Research Paper

GYAN MANAGEMENT

AN INTERNATIONAL BI-ANNUAL REFEREED JOURNAL OF MANAGEMENT & TECHNOLOGY

Year 2024, Volume-18, Issue-1 (January - June)

ISSN 0974-7621 (Print)

# A study of the indian taxation system on cryptocurrency

Dr. Jyoti Arora[1] & Lakhwinder Kaur[2]

[1]Assistant Professor, GGDSD College, Kheri Gurna, India, csjyotidhillon@gmail.com
[2]Assistant Professor, Khalsa College (Amritsar) Of Technology & Business Studies, Mohali, India, Lakhwindersomal86@gmail.com

## ARTICLE INFO

***Key Words:*** *Taxation, Cryptocurrency, Crypto assets, Virtual Digital Assets*

## *ABSTRACT*

Cryptocurrencies are digital tokens that allow people to make payments directly to each other through an online system. Since it can be used to buy and sell items and has the ability to store value and increase in value, cryptocurrency is drawing the attention of a lot of investors. As to the nature of cryptocurrency, there are different sets of opinions as to whether it is a currency or a Commodity or Security. The Finance Act 2022 was the first law to recognize Virtual Digital Assets (VDAs) in India and introduced crypto taxes. Accordingly, the income generated from investment in cryptocurrency is subject to tax. The present paper studies the emerging cryptocurrency market in India and the provisions of prevailing income tax law in India related to the taxation of cryptocurrency.

## Introduction

Tax is a compulsory financial charge or some type of levy imposed upon a taxpayer by any government organization in order to fund government spending. Tax revenue serves as a prime source to fund public expenditures. The swift development in ICT has enabled the Govt. to identify new avenues to collect taxes such as the taxation of Cryptocurrency. Taking an inchoate step, the government for the first time has officially termed digital assets including crypto assets under "Virtual Digital Assets".

The most commonly known type of crypto asset is a cryptocurrency which is a digital currency and acts as the medium of exchange for exchange of products or services like fiat currency. Although the cryptocurrency market in India is presently unregulated, any profit/loss on transactions involving cryptocurrency typically gets

Received 12.06.2023; Accepted 01.08.2023
DOI: 10.48165/gmj.2023.18.1.5

covered under Income Tax Act, 1961. This paper aims to explore cryptocurrency and the prevailing tax regulations concerning the income from these assets.

## Meaning of cryptocurrency

Cryptocurrency is a decentralized and digital currency that uses encryption algorithms to verify transactions. It is a peer-to-peer system that operates as an alternative form to send and receive payments without any third-party intervention i.e. without relying on banks to verify transactions. These currencies run on blockchain technology which is based on a distributed public ledger where the record of all transactions is updated and held by currency holders. Cryptocurrency is attracting a lot of investors as it can be used to buy and sell things and has potential to store and grow in value. There are many different cryptocurrencies available in the market like Bitcoin, Ethereum, Litecoin and Ripple etc.

## Nature of cryptocurrency

As to the nature of cryptocurrency, there are different sets of opinions as to whether it is a currency or a Commodity or Security. A major segment of financial experts believes that all the major characteristics of a currency like mode of exchange, unit of account and store of value are satisfied when it comes to cryptocurrency which supports the idea that it should be treated as currency whereas the other set of experts believe that since cryptocurrency is bought and sold for money, it should be considered as commodity. There is also one more conviction that cryptocurrency should be treated as a security as is a tradeable commodity that can be bought and sold over Crypto-Exchanges.

## Objectives of the study

- To study the emerging cryptocurrency market in India.
- To study the provisions of prevailing income tax law in India related to cryptocurrency.

## Emerging cryptocurrency market in india

The cryptocurrency market has grown in size and popularity among investors to facilitate financial activities such as buying, selling, and trading in India and around the world. According to the United Nations Conference on Trade and Development Report 2021, 7.3% of Indians owned cryptocurrency in 2021.

Bitcoin, along with other cryptocurrencies, has been operating in the Indian market for a long while. It was in 2012 when small-scale Bitcoin transactions were reported in India for the first time. By 2013, Bitcoins started gaining popularity among the masses and few businesses began to accept Bitcoin payments along with the Indian currency. With the arrival of BtexIndia, Unocoin, and Coinsecure, cryptocurrency exchanges began to spring up within the Country. Later, a few more exchanges like Zebpay, Koinex, and Bitcoin-India made up the list.

