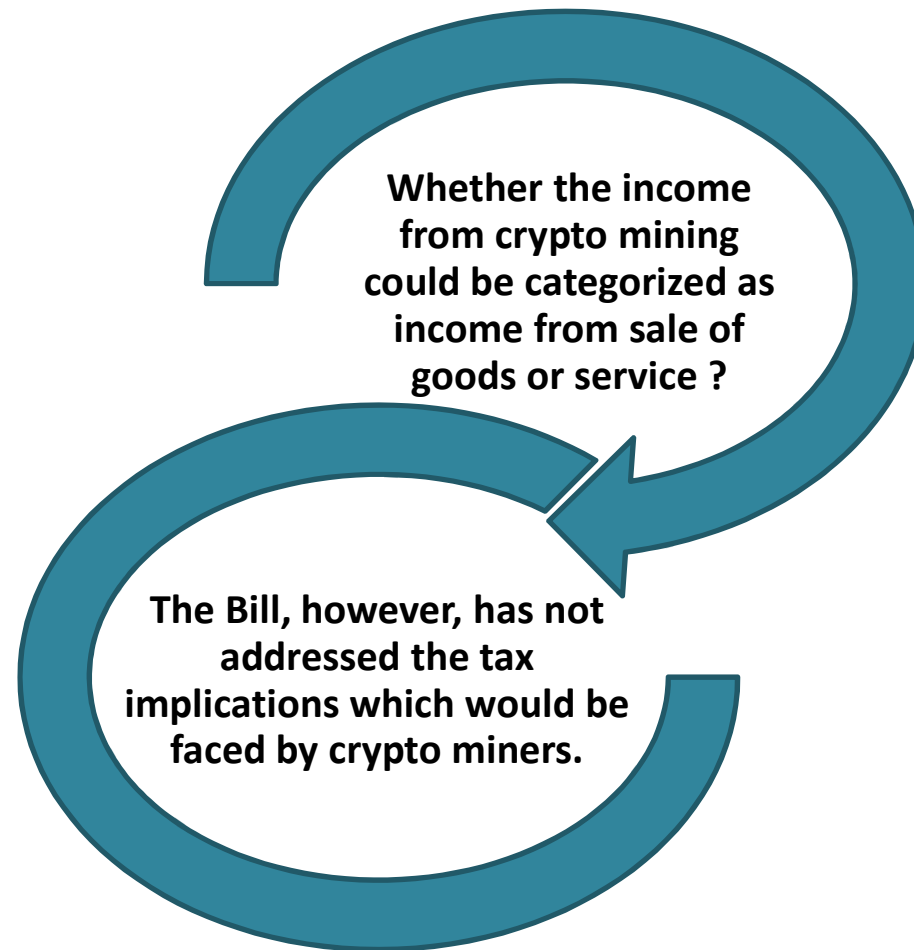
Sales consideration and Cost of Acquisition are not defined in the tax proposals

Taxation under the Business Income

Provisions under Section 115BBH

- If the transactions in virtual digital assets are substantial and frequent, it should be held that the taxpayer is trading in such assets.
- In this case, income from the sale of such assets should be taxable as business income.
- The gains (without deduction of any expense or allowance) shall be taxable at the flat rate of 30%
- Definition of 'transfer' shall apply even if VDA is not held as a capital asset. The Finance Bill (as passed by Lok Sabha on 25.03.2022) has inserted sub-section (3) under section 115BBH to provide that the definition of transfer shall apply to any VDA, whether held as a capital asset or not.

Taxation for Crypto Miners



Treatment of Losses

No set-off of any loss shall be allowed to the assessee in computing the income arising from transfer of any VDA



No set off of loss from transfer of the virtual digital asset shall be allowed against income computed under any **other** provision of this Act to the assessee and such loss shall not be allowed to be carried forward to succeeding assessment years.



Any loss arising from the transfer of VDA would be a dead loss. It will not be allowed to be adjusted against income arising from the transfer of another VDA (whether of the same category or not).

