Handbook on Taxation of Virtual Digital Assets

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Direct Taxes Committee

The Institute of Chartered Accountants of India

(Set up by an Act of Parliament)

New Delhi

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First Edition	:	July, 2022
Committee/Department	:	Direct Taxes Committee
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Website	:	www.icai.org
Published by	:	Direct Taxes Committee on behalf of the Institute of Chartered Accountants of India, ICAI Bhawan, Post Box No. 7100, Indraprastha Marg, New Delhi - 110 002.

Foreword

The Direct Taxes Committee (DTC) of the Institute of Chartered Accountants of India (ICAI) is one of the important Committees of the ICAI which is engaged in the matters related to direct taxes and makes representations to the Government, Central Board of Direct Taxes and at other appropriate forums from time to time on various legislative amendments and issues concerning direct taxes. One of the main activities of the Committee is to disseminate knowledge and honing skills of the membership in the area of direct taxation.

Our Hon'ble Finance Minister Smt. Nirmala Sitharaman while presenting the Union Budget 2022, announced a scheme for taxation of virtual digital assets (VDAs), such as cryptocurrencies and non-fungible tokens (NFTs). A new era in taxes been undertaken with taxation of VDAs. I am happy to note that the Direct Taxes Committee of ICAI has come out with this publication namely ***"Handbook on Virtual Digital Assets"*** so as to assist the members in understanding this new area.

I appreciate the efforts of CA. Chandrashekhar V. Chitale, Chairman, Direct Taxes Committee, CA. Raj Chawla, Vice-Chairman, Direct Taxes Committee and all other members of the Committee who have worked sincerely for bringing out this handbook in a timely manner.

I am confident that this publication will be a useful resource for the members.

Date: 27.06.2022 **CA. (Dr.) Debashis Mitra**

Place: New Delhi President, ICAI

Preface

Dynamics of the income-tax law, compel sharpening of skill sets in the arena for effective performance. Addressing counselling and compliance responsibilities of clients and the other stakeholders, importance of updating professional knowledge, need not be overemphasized. ICAI publications afford professionals, worthwhile insight and guidance in this behalf.

A cryptocurrency or coin is a digital currency (it does not exist in physical form like paper money) designed to work as a medium of exchange through a computer network that is not reliant on any central authority, such as a government or bank, to uphold or maintain it. The first decentralized cryptocurrency was Bitcoin, which first released as open-source software in 2009.

As the members are well aware that Virtual digital assets have gained tremendous popularity in recent times and the volumes of trading in such digital assets has increased substantially. In view of the trading volume of Virtual digital assets in India, Our Hon'ble Finance Minister Smt. Nirmala Sitharaman while presenting the Union Budget 2022, stated that magnitude and frequency of these transactions had made it imperative to provide for a specific tax regime and announced a scheme for taxation of virtual digital assets, such as cryptocurrencies and non-fungible tokens (NFTs).

In order to make available various aspects of law of taxation of Virtual Digital Assets and to provide guidance to the members, an effort has been made by the Direct Taxes Committee through this handbook. It covers the law and procedures relating to what is Virtual Digital Assets, how it's different from digital currency, Legislative Intent and Legal Provisions and taxation provision of Virtual Digital Assets. This new publication would enable the members to better understand the aforesaid new provisions.

Under the aforesaid circumstances, we at the Direct Taxes Committee thought it fit to bring out this brief publication namely "Handbook on Virtual Digital Assets" as a handy tool to assist the fraternity to make proper compliance of the new provisions and procedures in more objective manner and with consciousness towards related documentations. Of course, members are expected to update themselves continuously.

We are sincerely thankful to CA. (Dr.) Debashis Mitra, President, ICAI and CA. Aniket Sunil Talati, Vice-President, ICAI for being guiding force behind all initiatives being taken by the Committee.

We are pleased to place on record my sincere gratitude for the involvements and contributions by all the Committee members and our dear Council Colleagues of ICAI. We are sure that this effort of DTC of ICAI would go a long way in assisting our members in making utmost compliance of the new provisions.

Last but not the least, we appreciate the dedicated efforts of CA. Shrutika Oberoi, Secretary, Direct Taxes Committee and CA. Ravi Gupta, Assistant Secretary, Direct Taxes Committee and CA. Rudrakshi Sharma, Professional and CA. Ajay Yadav, Project Associate for their technical and administrative assistance in bringing out this handbook in a limited time.

CA. Raj Chawla
Vice-Chairman
Direct Taxes Committee, ICAI

CA. Chandrashekhar V. Chitale
Chairman,
Direct Taxes Committee, ICAI

Date: 27.06.2022

Place: New Delhi

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TAXATION OF VIRTUAL DIGITAL ASSETS

Introduction

Crypto Currency has caught fancy, these days. A good number of persons, including several corporates from various countries are acquiring and holding Crypto Currency. People were confined to home as a consequence of pandemic and that really provided time for many to dabble into various other arena. Crypto was one top runner, in such endeavours. The magnitude of existence and transactions have made many believe cryptocurrency equivalent to virtual digital assets.

Virtual Digital Assets (VDA) are subsets of all digital assets transacted on a blockchain, such as non-fungible tokens (NFTs), cryptos and other virtual assets. In layman's terms, it basically means cryptocurrencies, DeFi (decentralised finance) and non-fungible tokens (NFTs), however not limited to these assets.

Currency includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travelers' cheque, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments as may be notified by the Reserve Bank.

Bitcoin has been one of the first cryptocurrencies which entered the market in year 2009, and it was invented by Satoshi Nakamoto. After that, several Cryptocurrencies came in the market, and some of the popular currencies are Bitcoin Cash, Ripple (XRP), Litecoin, etc. As per an estimate, thousands of cryptocurrencies exist as of year 2022

Crypto currency has been a surrounded with a veil of secrecy and this has for quite a long time, in many jurisdictions, remained as a suspense from the point of view of legal perspective. The interesting debate has arisen about the legality of crypto currency as a legal tender or medium of being accepted as currency in payment settlement system. Further taxation aspect has, also, been a challenge for government exchequer. The suspense and secrecy, which is prevailing all along, has been omnipresent. This has posed challenge to the legal system controlling currency in different geographies. As a necessary consequence, this has also been a cause of concern for the taxman.

The latest Finance Act, 2022 has taken note of this phenomenon and introduced separate provisions to address taxation of transactions in the virtual digital asset (VDA) by amending provisions of the Income tax Act, 1961. Law has taken in its sweep all transactions in Virtual Digital Assets. Newly enacted provisions by the Finance Act, 2022, for the first time, have changed the taxation system and there is a separate manner of taxing income form virtual assets and losses therefrom. As a measure of anti-avoidance, tax withholding has been made mandatory for transactions in VDA.

To capture these changes in the provisions of the Income tax Act, 1961 concerning taxation of gains and losses arising from transactions and dealings in VDA, Direct taxes Committee of the ICAI has considered it necessary to publish a handbook that shall provide useful information to professionals and the other stakeholders on tax aspects of transactions in Virtual Digital Assets (VDA). The DTC appeals readers to communicate any improvement in this handbook and welcomes any suggestion.

Background for Taxation VDA

The Income tax Act, 1961 provides, in a comprehensive manner, taxation of each and every transaction and activities as also loss flowing from any transaction or activity. One may, therefore, wonder as to what can be objectives for enacting separate provisions for taxation of transactions and activities in Virtual Digital Assets (VDA).

Important reasons are hereunder discussed.

In this decade, virtual digital assets (VDAs) have become immensely popular. The magnitude of deals in VDAs has increased substantially, both in terms of numbers and value. Thus, VDAs are occupying a pivotal position in economies of all the countries in the globe.

This singular factor has resulted in emergence of a market where settlement of obligations arising from transactions are being made by exchange of VDAs, particularly in the form of crypto currency and by employing such other virtual digital assets. The magnitude and frequency of these transactions have made it imperative to provide for a specific tax regime.

The gifting of virtual digital assets is becoming fashion of the age and fancy for the same is fast catching up, particularly in tach world.

Cryptocurrency is a most popular form of VDA. It is being used as a currency i.e. mechanism to settle consideration and debts. Currency of any country is backed by ruler or government of respective jurisdiction. There is a federal or governmental authority monitoring and backing supply of currency and guarantee backing up value thereof. Unlike this, cryptocurrency is product of blockchain. Creators of cryptocurrency have remained under veil of secrecy. Therefore, sovereign authority that shall own up and deliver value against such a currency is unknown.