The increase in demand for Cryptocurrency in India attracted the attention of the Government and the Reserve Bank of India. The Reserve Bank of India can either regulate or prohibit anything that may pose a threat to or have an impact on the financial system of the Country. Reserve Bank has repeatedly through its public notices on December 24, 2013, February 01, 2017 and December 05, 2017, cautioned users, holders and traders of cryptocurrency regarding various risks associated in dealing with such virtual currencies.

In April 2018, through a decree passed by RBI, it declared that all RBI Regulated bodies like banks were prohibited from having any business relationships with entities dealing with cryptocurrency. Furthermore, those who already have any business connection with such entities were asked to end the relationship within three months. Later, the Supreme Court of India overturned a decision by the Reserve Bank of India prohibiting banks from dealing with cryptocurrency The Court found that virtual currencies had not caused any visible damage to banks regulated by the RBI.

The government of India is yet to bring any legislation concerning the regulation of Cryptocurrency in the Indian market. However, a draft bill for banning cryptocurrency has been in the works. According to the draft “Banning of Cryptocurrency and Regulation of Official Digital Currency Bill 2019”, if any person either holds, sells, transfer disposes of, issues, or deals in cryptocurrencies, he shall be liable to imprisonment which may extend to 10 Years. This bill further makes holding any cryptocurrency a non-bailable offense.

## Tax on cryptocurrency

The Indian Income Tax Act has always sought to tax income received and hence the levy of taxes on cryptocurrency can’t be ruled out. A taxation mechanism on cryptocurrency and crypto assets has been introduced by the Finance Act 2022. Section 2(47A) has been introduced in the Income-tax Act, 1961 to define Virtual Digital Assets:

VDA means:

a. any information or code or number or token (not being Indian currency or foreign currency), generated through cryptographic means or otherwise, by whatever name called, providing a digital representation of value exchanged with or without consideration, with the promise or representation of having inherent value, or functions as a store of value or a unit of account including its use in any financial transaction or investment, but not limited to investment scheme; and can be transferred, stored or traded electronically;
b. a non-fungible token or any other token of similar nature, by whatever name called;
c. any other digital asset, as the Central Government may, by notification in the Official Gazette specify:

Provided that the Central Government may, by notification in the Official Gazette, exclude any digital asset from the definition of virtual digital asset subject to such conditions as may be specified therein.

Explanation: For the purposes of this clause,-

a. “non-fungible token” means such digital asset as the Central Government may, by notification in the Official Gazette, specify;
b. the expressions “currency”, “foreign currency” and “Indian currency” shall have the same meanings as respectively assigned to them in clauses (h), (m) and (q) of section 2 of the Foreign Exchange Management Act, 1999 (42 of 1999).

## Applicable tax rate on cryptocurrency

As per the newly introduced Section 115BBH of the Act (applicable from FY 2022-23), the income on the transfer of VDA will attract a tax rate @ 30% . The cost of acquisition shall be allowed as a deduction, however, no incidental expenses like Brokerage etc. shall be allowed as a deduction.

## Set-off & carry forward of losses

Loss on the sale of a VDA can be set off against the income from other VDA. For example, Loss on transfer of Dogecoin can be adjusted against the income from a Bitcoin. Carry forward of loss is also not allowed and therefore, set off of loss is possible only in the current year itself. If the total income of an assessee comprises income solely from VDA, then the benefit of the basic exemption limit of Rs. 2,50,000/ 3,00,000/ 5,00,000 is not allowed.

## Tax deduction at source on vdas

Section 194S has been inserted in the Income Tax Act, 1961to provide for the tax deduction at source on payment of any income on VDA. The responsibility of tax

| Particulars | Transaction Value |
|---|---|
| If the total sales of an individual/ HUF do not exceed Rs. 1 crore in case of a business and Rs. 50 lacs in case of a profession in FY immediately preceding the year in which VDA is transferred | Transaction value does not exceed Rs. 50,000 during the FY |
| Individual/HUF who doesn’t have the income from business or profession | Transaction value does not exceed Rs. 50,000 during the FY |
| Any person not covered in above two categories | Transaction value does not exceed Rs. 10,000 during the FY |

deduction lies with the buyer, being a resident person. TAN number is not required by the buyer of VDA as the provisions of section 203A are not applicable. The rate of TDS is 1% except the following cases:

## Head under which income from cryptocurrency is taxable

The income generated from investment in cryptocurrency is subject to tax under any of the following three heads:

- Income from Capital Gain: In view of Section 2(14) of the Income-tax Act 1961, cryptocurrencies could be deemed to be capital assets if purchased for investments by taxpayers. Therefore, any gain arising on the transfer of a cryptocurrency shall be taxable as capital gains. Thus, if Cryptocurrency is not traded frequently but held as investment / asset then the gains arising at the time of sales will be taxed under the head Income from Capital Gains based on the period of holding.
    a. If the period of holding is up to 1 year – Short term Capital Gain (STCG) is calculated.
    b. If the period of holding is more than 3 years – Long term Capital Gain (LTCG) is calculated.
- Profit & Gain from Business & Profession: If Cryptocurrency is traded frequently then the gains from the sale will be taxed under the head Profits and Gains from Business and Profession. This is so when cryptocurrency is used to buy goods or services and cryptocurrency is accepted as payment for goods or services.
- Income from Other Sources: In the case of crypto mining, the value of the cryptocurrency at the time it was mined counts as income from other sources. Experts believe that currency generated through mining will indeed be considered under the head of income from other sources.

## Conclusion

Cryptocurrency is a social, cultural and technological advancement that goes far beyond the financial innovation. The countries that accept cryptocurrency network strengthen their economy in terms of innovation, investment, employment and taxes. Levy of tax on crypto income is a great move by Indian Govt. Some crypto finance experts believe that the tax clarity will encourage more people to invest in the cryptocurrency market which would result in accelerating the growth of the unsupervised cryptocurrency industry. Also, a well-regulated crypto ecosystem will foster an environment that is conducive to innovation. On the other hand, one set of experts believes that the levy of a flat 30 percent tax on income from crypto transactions and TDS of 1% on each crypto transfer will significantly reduce the daily turnover of crypto transactions on Indian exchanges. Most of the users will now shift to international exchanges in anticipation to escape from this heavy TDS on trading transactions. Many start-ups will also see either moving out of India or considering crypto-friendly countries to execute operations. In the end, we can say that though there has been a rapid expansion in the area of financial technology with has resulted in the tremendous growth of FinTech products but yet there is a gap in the regulation of the virtual currency business in India. The Indian Government should think of formulating a regulatory body to regulate the cryptocurrency market so as to provide a sheltered and protected platform for the investors and putting a ban on illegal activities with increased revenue for the Govt. In the absence of a regulatory framework, investors are exposed to avoidable frauds and there is also an uncertainty for new ventures trying to enter this market. It causes a threat to unconstrained movement of money in the economy giving a boost to many illegal activities like money laundering and the funding of terrorism etc.

## References:

https://taxguru.in/income-tax/taxation-crypto-assets-nutshell.html

Cryptocurrency Taxation Exclusive Guide for 7 Countries (regtechtimes.com)

Bitcoin gains currency in India - The Hindu

This interpretation of powers vested in RBI was given by the Apex Court in the case of the Internet and Mobile Association of India v. RBI. (2020 SCC Online SC 275).

Ibid. Court noted that "Nothing prevented RBI from notifying VCs under the category of "other similar instruments" indicated in Section 2(h) of FEMA, 1999 and to pass circulars" 15 RBI (2018a) Reserve Bank of India, https://rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=3 0247 16

RBI (2016) RBI cautions users of virtual Currencies, https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx? prid=39435

RBI (2017) Reserve Bank cautions regarding the risk of virtual currencies including Bitcoins, https://rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=4 2462

RBI (2018b) Edited Transcript of Reserve Bank of India's First Bi-Monthly Policy Press Conference, https://www.rbi.org.in/Scripts/bs_viewcontent.aspx?Id=3465 19

ED officials raided two bitcoin trading firm in Ahmedabad; Available at https://economictimes.indiatimes.com/news/economy/finance/ed-officials-raided-two-bitcoin-trading-firm-inahmedabad/articleshow/28006859.cms?from=mdr

Bitcoin exchanges under IT radar, survey at 9 exchanges across the countryvailable at: https://www.oneindia.com/india/bitcoin-exchanges-under-it-radar-survey-at-9-exchanges-acrossthe-country-2601156.html

Venkateswaran, A. (2018) Budget 2018: Bitcoin in India is Dead. Long Live Blockchain https://thewire.in/banking/budget-2018-bitcoin-india-dead-long-live-blockchain

Draft Banning of Cryptocurrency & Regulation of Official Digital Currency Bill, 2019. Available at https://www.prsindia.org/billtrack/draft-banning-cryptocurrency-regulation-official-digital-currency-bill-2019