Illustration

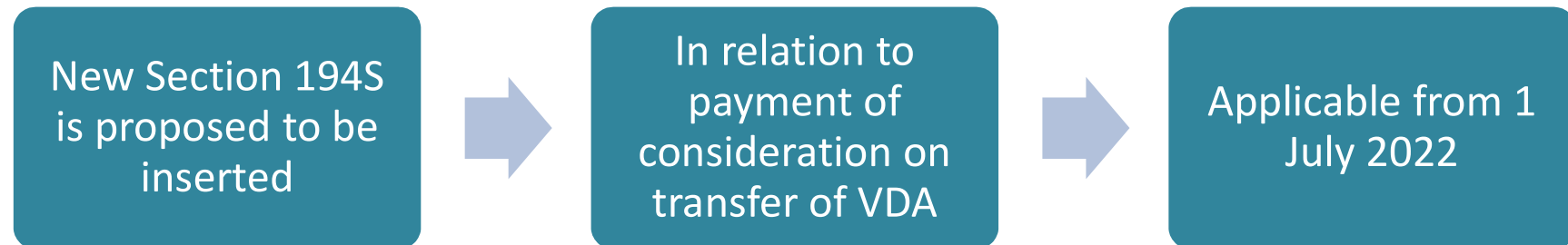
Ram purchased 1,000 Bitcoins at Rs. 1,000 each on 12 August 2020. He transferred all the Bitcoins in the previous year 2022-23. The capital gains from the transfer of Bitcoins shall be computed as under:

Units (A)	Sold on (B)	Consideration (C)	Brokerage (D)	Cost of Acquisition (E)	Taxable Profit / Loss (C- E)
1000	18 April 2022	5,00,000	1000	10,00,000	(5,00,000)
1000	18 March 2023	16,00,000	1500	10,00,000	6,00,000

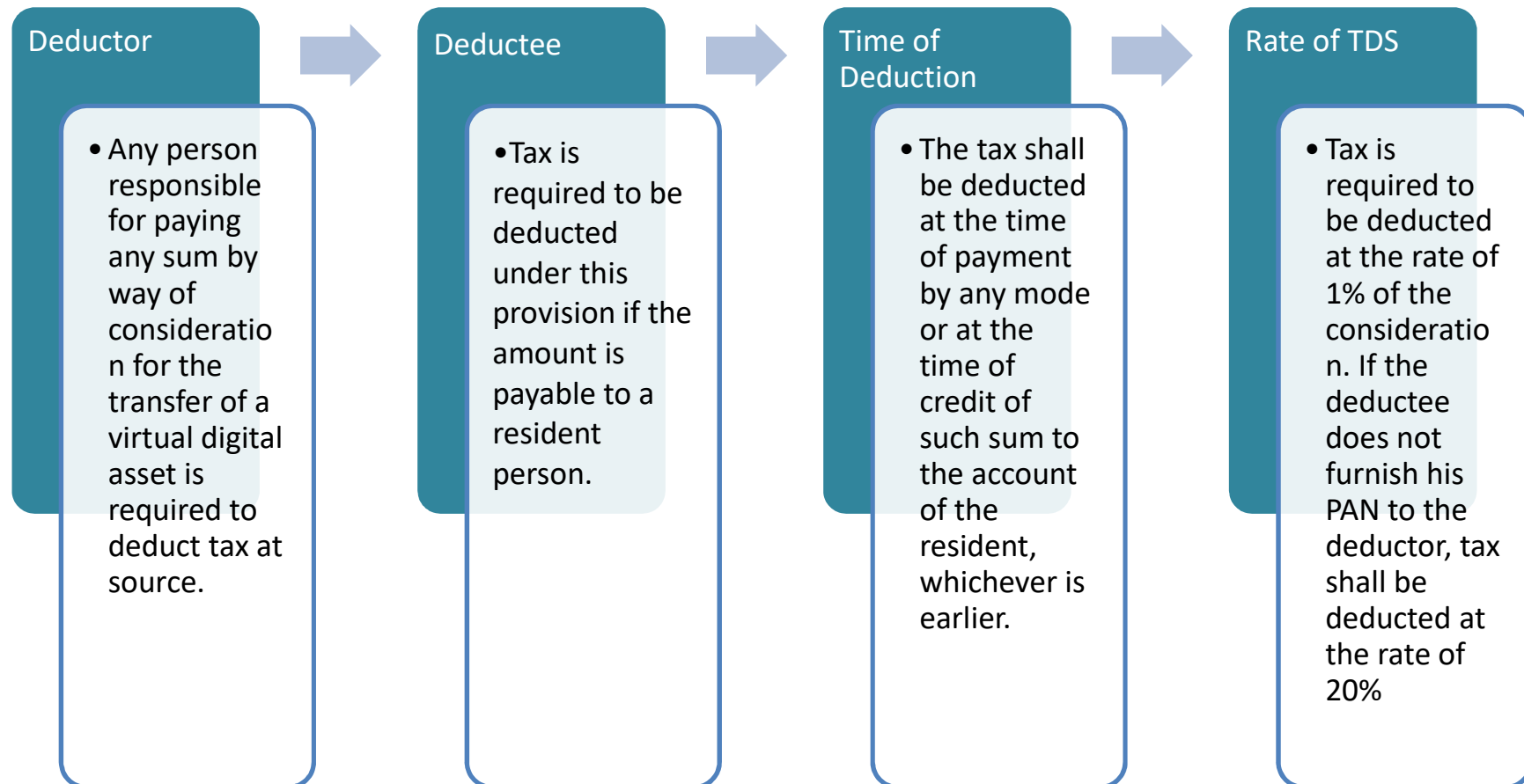
- Sales consideration less cost of acquisition shall be taxable. No deduction shall be allowed for brokerage.
- Loss of Rs. 500,000 on sale bitcoins cannot be set off against any other income including gains from sale of bitcoins.
- Such loss cannot be carried forward to subsequent years