The veil of secrecy has made it more advantageous for antisocial and antinational elements to transact in cryptocurrency and remain in dark. Terrorists, it is believed, are hoarding cryptocurrency for obvious reasons.

The fluctuations in value of cryptocurrency are very wide and are unthinkable.

This is the reason that the Reserve Bank of India, for a very long time has put up a red flag towards private cryptocurrencies. Implications cryptocurrencies on national security and financial stability can be serious.

Stricter regimen of taxation clearly indicates substantiating the RBI philosophy of discouraging indulging in these virtual digital assets.

Plight of money across the globe without regulatory restrictions is possible. It is difficult to keep trail of transactions in cryptocurrency, affording easy hide out for tax dodgers.

These and such other factors must have prompted the Government to provide disincentive for dealing in cryptocurrency.

The Finance Bill 2022

While presenting the Union Budget for 2022-2023 on 1st February 2022, the Hon'ble Finance Minister Smt Nirmala Sitharaman announced a new provision for taxation of virtual digital assets, including cryptocurrencies and non-fungible tokens (NFTs). Stating that there had been a phenomenal increase in transactions in virtual digital assets, she said the magnitude and frequency of these transactions had made it imperative to provide for a specific tax regime. Accordingly, for the taxation of virtual digital assets, I propose to provide that any income from transfer of any virtual digital asset shall be taxed at the rate of thirty per cent.

Tax is a tool to encourage fields that contribute to well being of the subject and further government policy. Similarly, tax is a tool used to discourage activities that are counterproductive for benefit of countrymen and disapproved by the government.

In this background, the union budget tax proposal addressed serious concerns of unreliability and various negative factors from regulatory and tax perspective for transactions in VDAs and particularly, cryptocurrencies, being a dominant portion thereof.

Proposals from the Union Budget presented through the Finance Bill, 2022 have been enacted by refinement therein and accordingly, the Income tax Act, 1961 has been amended.

These proposals, after being enacted and becoming part of the Income tax Act, 1961, have come into force from April 1, 2022 except provisions for tax withholding, which came into force from July 1, 2022.

The amendments are aimed at discouraging entering into transactions including investment into virtual digital assets, it is widely believed.

India can, possibly, be the first country to take such strict statutory measures to discourage transactions in virtual digital assets. The other world shall be keenly observing execution of these provisions.

Legislative Intent

This section discusses provisions from the Income tax Act, 1961 inserted by the Finance Act, 2022 for taxation of income from virtual digital assets and treatment of loss from virtual digital assets as also tax withholding obligation in this behalf. Noncompliance attracts certain unpleasant consequences.

Ahead of discussion on law, legislative intent has been narrated. This will be useful for interpretation of provisions particularly, where there may be ambiguity.

Hon. Supreme Court has ruled that "Now it is true that the speeches made by the Members of the Legislature on the floor of the House when a Bill for enacting a statutory provision is being debated are inadmissible for the purpose of interpreting the statutory provision but the speech made by the Mover of the Bill explaining the reason for the introduction of the Bill can certainly be referred to for the purpose of ascertaining the mischief sought to be remedied by the legislation and the object and purpose for which the legislation is enacted. This is in accord with the recent trend in juristic thought not only in Western countries but also in India that interpretation of a statute being an exercise in the ascertainment of meaning, everything which is logically relevant should be admissible." [K P Varghese V. ITO 1981 AIR 1922 SCR (1) 629, 4/09/1981]

Other three decisions of Supreme Court, one in Loka Shikshana Trust v. Commissioner of Income-Tax (101 ITR 234), the other Indian Chamber of Commerce v. Commissioner of Income-tax (101 ITR 796) and the third in Additional Commissioner of Income-tax v. Surat Art Silk Cloth Manufacturers Association (121 ITR 1) where the speech made by the Finance Minister while introducing the exclusionary clause in section 2 clause (15) of the Act was relied upon by the Court for the purpose of ascertaining what was the reason for introducing that clause.

Budget Speech

Hon. Finance Minister Smt. Nirmala Sitharaman ji, while moving the Finance Bill, 2022 dealt with the provisions for taxation of virtual digital assets in paragraph 131, in the following words:

Scheme for taxation of virtual digital assets

There has been a phenomenal increase in transactions in virtual digital assets. The magnitude and frequency of these transactions have made it imperative to provide for a specific tax regime. Accordingly, for the taxation of virtual digital assets, I propose to provide that any income from transfer of any virtual digital asset shall be taxed at the rate of 30 per cent.

- No deduction in respect of any expenditure or allowance shall be allowed while computing such income except cost of acquisition. Further, loss from transfer of virtual digital asset cannot be set off against any other income.
- Further, in order to capture the transaction details, I also propose to provide for TDS on payment made in relation to transfer of virtual digital asset at the rate of 1 per cent of such consideration above a monetary threshold.
- Gift of virtual digital asset is also proposed to be taxed in the hands of the recipient.

Explanatory Memorandum to the Finance Bill 2022

Paragraph 2 on Page no. 54 of the Memorandum explains the proposals as follows:

''Virtual digital assets have gained tremendous popularity in recent times and the volumes of trading in such digital assets has increased substantially. Further, a market is emerging where payment for the transfer of a virtual digital asset can be made through another such asset. Accordingly, a new scheme to provide for taxation of such virtual digital assets has been proposed in the Bill.

The following Extract from Budget Speech provides background of virtual digital assets.

No deduction in respect of any expenditure or allowance shall be allowed while computing such income except cost of acquisition. Further, loss from transfer of virtual digital asset cannot be set off against any other income.

Further, in order to capture the transaction details, I also propose to provide for TDS on payment made in relation to transfer of virtual digital asset at the rate of 1 per cent of such consideration above a monetary threshold. Gift of virtual digital asset is also proposed to be taxed in the hands of the recipient.

In her post-budget media interaction, Hon. FM Nirmala Sitharaman was asked about cryptocurrencies. She explained that a currency can be defined if it is issued by the central bank. "I said the Reserve Bank will be issuing a digital currency, a currency is a currency only when it is issued by the central bank even if it is a crypto. But anything which is outside of that loosely all of us refer it to be cryptocurrency, but they are not currencies,"

Notes on Clauses

Official statement of the Government on these provisions is available in notes on clauses.

Section 115BBH has been inserted to provide for tax on income from virtual digital assets. Notes on this clause are as follows:

Clause 28 seeks to insert new section 115BBH relating to tax on income from virtual digital assets and new section 115BBI relating to specified income of certain institutions.

Sub-section (1) of the proposed new section 115BBH seeks to provide that where the total income of an assessee includes any income from the transfer of any virtual digital asset, 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 (a).

Sub-section (2) of the said section seeks to provide that notwithstanding anything contained in any other provision of the Act,––

(a) no deduction in respect of any expenditure (other than cost of acquisition) or allowance or set off of any loss shall be allowed to the assessee under any provision of the 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 other provision of the Act to the assessee and such loss shall not be allowed to be carried forward to succeeding assessment years.

Definition of Virtual Digital Assets?:

The definition of Virtual Digital Assets is inserted by the Finance Act 2022 , w.e.f. 1-4-2022, vide new clause (47A) of the section 2 of the Income-tax Act 1961, where Virtual Digital Assets 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.

As per Notification No. 74/2022, dated. 30-06-2022, the Central Government hereby notifies following virtual digital assets which shall be excluded from the definition of virtual digital asset:

(i) Gift card or vouchers, being a record that may be used to obtain goods or services or a discount on goods or services;

(ii) Mileage points, reward points or loyalty card, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services;

(iii) Subscription to websites or platforms or application.

2. This notification shall come into force from the date of publication in the Official Gazette.

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;

As per Notification No. 75/2022, dated. 30-06-2022 , the Central Government hereby specifies a token which qualifies to be a virtual digital asset as non-fungible token within the meaning of sub-clause (a) of clause (47A) of section 2 of the Act but shall not include a nonfungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

(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);]

(h) “currency” includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travellers cheques, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank.