Deduction of Tax at Source

Deduction of Tax at Source [Section 194S]



Requirements under Section 194S



Liability to deduct tax – Point to Ponder

- Typically, crypto currencies are purchased/sold on a crypto exchange (which may or may not be in India).
- In most cases, buyers and sellers do not know each other since the transaction is facilitated by the exchange directly.
- **Accordingly, in such situation whether tax is to be deducted at source by the crypto exchange?**

Requirements under Section 194S

Amount on which tax is to be deducted - Tax is required to be deducted from the gross amount of consideration paid to the resident person for the transfer of virtual digital assets.

However, in the following cases, before releasing the consideration, the person responsible shall ensure that tax **required to be deducted** has been paid in respect of such consideration for the transfer of virtual digital asset:

- (a) Where consideration is wholly in kind;
- (b) Where a transaction is in exchange for another virtual digital asset, and there is no part in cash; or
- (c) Where consideration is partly in cash and partly in kind, but the part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of such transfer.

Exemption from deduction of tax at source

Threshold Limit	Exemption
Consideration is below Rs. 10,000	No tax shall be deducted under this provision if the consideration is payable by any person (other than a specified person) and its aggregate value does not exceed Rs. 10,000 during the financial year.
Consideration is below Rs. 50,000	<p>No tax shall be deducted under this provision if the consideration is payable by the following specified persons and its aggregate value does not exceed Rs. 50,000 during the financial year:</p> <ul style="list-style-type: none">▪ An individual or a HUF, whose total sales, gross receipts or turnover does not exceed Rs. 1 crore in case of business or Rs. 50 lakh in case of a profession, during the financial year immediately preceding the financial year in which such virtual digital asset is transferred;▪ An individual or a HUF who does not have any income under the head profits and gains of business or profession.