(i) “currency notes” means and includes cash in the form of coins and bank notes;

(m) “foreign currency” means any currency other than Indian currency;”

(q) “Indian currency” means currency which is expressed or drawn in Indian rupees but does not include special bank notes and special one rupee notes issued under section 28A of the Reserve Bank of India Act, 1934 (2 of 1934);

What is Virtual Digital Assets:

From the definition of Virtual Digital Assets appearing in Section 2(47A) of the Act, the following aspects emerge:

Features of Virtual Digital Assets:

(a) Any information, code, number or token generated through cryptographic means. Cryptography is the study of secure communications techniques that allow only the sender and intended recipient of a message to view its contents

(b) a non-fungible token or any other token of similar nature, by whatever name called. Non-fungible token" means such digital asset as the Central Government may, by notification in the Official Gazette, specify. As per Notification No. 75/2022, dated. 30-06-2022, the Central Government hereby specifies a token which qualifies to be a virtual digital asset as non-fungible token within the meaning of sub-clause (a) of clause (47A) of section 2 of the Act but shall not include a nonfungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

(c) any other digital asset, as the Central Government may, by notification in the Official Gazette specify

Virtual Digital Assets Excludes

(a) Indian Currency

(b) Foreign Currency

(c) 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.

(d) As per Notification No. 75/2022, dated. 30-06-2022 , it shall not include a nonfungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

(e) As per Notification No. 74/2022, dated. 30-06-2022, the Central Government hereby notifies following virtual digital assets which shall be excluded from the definition of virtual digital asset:

  (i) Gift card or vouchers, being a record that may be used to obtain goods or services or a discount on goods or services;

  (ii) Mileage points, reward points or loyalty card, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services;

  (iii) Subscription to websites or platforms or application.

2. This notification shall come into force from the date of publication in the Official Gazette.

How are Virtual Digital Assets different from Digital Currency?

Currency is medium of exchange which can be defined as currency only if it is issued by the central bank. e.g. dollar, rupee etc. Hence, crypto will be called a currency only when it will be issued by the central bank. Digital Currency is what the RBI will issue in the next fiscal, beginning 1 April, will be the digital currency. This digital currency will be called a 'digital rupee'. Virtual Digital Assets is anything which is created outside of the central bank are virtual digital assets created by individuals. These private virtual currencies do not represent any person's debt or liabilities, as there is no issuer. They are not money and certainly not currency. Virtual Digital Assets also include Non-fungible tokens or NFTs, which are cryptographic assets on a blockchain with unique identification codes and metadata that distinguish them from each other. NFTs can also be used to represent individuals' identities, property rights, and more.

Thus, the proposed 'Digital Rupee' would essentially mirror the prevalent physical currency in digital form. It will be issued by the Reserve Bank of India and will be fungible with physical currency. The exact regulation governing this Central Bank Digital Currency (CBDC) is yet to be finalised. However, it will not be considered as a VDA.

In a post Budget interactions, the FM has clarified that what the RBI issues in the next fiscal will be the digital currency and everything else apart from that are digital assets being created by individuals and the government will be taxing the profit which are made during transactions of such assets at 30 per cent.

Cryptocurrency

Cryptocurrency is a form of currency that only exists digitally, that usually has no central issuing or regulating authority but instead uses a decentralized system to record transactions and manage the issuance of new units, and that relies on cryptography to prevent counterfeiting and fraudulent transactions. Cryptocurrencies are not controlled by the government or central regulatory authorities. As a concept, cryptocurrency works outside of the banking system using different brands or types of coins – Bitcoin being the major player. It is highly risky assets as their implications on national security and financial stability could be serious. It is not regulated digital currency even in the past as well as in current times. Government has not promoted cryptocurrency . Despite a new scheme to provide for taxation of such virtual digital assets has came, the government is yet to clarify its stance on whether cryptocurrencies would be regulated or banned. Currently, India has not regulated crypto currencies.

The matter related to cryptocurrencies in India was first discussed on the floor of the house of the parliament, when the then finance minister late Shri Arun Jaitley famously remarked “India does not accept cryptocurrencies as a form of legal tender, however, the benefits of blockchain technology shall be used for the development of our country”. As the market matured, there are more number of people getting associated with crypto transactions. The

matter about registration & regulation of crypto exchanges was raised to SEBI. SEBI concluded that cryptos were neither securities nor commodities nor currencies, and in that case they would not have jurisdiction over these crypto exchanges. This makes us ponder over another question that how did these exchanges get recognized as exchanges. If one takes a liberal view, it is prudent to say these so called crypto exchanges are self regulated, self assumed and self governed. There is absolutely no regulatory authority, agency or department which governs the transactions taking place on these so called crypto exchanges. On analysing the above given facts and the sequence of events, one wonders whether this was a collective failure of the system at large.

When provisions have been enacted in tax law, the issue raised is that is Cryptocurrency Legal in India? This has been clarified by the Finance Minister. Taxing cryptocurrencies does not give them legal status in the country, finance minister Nirmala Sitharaman clarified in the Parliament. It’s the country’s sovereign right to tax cryptocurrency transactions. However, any official stance on regulation will only come once the ongoing consultations are completed, finance minister said.

Taxability of virtual digital assets till 31.3.2022

Though Budget 2022 from April 1, 2022, inserted Section 115BBH relating to taxation of virtual digital assets, an era of taxation of VDA in express terms has been flagged of, one may wonder what was the position till then.

Virtual Digital Assets were held, traded, exchanged by people. The inclusive definition of 'income' appearing in clause (24) of Section 2 of the Income tax Act, 1961 brings under its sweep all sorts of income. Even illegal income is also subject to tax.

Therefore, though express provisions were absent, tax payers were adopting different approaches for taxation, depending on the character of Virtual Digital Asset in their respective hands. Income was considered to be taxable under the head 'Income from business and profession', where VDA was held as a business commodity or from 'Capital Gains' if held as a capital asset. If tax payer is trading in cryptocurrencies as stock-in-trade and the same is also reflected by way of volume and frequency of trades, the income was categorized as 'Business income'. In case of stray transactions in VDA, the residuary head of income 'Income from Other Sources' found reporting of income from transaction in VDA. There being no separate applicable tax rate for VDA income, the same was taxed at specific rate for capital gains or otherwise, at normal slab rates applicable to the tax payer. Thus, if the assessee held the VDA as investment, then depending on the holding period of the capital asset , the gain may be classified as Long-term (more than 36 months) or Short-term (up to 36 months or lower). Long term gains are subject to tax at 20% and the indexation benefit is available. Short term gains are taxable at normal applicable slab rates of the tax payer.

To sum up, although separate provisions have been made in the Act for taxation of Virtual Digital Assets from 1st April, 2022, the income therefrom was subjected to tax even prior to that date. The benefit of section 54, 54EC and 54 will be available.

Taxability of virtual digital assets from 01.4.2022

Section 115BBH has been inserted by the Finance Act, 2022, w.e.f. 1-4-2023 i.e. Financial Year beginning from 01.04.2022. The said section provides for charge of tax on income from transfer of Virtual Digital Assets at a flat rate of 30%. Thus, income resulting from transactions in Virtual Digital Assets on and after April 1, 2022 shall be taxed under section 115BBH, notwithstanding any other provisions of law.

Provisions of section 115BBH are hereunder reproduced:

Section 115BBH- Tax on income from virtual digital assets:

(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 (a).

(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.

From the provisions of Section 115BBH, reproduced above, the emerging aspects are:

(i) The section has prescribed separate system for taxation of income from transfer of virtual digital asset.

(ii) Income from transfer of virtual digital asset shall be ascertained separately for the purpose of imposing tax thereon.

(iii) Income from transfer of virtual digital asset shall be subjected to income tax at the rate of 30 per cent.

(iv) Tax on transfer of virtual digital asset shall be charged irrespective of :

  (a) income is below threshold limit or

  (b) the assessee has sustained loss

(v) Loss from transfer of virtual digital asset is not eligible for setoff against any income including, income from transfer of any other virtual digital asset.

Where the total income of an assessee includes any income from transfer of any virtual digital asset, the income tax payable shall be the aggregate of the amount of income-tax calculated on income of transfer of any virtual digital asset at the rate of 30% and 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 the income from transfer of virtual digital assets. It is interesting to note that no amendment is proposed in section 2(24), section 28 and section 45 of Income-tax Act. None of the heads of the income as specified in section 14 of the Act are made applicable for computation of income from transfer of VDA. Generally, Income-tax Act, provides that if the income is not taxable under the head Profits and Gains from Business and Profession, under Capital Gain, the income will be taxed as Income from other Sources.

This makes it necessary to understand the following aspects to understand the new taxation regime of taxation of Virtual Digital Assets:

1. What are Virtual Digital Assets
2. What is 'transfer' in relation to virtual digital asset
3. How income from transfer from Virtual Digital Assets is computed
4. What is treatment for loss from transfer of Virtual Digital Assets

These issues have been discussed hereunder:

1. What are Virtual Digital Assets

The Income tax Act, 1961 defines various terms in section 2 of the Act. Clause (47A) of the Act defines 'Virtual Digital Asset'.

2. What is 'transfer' in relation to virtual digital asset

In relation to 'virtual digital asset', meaning of 'transfer' has been separately supplied.

Sub section (3) of Section 115BBH of the Act provides that:

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.

This definition should be employed to consider whether virtual digital asset has been transferred. The said section 2(47) provides as follows:

Section 2(*47*) "transfer", in relation to a capital asset, includes,—

(*i*) the sale, exchange or relinquishment of the asset ; or

(*ii*) the extinguishment of any rights therein ; or

(*iii*) the compulsory acquisition thereof under any law ; or

(*iv*) in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment ; or

(*iva*) the maturity or redemption of a zero coupon bond; or

(*v*) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882) ; or

(*vi*) any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring, or enabling the enjoyment of, any immovable property.

Explanation 1.—For the purposes of sub-clauses (*v*) and (*vi*), "immovable property" shall have the same meaning as in clause (*d*) of section 269UA.

Explanation 2.—For the removal of doubts, it is hereby clarified that "transfer" includes and shall be deemed to have always included disposing of or parting with an asset or any interest therein, or creating any interest in any asset in any manner whatsoever, directly or indirectly, absolutely or conditionally, voluntarily or involuntarily, by way of an agreement (whether entered into in India or outside India) or otherwise, notwithstanding that such transfer of rights has been characterised as being effected or dependent upon or flowing from the transfer of a share or shares of a company registered or incorporated outside India;

Thus, the above definition of term “transfer” has been rendered in respect of a capital asset. Under section 2 (*14*) "capital asset" means property of any kind held by an assessee, whether or not connected with his business or profession.

Virtual digital asset may be held as a capital asset or it may be held otherwise say, it may be held as an asset of business or profession. Subsection (3) of section 115 has made it clear that the above definition of ‘transfer’ should be used in relation to virtual digital asset, irrespective of the nature or character of virtual digital asset in the hands of the assessee. Thus, even if any assessee is holding virtual digital asset as a stock in trade for business, still the above definition is to be used.

Income will arise when anyvirtual digital asset is transferred by an assessee.

3. How income from transfer from Virtual Digital Assets is computed

For the purpose of ascertaining income from virtual digital asset is required to be ascertained separately.

For ascertainment of income from transfer of any virtual digital asset, two provisions have been made in subsection (2) of section 115BBH.

Let us consider these provisions.

Provisions of subsection (2) of section 115BBH are to be considered notwithstanding anything contained in any other provision of the income tax Act, 1961 concerning computation of income or any other provision is to be ignored. Computation is to be made as prescribed under subsection (2) of section 115BBH of the Act.

The provisions of subsection (2) of section 115BBH state that

(a) (i) Deduction only in respect of cost of acquisition of virtual digital asset

(ii) No deduction in respect of any other expenditure

(iii) No deduction in respect of any loss

(b) (i) No set off of loss from transfer of the virtual digital asset

(ii) No loss from transfer of the virtual digital asset is allowed to be carried forward to succeeding assessment years.

These provisions are hereunder discussed at length:

(i) Deduction only in respect of cost of acquisition of virtual digital asset

Clause (a) of sub-section (2) of Section 115BBH provides that deduction in respect of any expenditure on cost of acquisition of virtual digital asset shall be allowed.

(ii) No deduction in respect of any other expenditure

Clause (a) of sub-section (2) of Section 115BBH provides that no deduction in respect of any expenditure, other than cost of acquisition, if any 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) of Section 115BBH of the Act.

Common Expenses:

It is possible that a business enterprise may be having a composite business of say, trading in goods and dealing in virtual digital assets. It will incur certain overheads that are common for both the activities viz. dealing in virtual digital assets and the other activity, for the sake of brevity, normal business activity.

For ascertaining income from dealing in virtual digital assets, clause (a) of section 115BBH(2) provides that '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'.

This leads to an issue, as to whether such common overheads or expenses can be allowed as a deduction, in entirety, against income

from the normal business activity i.e. business other than dealing in virtual digital assets.

Hon. Supreme Court, in a similar circumstance, while addressing issue of allowability of common overheads or expenses in entirety, when incurred for agricultural activity i.e. earning exempt income and normal taxable business activity, only against normal taxable business income, in entirety, has observed as follows:

The assessee's council has fairly conceded that if the exempted income and the taxable income are earned from one and indivisible business, then the apportionment of the expenditure cannot be sustained. But, submits the learned counsel, in this case the Tribunal did not record a finding that the business of the assessee is one indivisible, therefore, the apportionment of the expenditure is valid. We are afraid, we cannot accede to the contention of the learned counsel inasmuch as a plain reading of the question itself shows that it embodies "the business of the assessee being one and indivisible". This being the position, it is not open to the revenue to contend that the business is not one and indivisible. In view of the fact that a perusal of the question itself discloses that income from various ventures is earned in the course of one and indivisible business, the impugned order upholding the apportionment of the expenditure and allowing deduction of only that proportion of it which is referable to taxable income, is unsustainable.

In computing `profits and gains of business or profession' when an assessee is carrying on business in various ventures and some among them yield taxable income and the others do not, the question of allowability of the expenditure under section 37 of the Act will depend on: (a) fulfilment of requirements of that provision noted above; and (b) on the fact whether all the ventures carried on by him constituted one indivisible business or not; if they do, the entire expenditure will be a permissible deduction but if they do not, the principle of apportionment of the expenditure will apply because there will be no nexus between the expenditure attributable to the venture not forming integral part of the business and the expenditure sought to be deducted as the business expenditure of the assessee.

[Rajasthan State Warehousing Corporation Vs. CIT Civil Appeal No. 4049 of 1994]

Based on these observations of the Supreme Court, the answer to the question of allowability of common business expenses against income from the normal business activity, appears to be in affirmative.

In order to negate effect of the aforesaid Supreme Court judgment, provisions of section 14A have been enacted. However, section 14A addresses bifurcation of common expenses wherein one business is that income from which is not forming part of total income. In case of VDA business income, since income from which it is forming part of total income, provisions of section 14A of the Act are not applicable.

To sum up, the debate of deduction for common overheads or expenses, in entirety, against income from the normal business activity i.e. business other than dealing in virtual digital assets will reach finality when there is any court judgment or legislative amendment.

(iii) No set off of loss from transfer of the virtual digital asset

Clause (b) of sub-section (2) of Section 115BBH provides that 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.

(iv) No loss from transfer of the virtual digital asset is allowed to be carried forward to succeeding assessment years.

Clause (b) of sub-section (2) of Section 115BBH provides that loss from transfer of the virtual digital asset computed under clause (a) of sub-section (1) shall not be allowed to be carried forward to succeeding assessment years.

Head of Income:

The Government did not clarify regarding head of income under which virtual digital assets will be taxable.

Taxation under the head Business Income

If the transactions in virtual digital assets is frequent and voluminous, it may held that taxpayer is trading in such assets. In this case income from sale or transfer of virtual digital assets is taxable as business income. The income (net of cost of acquisition) will be taxable at the rate of 30% plus surcharge and cess.

Example: Mr. A has purchased 1,000 NFTs at Rs. 1,400 each on 16 July 2020. He transferred all NFTs at Rs 1,700 in the previous year 2022-23

The income under head business will be Rs 3,00,000 which will be taxable at rate of 30%. Under the head business income , surcharge can be levied upto 37%.

Where virtual digital assets is held as stock in trade, any income from sale/transfer shall be included under head Income from Business & Profession.

Taxation under the head Capital Gain

The Government did not clarify if the virtual digital assets is currency, commodity or security. Virtual digital assets may be classified as income under head capital gain if purchased by assessee for investments purpose. If gain arising from sale of virtual digital assets , then further classification relating to long-term or short-term gain would depend on period of holding of assets.

If virtual digital assets is hold by assessee for more than 36 months from date of purchase, it will be treated as long term capital gain, otherwise as short term capital gain. The tax shall be applicable at 30% plus surcharge and cess at Full value of consideration less cost of acquisition.