Some examples

Date of Sale or Exchange	Nature of transaction	Consideration	PAN of payee available	Payer is specified person	Applicability of TDS
01.03.2022	Cash	25,00,000	Yes	No	Not applicable
01.07.2022	Cash	8,000	Yes	No	Not applicable
01.07.2022	Cash	48,000	Yes	Yes	Not Applicable
01.07.2022	Cash	25,00,000	Yes	No	TDS @ 1%
01.07.2022	Cash	25,00,000	No	No	TDS @ 20% (S. 206AA)
01.07.2022	Property	25,00,000	Yes	No	Deductor to ensure that tax required to be deducted has been paid

Section 194S : Overriding effect

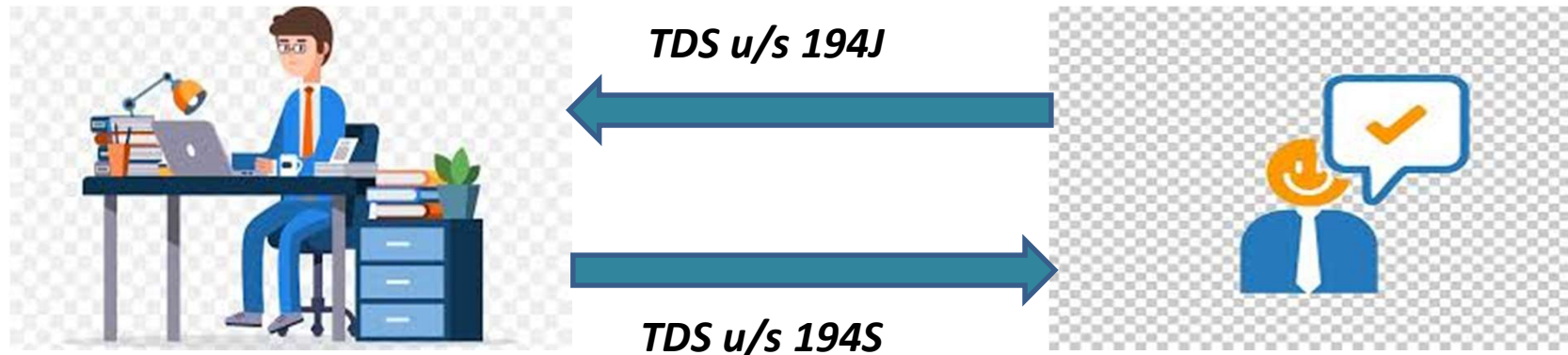
Overriding effect of provision

Where a transaction is subject to TDS under section 194-O and section 194S, tax shall be deducted under section 194S.

Amendments made in the Finance Bill as passed by the Lok Sabha

Omitted - a transaction in respect of which tax has been deducted under this provision, no tax shall be deducted or collected under any other provisions.

Provision of S. 194S vis a vis other TDS sections



CA providing professional services to a client

Client paying by means of **Bitcoins**

Giftng of Virtual Digital Asset

Scope of Section 56(2)(x)

- Section 56(2)(x) applies when any person **receives any benefit** whose value exceeds Rs. 50,000.
- This provision is applicable notwithstanding the residential status or class of assessee. The donor or donee can be an individual, partnership firm, LLP, company, AOP, BOI, co-operative society or artificial juridical person, whether resident or non-resident.
- The deemed income under this provision arises from the following transactions:
 - Receiving **monetary benefits** without consideration;
 - Receiving **immovable property** without consideration or for inadequate consideration; and
 - Receiving **specified movable properties** without consideration or for inadequate consideration.

Benefit arising from Movable Property

Deemed Income

- Where any property is received without consideration and the aggregate fair market value of which exceeds Rs. 50,000, the whole of the aggregate fair market value of such property will be chargeable to tax.
- Where any property is received for a consideration that is less than the aggregate fair market value of the property by an amount exceeding Rs. 50,000, the difference between fair market value and consideration is chargeable to tax.

Specified Movable Property

- In both the situations, the limit of Rs. 50,000 shall be checked for every transaction and not in aggregate of all transactions.
- This provision is applicable to any property in the nature of shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art, or bullion. Where the transaction involves any other movable property, excess of consideration over the fair market value shall not be chargeable to tax.

VDA – Movable Assets

- The Finance Bill, 2022 proposes to include virtual digital assets within the scope of movable assets.
- Thus, if a person receives a virtual digital asset without consideration (gift) or for inadequate consideration and the value of such benefit exceeds Rs. 50,000, it shall be taxable in the hands of the recipient under Section 56(2)(x) as income from other sources.