Example: Mr. A has purchased 1,000 NFTs at Rs. 1,400 each on 16 July 2020. He transferred all NFTs at Rs 1,700 in the previous year 2022-23

The income under head capital gain will be Rs 3,00,000 which will be taxable at rate of 30% irrespective of whether it is long term or short term capital gain.

If it is the long term capital gain, surcharge will be restricted to 15% but in case of short term capital gain, surcharge can be levied upto 37%

Taxation under head Income from other Sources

In case of stray transactions in virtual digital assets, the residuary head of income 'Income from Other Sources' found reporting of income from transaction in VDA which will be taxable at rate of 30% (net cost of acquisition) plus surcharge and cess.

Example: Mr. A has purchased 1,000 NFTs at Rs. 1,400 each on 16 July 2020. He transferred all NFTs at Rs 1,700 in the previous year 2022-23

The income under head income from other sources will be Rs 3,00,000 which will be taxable at rate of 30%. Surcharge on income from other sources can be levied upto 37%.

Applicability of Advance Tax provisions on income arising on VDA- As per Section 207 of the Act, Tax shall be payable in advance during any financial year, in respect of the total income of the assessee which would be chargeable to tax for the assessment year immediately following that financial year. However, the above provisions shall not apply : (i) to a resident who does not have any income chargeable under head "Profit and gains of business or profession" and (ii) assesse is of age of age of sixty years or more during previous year. Advance tax is payable during a financial year ,if amount of tax payable by assesse during the year is ten thousand rupees or more. Therefore, Assessee earning income from sale of VDA is required to pay advance tax as per applicable advance tax provisions under Income-tax law**.** In such cases interest under section 234C may not be applicable.

4. What is treatment for loss from transfer of Virtual Digital Assets

Section 115BBH(2)(*b*) provides that no set-off of loss from the transfer of the virtual digital asset shall be allowed against income computed under any other provision of this Act to the assessee

However, in the context of the proposed amendment, no set off of loss/ expenditure except for cost of acquisition is permissible. The provision is very harsh. As a taxpayer, if the money is lost, then obviously there cannot be flow for payment of taxes. However, as the Government and RBI wants to discourage transactions in virtual digital assets.

Each VDA in an investor's portfolio, i.e, crypto coins or non-fungible tokens (NFT), will be treated as a separate asset class, and the gain or loss against the transfer of a particular VDA cannot be set off/adjusted against the loss or gain, respectively, in any other VDA.

Section 115BBH(2)(b) also provides that loss from virtual digital assets not be allowed to be carried forward to succeeding assessment years.

Payment on transfer of Virtual Digital Assets

Provisions of section 194S are hereunder reproduced:

Section 194S – Payment on Transfer of Virtual Digital Assets

(1) Any person responsible for paying to any resident any sum by way of consideration for transfer of a virtual digital asset, shall, at the time of credit of such sum to the account of the resident or at the time of payment of such sum by any mode, whichever is earlier, deduct an amount equal to one per cent of such sum as income-tax thereon:

Provided that in a case where the consideration for transfer of virtual digital asset is—

(a) wholly in kind or in exchange of another virtual digital asset, where there is no part in cash; or

(b) 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,

the person responsible for paying such consideration shall, before releasing the consideration, ensure that tax required to be deducted has been paid in respect of such consideration for the transfer of virtual digital asset.

(2) The provisions of sections 203A and 206AB shall not apply to a specified person.

(3) Notwithstanding anything contained in sub-section (1), no tax shall be deducted in a case, where—

(a) the consideration is payable by a specified person and the value or aggregate value of such consideration does not exceed fifty thousand rupees during the financial year; or

(b) the consideration is payable by any person other than a specified person and the value or aggregate value of such consideration does not exceed ten thousand rupees during the financial year.

(4) Notwithstanding anything contained in section 194-O, in case of a transaction to which the provisions of the said section are also applicable along with the provisions of this section, then, tax shall be deducted under sub-section (1).

(5) Where any sum referred to in sub-section (1) is credited to any account, whether called "Suspense Account" or by any other name, in the books of

account of the person liable to pay such sum, such credit of the sum shall be deemed to be the credit of such sum to the account of the payee and the provisions of this section shall apply accordingly.

(6) If any difficulty arises in giving effect to the provisions of this section, the Board may, with the prior approval of the Central Government, issue guidelines for the purposes of removing the difficulty.

(7) Every guideline issued by the Board under sub-section (6) shall be laid before each House of Parliament, and shall be binding on the income-tax authorities and on the person responsible for paying the consideration on transfer of such virtual digital asset.

Explanation.—For the purposes of this section "specified person" means a person,—

(a) being an individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business carried on by him or profession exercised by him does not exceed one crore rupees in case of business or fifty lakh rupees in case of profession, during the financial year immediately preceding the financial year in which such virtual digital asset is transferred;

(b) being an individual or a Hindu undivided family, not having any income under the head "Profits and gains of business or profession"

From the provisions of Section 194S, reproduced above, the emerging aspects are:

In order to widen the tax base from the transactions so carried out in relation to these assets, Finance Act 2022, w.e.f. 1-7-2022 inserted vide section 194S to the Act to provide for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of one per cent of such sum. However, no deduction will be required wherein the consideration paid during the Financial Year does not exceed Rs. 50,000/- (in case of specified person) or Rs. 10,000/- (in any other case)

It is to be noted that the rate of deduction of tax at source under section 194S is prescribed at the rate of 1%. The rate of tax under section 115BBH is to be increased by surcharge to be levied based on status of the taxpayer and slab of income. However, for rate of tax deduction under 194S there is no provision for considering surcharge.

Where the consideration is wholly in kind or in exchange of another virtual digital asset where there is no part in cash; or 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, the person paying such consideration shall make sure that the tax has been paid before releasing such consideration.

The provisions of Section 203A (Tax deduction and collection number) and 206AB (Higher TDS rates for non-filers of ITR) will not be applicable to payments made by specified person. Thus, even if the deductee has not furnished the return of income for a specified period, the tax shall be deducted at the rate prescribed under this provision and not as specified in Section 206AB, if the payer is a specified person.

The section also provides that if tax has been deducted under section 194S, then no other TDS/TCS provision shall apply in respect of the said transaction. Where tax is deductible under both section 194-O and proposed section 194S, then tax shall be deducted under section 194S and not under section 194-O.

If the deductee does not furnish his PAN to the deductor, the tax shall be deducted at the rate of 20% as prescribed under Section 206AA.

Specified person as defined does not require to apply or obtain a Tax Deduction or Collection Account Number (TAN) for deducting tax under this section. Hence, such a deductor can use his PAN in place of TAN

If the virtual digital asset is transferred to non resident citizens of india, tax on payment on transfer of virtual digital asset will be covered under section 195 of Income-tax Act. Any kind of income is chargeable under section 195 of Income-tax Act.

When virtual digital assets received as gifts are Taxable:

Section 56(2)(x) inserted by Finance Act, 2017 and applicable for receipt without consideration/ inadequate consideration on or after 01st April, 2017, the meaning of the word “property” is clarified in explanation thereto (explanation to clause (vii) of section 56 (2)). Now, the said explanation is proposed to be amended to enlarge the meaning of the word “property” to include virtual digital assets. The said amendment will take effect from 01st April 2023 and will apply in relation to assessment year 2023-2024 and subsequent years thereon.

In order to provide for taxing the gifting of virtual digital assets, Finance Act 2022, w.e.f. 1-4-2023, amended Explanation to clause (x) of section 56(2) of

the Income-tax Act,1961 and for the purpose of the said clause definition of property vide Section 56(2)(x) shall include virtual digital assets.

Particulars of Income	**Amount Taxable under the head 'Income from Other Sources'**
(A) Any sum of money,— without consideration, the aggregate value of which exceeds Rs. 50,000	The whole of the aggregate value of such sum
(B) Any immovable property,— (i) without consideration, the stamp duty value of which exceeds Rs. 50,000;	The Stamp Duty Value of such property
(ii) for a consideration which is less than the stamp duty value of the property by an amount exceeding Rs. 50,000.	the stamp duty value of such property as exceeds the consideration received
(C) Any property, other than immovable property,— (i) without consideration, the aggregate fair market value of which exceeds Rs. 50,000;	The whole of the aggregate fair market value of such property
(ii) for a consideration which is less than the aggregate fair market value of the property by an amount exceeding Rs. 50,000:	The aggregate fair market value of such property as exceeds such consideration

The above clause shall not apply to any sum of money received—

(a) from any relative; or

(b) on the occasion of the marriage of the individual; or

(c) under a will or by way of inheritance; or

(d) in contemplation of death of the payer; or

(e) from any local authority as defined in the Explanation to clause (20) of section 10; or

(f) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or

(g) from any trust or institution registered under section 12AA or section 12AB].

(h) by any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in subclause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10

Some Practical Illustrations relating to VDA

1. Particulars of Income of individual -

Income from salary	Rs. 1,80,000
Interest income	Rs. 20,000
Income from transfer of VDA	Rs. 45,000
Compute Tax	

Solution: Total income (excluding Income from VDA) is below Maximum amount of income not chargeable to tax. Therefore tax on income other than income from VDA is Nil. Tax on Income from VDA is Rs. 14,040 (VDA will taxed at rate of 30% plus surcharge and cess).

As per section 194S of Income-tax act, 1961 provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of one per cent of such sum. However, no deduction will be required wherein the consideration paid during the Financial Year does not exceed Rs. 50,000/- (in case of specified person) or Rs. 10,000/- (in any other case)

2. Particulars of Income of individual -

Income from salary	Rs. 1,80,000
Interest income	Rs. 20,000
Income from transfer of VDA	Rs. 1,50,000
Compute Tax	

Solution: Total income (excluding Income from VDA) is below Maximum amount of not income chargeable to tax. Therefore, tax on income other than income from VDA is Nil. Tax on Income from VDA is Rs. 46,800 (VDA will taxed at rate of 30% plus surcharge and cess).

As per section 194S of Income-tax act, 1961 provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of one per cent of such sum. However, no deduction will be required wherein the consideration paid during the Financial Year does not exceed Rs. 50,000/- (in case of specified person) or Rs. 10,000/- (in any other case)

3. Particulars of Income of individual -

Income from Business:	Loss of Rs 10,00,000
Interest Income:	Rs 50,000

Income from Transfer of VDA: Rs 2,50,000

Compute Tax

Solution: As per Section 71 of the Act, loss from business income (other than speculative business) can be set off against income from other sources. Therefore, total income excluding income from VDA is loss of Rs. 9,50,000 which will be carried forward to next assessment year.

Tax on Income from VDA is Rs. 78,000 (VDA will taxed at rate of 30% plus surcharge and cess @ 4%).

As per Section 115BBH of the Act, Loss arising from Transfer of VDA cannot be set off against income computed under any provisions of this Act. However, current Income-tax provisions is silent about whether loss other than from Transfer of Virtual Digital Assets can be set off against VDA Income. Income-tax provisions do not provide any clarification on this matter. Therefore, net loss of Rs. 9,50,000 is not set off with Income from VDA of Rs 2,50,000.

4. Whether rebate under section 87A of the Act is available-

Particulars of Income of individual -

Income from Salary	Rs. 3,00,000
Interest income	Rs. 50,000
Income from transfer of VDA	Rs. 1,00,000

Solution: As per Section 87A of the Act if a resident individual's taxable income is upto Rs. 5 lakhs then they will get the benefit/tax rebate of Rs. 12,500 or the amount of tax whichever is lower.

The provisions relating to VDA is not clear whether the rebate under Section 87A can be claimed. This is the matter of clarification and should be considered thereof.

If rebate under Section 87A might be claimed on income from VDA then Tax as per the above example would be Nil as Total Income including income from VDA is Rs 4,50,0000 i.e. within the threshold limit prescribed for claiming rebate under Section 87A.

Income from Salary Rs. 3,00,000

Interest income Rs. 50,000

Income from transfer of VDA Rs. 2,00,000

If rebate under Section 87A might be claimed on income from VDA then, Total income would be Rs. 5,50,000, therefore benefit of Section 87A would not be applicable as Total income exceeds Rs. 5,00,000. So Total tax on above income would be Rs. 67,600 (Tax on normal income upto Rs 2,50,000 is exempted. Tax over and above Rs. 2,50,000 is Rs. 5,000 as per slab rate for individual below 60 years and income from VDA is chargeable flat at 30% rate i.e. Rs. 60,000, plus surcharge and cess @ 4%)

If rebate under Section 87A not available on Income from VDA, then as per above example ,Total income for claiming Section 87A is Rs. 3,50,000, so no tax will be levied on total income other than income from VDA as it is below Rs. 5,00,000

Tax from VDA will be Rs. 62,400 (VDA will taxed at rate of 30% plus surcharge and cess @ 4%).

5. In the following circumstances, whether Section 44AD is applicable and income can be returned under estimated income scheme?

Income from business is Rs. 1,90,00,000

Income from transfer of VDA Rs.11,00,000

Section 44AD deals with Presumptive Taxation scheme for an eligible assessee engaged in eligible business. Income will be computed at rate of 6%/8% of the turnover or gross receipts. Eligible assesse and eligible business is defined under the Section 44AD of the Act.

We are considering the possibility of holding VDA as capital asset, As far as taxation is concerned , Income from transfer of VDA is chargeable flat at rate of 30% as per Section 115BBH, therefore section 44AD will not be applicable over it.

Therefore, here Section 44AD will be applicable on Income of business of Rs 1,90,00,000 and Section 115BBH will be applicable on Income from VDA of Rs. 11,00,000

In the following circumstances, whether tax audit is applicable?

Income from business is Rs. 90,00,000

Income from transfer of VDA Rs. 11,00,000

As per Section 44AB of the Act, Every person carrying on business , if his sales or Gross receipts exceeds 1 crore/50 lakhs, get his accounts of such

previous year audited by an accountant before the specified date and furnish by that date the report of such audit in the prescribed form duly signed and verified by such accountant .Here, we are considering possibility of holding VDA as business assets, then in that case , sale proceeds from VDA should ideally be included for purpose of carrying out Tax Audit.

Since, Total Income from Business is Rs. 1,01,00,000, therefore Tax Audit under section 44AB is applicable.

Various Issues relating to Virtual Digital Assets

1. Treatment of loss due to devaluation of stock-in-trade of Virtual Digital Asset: This issue is not yet clear. There may be two possibilities that is devaluation may occur due to change in price of the assets at stock exchanges or if change in foreign exchange rates, if VDA purchased in any currency other than INR. Such notional losses may arise at the end of financial year of unsold stock of VDA. Issues may also arise at the time of sale of such VDA. Current Income-tax provisions do not provide any clarification on this matter.

2. Whether loss sustained by assessee on sale or transfer of virtual digital assets prior to 31.03.2022 is allowed to be set off or carry forward: The law on this matter is not clear and there is ambiguity and assessee should take decision on basis of facts and circumstances.

3. Whether Virtual Digital Assets are accepted as Legal Currency: It is determined by law of land. As of now, in India, there are no law which legalizes them. At the same time, there is no law which prohibits them either. So, in the absence of any specific law, the decision of a person lies on the interpretation of the facts and circumstances of every case. However, globally some countries have recognised cryptos as a separate asset class. In some countries such as El Salvador, it is a legal tender, which is to say that one can pay taxes to the government in crypto.

Circular No. 13 of 2022

F. No. 370142/29/2022-TPL (Part-I)

Government of India Ministry of Finance Department of Revenue Central Board of Direct Taxes (TPL Division)

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New Delhi, dated 22nd June, 2022

Subject: Guidelines for removal of difficulties under sub-section (6) of section 194S of the Income-tax Act, 1961

Finance Act 2022 inserted a new section 194S in the Income-tax Act, 1961 (hereinafter referred to as "the Act") with effect from 1st July 2022.

The new section mandates a person, who is responsible for paying to any resident any sum by way of consideration for transfer of a virtual digital asset (VDA), to deduct an amount equal to 1% of such sum as income tax thereon. The tax deduction is required to be made at the time of credit of such sum to the account of the resident or at the time of payment, whichever is earlier.

This deduction is not required to be made in the following cases:-

(i) the consideration is payable by a specified person and the value or aggregate value of such consideration does not exceed fifty thousand rupees during the financial year; or

(ii) the consideration is payable by any person other than a specified person and the value or aggregate value of such consideration does not exceed ten thousand rupees during the financial year

The following are defined as specified person for the purposes of this provision:

(i) An individual or Hindu undivided family (HUF) who does not have any income under the head "profit and gains of business or profession"; and

(ii) An individual or HUF having income under the head "profits and gains of business or profession", whose total sales/gross receipts/turnover from business carried on by him does not exceed one crore rupee or in case of profession exercised by him does not exceed fifty lakh rupee. This threshold is to be seen in the financial year immediately preceding the financial year in which the VDA is transferred.