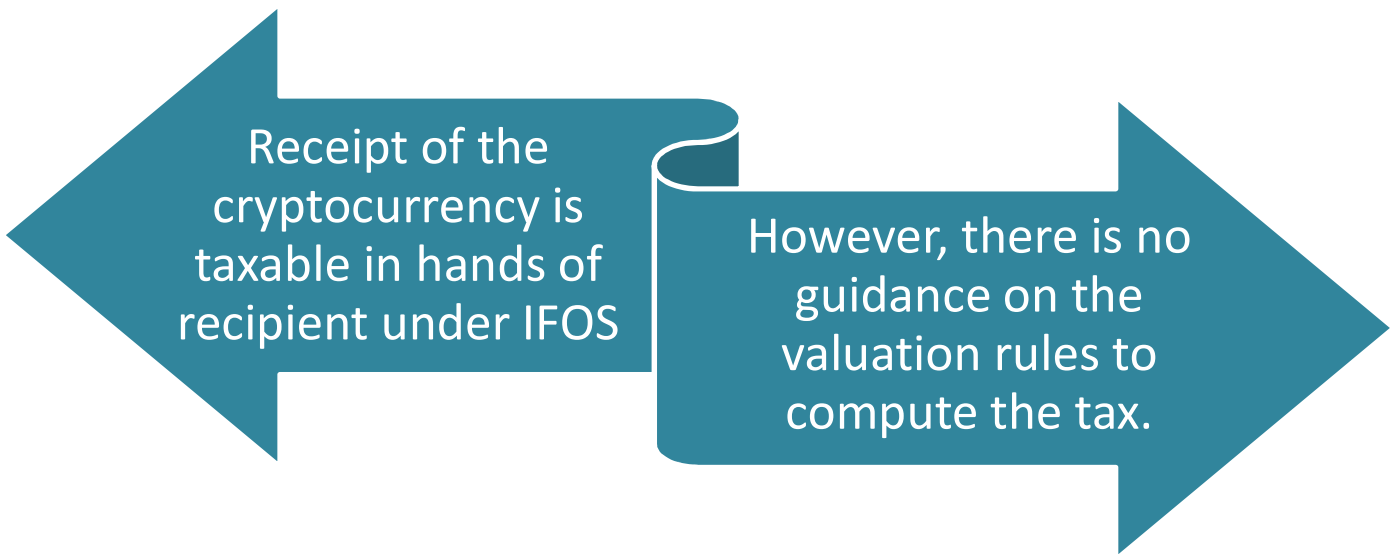
Tax Rates in case of Gift of VDA

The value of the benefit arising under this provision shall be taxed at the rate applicable to the assessee.

Such income shall not be taxed at 30% under Section 115BBH because it does not arise due to the transfer of a virtual digital asset.

However, when the recipient further transfers such assets, the resultant gains shall be taxable under Section 115BBH.

Absence of Valuation Rules



Receipt of the
cryptocurrency is
taxable in hands of
recipient under IFOS

However, there is no
guidance on the
valuation rules to
compute the tax.

Applicability of equalization levy

The Finance Act, 2020 had expanded the scope of EL to apply 2% EL on the amount of consideration received or receivable by an 'e-commerce operator' from 'e-commerce supply or services' made or provided or facilitated by or through it to :

- to a person resident in India
- to a non – resident in certain specified circumstances
- to a person who buys such goods or services or both using internet protocol address located in India. (collectively as “Specified Persons”)

Given the broad definition of e-commerce operator and e-commerce supply or services, it is possible that transactions in VDA by Indian users (especially buyers) on a foreign crypto exchange could be subject to EL. However, **the Finance Bill has not provided any clarity on applicability of EL on foreign crypto exchanges.**

Conclusion



Introduction and recognition of VDAs under the ITA is a **welcome move** for the industry.

Provides clarity on several open questions from an income-tax perspective

The policy intent for taxing income from VDAs similar to gambling transactions seems to stem from the **Government's discomfort on speculative activities relating to crypto-assets.**

There are several lacuna in regime and **further clarifications** in this regard may be useful



Thank You !