Sub-section (6) of section 194S of the Act authorises Central Board of Direct Taxes (CBDT) to issue guidelines, for removal of difficulties, with the

approval of the Central Government. These guidelines are required to be laid before each House of Parliament and are binding on the income-tax authorities and the person responsible for paying the consideration for transfer of VDA.

Accordingly, in exercise of the power conferred by sub-section (6) of section 194S of the Act, CBDT hereby issues the following guidelines. These guidelines will apply only in cases where transfer of VDA is taking place on or through an Exchange. In other cases (like peer to peer and others) provisions of section 194S of the Act shall apply and so far as these guidelines are concerned clarifications provided only in Question 6 shall apply.

Guidelines

Question 1. Who is required to deduct tax when the transfer of VDA is taking place on or through an Exchange and payment is made by the purchaser to the Exchange (directly or through broker) and then from the Exchange it goes to seller directly or through the broker?

Answer: According to section 194S of the Act, any person who is responsible for paying to any resident any sum by way of consideration for transfer of VDA is required to deduct tax. Thus, in a peer to peer (i.e. direct buyer to seller) transaction, the buyer (i.e person paying the consideration) is required to deduct tax under section 194S of the Act.

However, if the transaction is taking place on or through an Exchange there is a possibility of tax deduction requirement under section 194S of the Act at multiple stages. Hence, in order to remove difficulties for transactions taking place on or through an Exchange, the following clarifications are issued:

(i) In a case where the transfer of VDA takes place on or through an Exchange and the VDA being transferred is owned by a person other than the Exchange: In this case buyer would be crediting or making payment to the Exchange (directly or through a broker). The Exchange then would be required to credit or make payment to the owner of VDA being transferred, either directly or through a broker. Since there are multiple players, to remove difficulty it is clarified that:

    1. Tax may be deducted under section 194S of the Act only by the Exchange which is crediting or making payment to the seller (owner of the VDA being transferred). In a case where broker owns the VDA, it is the broker who is the seller. Hence, the

amount of consideration being credited or paid to the broker by the Exchange is also subject to tax deduction under section 194S of the Act.

2. In a case where the credit/payment between Exchange and the seller is through a broker (and the broker is not seller), the responsibility to deduct tax under section 194S of the Act shall be on both the Exchange and the broker. However, if there is a written agreement between the Exchange and the broker that broker shall be deducting tax on such credit/payment, then broker alone may deduct the tax under section 194S of the Act. The Exchange would be required to furnish a quarterly statement (in Form no 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962.

(ii) In a case where the transfer of VDA takes place on or through an Exchange and the VDA being transferred is owned by such Exchange: In this case there are no multiple players. The buyer is required to deduct tax under section 194S of the Act. However, there may be a practical issue as the buyer may not know whether the VDA being transferred is owned by the Exchange or not. Hence, there may be genuine doubt in the mind of buyer with regard to its responsibility to deduct tax under section 194S of the Act. This difficulty would also be there if the buyer is buying VDA from an Exchange through a broker.

To remove this difficulty, it is clarified that while the primary responsibility to deduct tax under section 194S of the Act, in this case, remains with the buyer or his broker, as an alternative the Exchange may enter into a written agreement with the buyer or his broker that in regard to all such transactions the Exchange would be paying the tax on or before the due date for that quarter. The Exchange would be required to furnish a quarterly statement (in Form No. 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962. The Exchange would also be required to furnish its income tax return and all these transactions must be included in such return. If these conditions are complied with, the buyer or his broker would not be held as assessee in default under section 201 of the Act for these transactions.

For the purpose of this circular,-

(i) The term "Exchange" means any person that operates an application or platform for transferring of VDAs, which matches buy and sell trades and executes the same on its application or platform.

(ii) The term "Broker" means any person that operates an application or platform for transferring of VDAs and holds brokerage account/accounts with an Exchange for execution of such trades.

Question 2: Question no 1 was with respect to transactions where the consideration for transfer of VDA is not in kind. How will this operate in a situation where it is in kind or in exchange of another VDA?

Answer: According to proviso to sub-section (1) of section 194S of the Act, there could be situations where the consideration is in kind or in exchange of another VDA or partly in kind and cash is not sufficient to meet the TDS liability. In these situations, the person responsible for paying such consideration is required to ensure that tax required to be deducted has been paid in respect of such consideration, before releasing the consideration.

In the above situation, the buyer will release the consideration in kind after seller provides proof of payment of such tax (e.g. Challan details etc.). In a situation where VDA "A" is being exchanged with another VDA "B", both the persons are buyer as well as seller. One is buyer for "A" and seller for "B" and another is buyer for "B" and seller for "A". Thus both need to pay tax with respect to transfer of VDA and show the evidence to other so that VDAs can then be exchanged. This would then be required to be reported in TDS statement along with challan number. This year Form No. 26Q has included provisions for reporting such transactions. For specified persons, Form No. 26QE has been introduced.

However, if the transaction is through an Exchange there is practical issue in implementing this provision. In order to address this practical issue and to remove difficulty, it is clarified that in such a situation, as an alternative, tax may be deducted by the Exchange. Such an alternative mechanism can be exercised by the Exchange based on written contractual agreement with the buyers/sellers.

If such an alternative mechanism is exercised,

(i) the Exchange would be required to deduct tax for both legs of the transactions and pay to the Government. In the Form 26Q it will, for the reasons explained before, need to report it as tax deducted on both legs of the transaction.

(ii) the buyer and seller would not be independently required to follow the procedure prescribed in proviso to sub-section (1) of section 194S of the Act.

When the Exchange opts for deduction of tax under section 194S of the Act on such transactions, there is also a possibility that the tax amount deducted is also in kind and needs to be converted into cash before it can be deposited with the Government. In this regard, the following mechanism shall be adopted by the Exchange

(i) At the time of transaction, the Exchange will deduct TDS in the pair being traded. For example, in case of trade for Monero to Deso, 1% of Monero and 1% Deso will be deducted as tax under section 194S of the Act by the Exchange and balance shall be transferred to the customer. The trail of transactions evidencing deduction of 1% of consideration for every VDA to VDA trade shall be maintained by the Exchange.

(ii) The Exchanges shall immediately execute a market order for converting this tax deducted in kind (1% Monero/ 1% Deso in the above example) to one of the primary VDAs (BT, ETH, USDT, USDC) which can be easily converted into INR. This step will ensure that the tax deducted under section 194S of the Act in the form of non-primary VDAs like Deso/Monero is converted to an equivalent of primary VDAs which have a ready INR market. Time stamps of timing of orders to be maintained to ensure such conversion of VDAs withheld to be done on immediate basis by the Exchange. If the taxes are withheld in primary VDAs, this step would be ignored.

(iii) All the tax deducted under section 194S of the Act in the form of primary VDAs {or converted into primary VDA under step (ii)} will be accumulated for the day. Time limit will be from 00:00 hours to 23:59 hours. VDA accumulation by the Exchange shall be verifiable from the trail of orders for VDA to VDA trades executed during the day.

(iv) The accumulated balance of primary VDAs at 00.00 hours will be converted into INR based on the market rate existing at that time. In order to bring in consistency and to avoid discretion, the Exchanges are required to place market order at 00:00 hours for the tax withheld {or converted under step (ii)} in form of primary VDAs for conversion into INR. These sell market orders shall be executed based on the open buy orders in the market. Price and quantity data for every matched trade shall be maintained by the Exchange and shall be aveilable for

verification. It shall be verifiable from the system coding that the conversion into INR happened at the first aveilable buy order based on the preveiling buy order book of the respective Exchange at the time of conversion. As a practice, the respective Exchange liquidating the VDA shall be prohibited to be a buyer for these VDAs.

(v) Customer will be issued a contract note over email which will include the amount of tax withheld in kind under section 194S and the amount of INR realized from such tax withheld.

(vi) The tax withheld in kind under section 194S of the Act and converted into INR by following the above procedure shall be deposited in the Government Account as per the time line and process given in the Income-tax Rules 1962.

It is clarified that there would not be any further TDS for converting the tax withheld in kind in the form of VDA into INR or from one VDA to another VDA and then into INR.

Question 3: Whether the provision of section 194Q of the Act is also applicable on transfer of VDA?

Answer Without going into the merit whether VDA is goods or not, it is clarified that once tax is deducted under section 194S of the Act, tax would not be required to be deducted under section 194Q of the Act.

Question 4: Whether the consideration for transfer of VDA shall be on Gross basis after including GST/commission or it shall be on "net basis" after exclusion of these items.

Answer: In order to remove difficulty, it is clarified that the tax required to be withheld under section 194S of the Act shall be on the "net" consideration after excluding GST/charges levied by the deductor for rendering service.

Question 5: In transactions where payment is being carried out through payment gateways, there may be tax deduction twice. To illustrate that a person 'XYZ' is required to make payment to the seller for transfer of VDA. He makes payment of one lakh rupees through digital platform of "ABC". On these facts liability to deduct tax under section 194S of the Act may fall on both "XYZ" and "ABC. Is tax required to be deducted by both?

Answer: In order to remove this difficulty, it is provided that in the above example, the payment gateway will not be required to deduct tax under section 194S of the Act on a transaction, if the tax has been deducted by the person ('XYZ') required to make deduction under section 194S of the Act.

Hence, in the above example, if "XYZ" has deducted tax under section 194S of the Act on one lakh rupees, "ABC" will not be required to deduct tax under section 194S of the Act on the same transaction. To facilitate proper implementation, "ABC" may take an undertaking from "XYZ" regarding deduction of tax.

Question 6: Section 194S shall come into effect from the 1st July 2022. The liability to deduct tax under section 194S of the Act applies only when the value or aggregate value of the consideration for transfer of VDA exceeds fifty thousand rupees during the financial year in case of consideration being paid by specified person and ten thousand rupees in other cases. It is not clear how this limit of fifty thousand (or ten thousand) is to be computed?

Answer: It is clarified that,-

(i) Since the threshold of fifty thousand rupees (or ten thousand rupees) is with respect to the financial year, calculation of consideration for transfer of VDA triggering deduction under section 194S of the Act shall be counted from 1st April, 2022. Hence, if the value or aggregate value of the consideration for transfer of VDA payable by a person exceeds fifty thousand rupees (or ten thousand rupees) during the financial year 2022-23 (including the period up to 30th June 2022), the provision of section 194S of the Act shall apply on any sum, representing consideration for transfer of VDA, credited or paid on or after 1st July 2022.

(ii) Since the provision of section 194S of the Act applies at the time of credit or payment (whichever is earlier) of any sum, representing consideration for transfer of VDA, such sum which has been credited or paid before 1st July 2022 would not be subjected to tax deduction under section 194S of the Act.

Circular no. 14 of 2022

Circular no. 14 of 2022
F. No. 370142/29/2022-TPL (Part 1)
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes (TPL Division)

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New Delhi, dated 28th June, 2022

Subject: Order under section 119 of the Income-tax Act, 1961 (the Act) in relation to tax deduction at source under section 194S of the Act for transactions other than those taking place on or through an Exchange

Finance Act, 2022 inserted a new section 194S in the Act with effect from 1st July 2022. The new section mandates a person, who is responsible for paying to any resident any sum by way of consideration for transfer of a virtual digital asset (VDA), to deduct an amount equal to 1% of such sum as income tax thereon. The tax deduction is required to be made at the time of credit of such sum to the account of the resident or at the time of payment, whichever is earlier.

This deduction is not required to be made in the following cases:-

(i) the consideration is payable by a specified person and the value or aggregate value of such consideration does not exceed fifty thousand rupees during the financial year; or

(ii) the consideration is payable by any person other than a specified person and the value or aggregate value of such consideration does not exceed ten thousand rupees during the financial year.

The following are defined as “specified person” for the purposes of this provision:

(i) An individual or Hindu undivided family (HUF) who does not have any income under the head “profit and gains of business or profession”; and

(ii) An individual or HUF having income under the head “profits and gains of business or profession”, whose total sales/gross receipts/turnover from business carried on by him does not exceed one crore rupee or in

case of profession exercised by him does not exceed fifty lakh rupee. This threshold is to be seen in the financial year immediately preceding the financial year in which the VDA is transferred.

Sub-section (6) of section 194S of the Act authorises Central Board of Direct Taxes (CBDT) to issue guidelines, for removal of difficulties, with the approval of the Central Government. Accordingly, in exercise of the power conferred by sub-section (6) of section 194S of the Act, CBDT has issued guidelines in the form of Circular No. 13 of 2022 dated 22.06.2022 for transactions conducted on or through an Exchange. For all other transactions only the clarification provided in answer to question no 6 of that circular is applicable. The term 2 "Exchange" has been defined to mean any person that operates an application or platform for transferring of VDAs, which matches buy and sell trades and executes the same on its application or platform. Same definition applies to this circular.

For all other transactions (not covered by circular no 13/2022), this circular is being issued under section 119 for proper administration of the Act.

1) Liability to deduct tax at source under section 194S of the Act when the consideration is other than in kind

According to section 194S of the Act, any person who is responsible for paying to any resident any sum by way of consideration for transfer of VDA is required to deduct tax. Thus, in a peer to peer (i.e. buyer to seller without going through an Exchange) transaction, the buyer (i.e person paying the consideration) is required to deduct tax under section 194S of the Act. The tax so deducted is required to be deposited with Government in accordance with the time and procedure prescribed in the Act read with the relevant provisions of the Income-tax Rules, 1962.

After deduction, the deductor is required to furnish a quarterly statement (in Form No. 26Q) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962. For specified person Form 26QE has been introduced.

It may be clarified that the TDS shall be on consideration for transfer of VDA less GST.

2) Liability to deduct tax at source under section 194S of the Act when the consideration is in kind or in exchange of VDA

According to the proviso to sub-section (1) of section 194S of the Act, there could be a situation where the consideration is in kind or in exchange of

another VDA or partly in kind and cash is not sufficient to meet the TDS liability. In this situation, the person responsible for paying such consideration is required to ensure that tax required to be deducted has been paid in respect of such consideration, before releasing the consideration.

Thus, the buyer will release the consideration in kind after seller provides proof of payment of such tax (e.g. challan details etc.). In a situation where VDA "A" is being exchanged with another VDA "B", both the persons are buyer as well as seller. One is buyer for "A" and seller for "B" and another is buyer for "B" and seller for "A". Thus both need to pay tax with respect to transfer of VDA and show the evidence to other so that VDAs can then be exchanged. This would then be required to be reported in TDS statement along with challan number by both of them. This year Form 26Q has included provisions for reporting such transactions. For specified persons, Form 26QE has been introduced.

3) Interplay between provision of section 194S and section 194Q

Without going into the merit whether VDA is goods or not, it is clarified that once tax is deducted under section 194S of the Act, tax would not be required to be deducted under section 194Q of the Act.

Notification No. 74/2022, dated 30-06-2022

MINISTRY OF FINANCE
(Department of Revenue)
(CENTRAL BOARD OF DIRECT TAXES)
NOTIFICATION
New Delhi, the 30th June, 2022
(Income-tax)

S.O. 2958(E).—In exercise of the powers conferred by proviso to clause (47A) of section 2 of the Income-tax Act, 1961 (43 of 1961), the Central Government hereby notifies following virtual digital assets which shall be excluded from the definition of virtual digital asset:

(i) Gift card or vouchers, being a record that may be used to obtain goods or services or a discount on goods or services; (ii) Mileage points, reward points or loyalty card, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services; (iii) Subscription to websites or platforms or application.

2. This notification shall come into force from the date of publication in the Official Gazette.

[Notification No. 74/2022, dated 30-06-2022]

Notification No. 75/2022, dated 30-06-2022

MINISTRY OF FINANCE
(Department of Revenue)
(CENTRAL BOARD OF DIRECT TAXES)
NOTIFICATION
New Delhi, the 30th June, 2022
(Income-tax)

S.O. 2959(E).––In exercise of the powers conferred by clause (a) of Explanation to clause (47A) of section 2 of the Income-tax Act, 1961 (43 of 1961) (hereinafter referred as 'the Act'), the Central Government hereby specifies a token which qualifies to be a virtual digital asset as non-fungible token within the meaning of sub-clause (a) of clause (47A) of section 2 of the Act but shall not include a nonfungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

2. This notification shall come into force from the date of publication in the Official Gazette.

[Notification No. 75/2022, dated 30-06-2022]

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