

# A STUDY OF THE LEGAL STATUS OF CRYPTOCURRENCY IN INDIA

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## **ABSTRACT**

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*One of the major changes in technology and finance is crypto currency. Crypto currency has been gaining tremendous amount of attention and growth of crypto currency since 2008 is remarkable. There are various issues associated with cryptocurrency like high volatility, frauds, Unregulated and others. Governments are analysing its effect over economy and taking different approach towards it. In India government has been very sceptical about accepting it. In 2018 RBI imposed ban on VC's and RBI raised red flag related to it. In 2020 SC uplifted the ban and at present government is still analysing and there is no legal frame work regulating it. There various aspects of crypto currency which are yet not explored. There is a huge scope of VCs in future. This paper analysing the legal status of crypto currency In India while analysing the Case of IMAI v. RBI and taxation implication on crypto currency as it is still unclear in India, also compares India's taxation implication with other countries.*

**KEYWORDS:** *Cryptocurrency, Taxation, regulation, decentralised*

## 1. INTRODUCTION

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*“The Web as I envisaged it, we have not seen it yet. The future is still so much bigger than the past.” - Tim Berners – Lee*

Technology has changed the entire world. It has created more opportunities in several aspects. One of the major fields which is benefiting from the technology is economy. Growing number of online users have create a new world. One of the major changes in technology and finance is crypto currency. Crypto currency has been gaining tremendous amount of attention and growth of crypto currency since 2008 is remarkable. Block chain technology is being used as the basic of the cryptocurrency. Story of crypto currency started in 2008 pseudonymous developer Satoshi Nakamoto published a paper titled “Bitcoin: a peer- to-peer electronic cash system”. In 2009 first transaction of Bitcoin took place. In 2011 other crypto currencies started to emerge apart from Bitcoin. Bitcoin act as centre for all other crypto currency. In Initial years crypto currency was criticised for being used for payment on ‘dark web’. Today VC’s have every government eye on it. Capitalization of Crypto in more than 3 trillion. Governments are analysing its effect over economy and taking different approach towards it. El Salvador recently became first country to give crypto currency legal status by declaring it ‘legal tender’. Whereas in Countries like China, Russia and Bangladesh they taken different approach to declare transaction of cryptocurrency as illegal. Third approach is where countries have neither declared it legal nor illegal eg:- India, USA etc. There are various issues associated with cryptocurrency like high volatility, frauds, Unregulated and others. India has been trying to regulate it. Nowadays crypto currency is being used to purchase goods and services. Person can buy a tesla through cryptocurrency. Various artist is accepting crypto as mode of payment. There various aspects of crypto currency which yet not explored. There is a huge scope of VCs in future.

### 1.1 CRYPTO CURRENCY: MEANING

Cryptocurrency means a **digital currency** like rupees, dollars, etc. that is used for buying goods and services just like an ordinary currency but the major difference is this **currency works on an online basis and uses online ledgers** and has very strong cryptography which helps in a **secure online transaction**. There are various types of cryptocurrencies like

Bitcoin, Ether, Polkadot, Ripple, etc Decentralised system is the **block chain technology** which is used to save the transaction history related to cryptocurrency

**Crypto Mining** - Cryptocurrencies are made with help of programming which is known as **mining**. Crypto mining is the process in which transactions between the various users are verified and they are added to the public ledger blockchain. The process of Mining also helps to **introduce new currencies** into the present existing circulating supply and it is one of the main key elements that allow crypto to work as a peer-to-peer decentralised network, without the third involvement (Central Authority).

## 1.2 CRYPTOCURRENCY IN INDIA: A BRIEF BACKGROUND

**The Global Bitcoin Conference 2013** that took place in Bangalore has been changing point in introduction of the cryptocurrency in India. It brought the people together who were supportive towards **BITCOIN**. India's first crypto currency exchange was started in 2013 by Nikkam and Vishwanath called **UNOCOIN**. They had 3000 registered users in less than one year<sup>1</sup>.

On other hand **Reserve Bank of India was not supportive of Bitcoin** and though it has allowed its operations to work. RBI issued pressed release in 2013 cautioning the users holders and traders of virtual currencies, including Bitcoins, regarding risks associated in dealing with such virtual currencies<sup>2</sup>. Also stated that crypto currency was not backed by RBI. In year of 2016 the adoption of crypto currency in India picked up the pace after demonetization was announced. In that year government emphasized on 'Digital India' and that's which spiked the shift from traditional method to using the virtual currency. There were other exchanges which were opened even after the time-to-time notification and notices being issued by RBI cautioning user and traders Like **zeppay, wazirx, coin switch** etc. Number of users were increasing tremendously RBI issued another notification in addition to 2013 press release cautioning users. In 2017 Two PIL's were filed in SC for restricting sale n

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<sup>1</sup>Shivani shinde Nadhe, 'the men behind India's first bitcoin exchange', Business standard (Oct 2 3:21 pm) [https://www.business-standard.com/article/specials/the-men-behind-india-s-first-bitcoin-exchange-114100900750\\_1.html](https://www.business-standard.com/article/specials/the-men-behind-india-s-first-bitcoin-exchange-114100900750_1.html).

<sup>2</sup>Shivani shinde Nadhe, 'the men behind India's first bitcoin exchange', Business standard (Oct 2 3:21 pm) [https://www.business-standard.com/article/specials/the-men-behind-india-s-first-bitcoin-exchange-114100900750\\_1.html](https://www.business-standard.com/article/specials/the-men-behind-india-s-first-bitcoin-exchange-114100900750_1.html).

purchase of virtual currency<sup>3</sup>. In that same year a committee was formed headed by Shri Shubhas Chandra Garg, main aim of committee was to study issues, risk relating to crypto and suggesting actions in regard to the same. In a press release Ministry of Finance stated that '*crypto currency is nothing mere a ponzi scheme*'.

On April 6, 2018 the RBI issued a notification to All commercial banks, NBFC's, Small Finance banks, Payment system provider, payments banks prohibiting on providing any kind of service in relation to VC's<sup>4</sup>. Member of IMAI filed a writ petition in SC for upliftment of ban of crypto currency in India which was imposed by RBI through its notification. In March 2020 Honourable Supreme Court delivered its Judgement and uplifted the ban on crypto currency imposed by RBI<sup>5</sup>.

*India has a lot of potential to become one of biggest market in crypto currency dealing. according to a recent Bloomberg report India ranks fourth in the list of the world's top 10 markets that are most likely to see mass adoption of crypto currency.*

## 2. ISSUES ASSOCIATED WITH CRYPTOCURRENCY

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Status of Crypto currency in every country is very different. Some countries have legalised the use of Crypto currency like El Salvador while, other like India have not even recognised it nor it is illegal in India. Whereas there are some countries like Russia and Bangladesh have declared sale and purchase of crypto currency as illegal. There are some major issues associated with the crypto currency which is why most countries are analysing its effect before regulating it.

### 1. High Volatility and potential for large Losses:

According to Bloomberg report India's has one of the highest crypto owners in the world. Crypto registered users in India have increased since the period of lockdown. The coins have shown unstableness, if we talk about bitcoin in December 2020 the return was over 76% whereas minimum was -38%. So, in case one invests in crypto

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<sup>3</sup>Vipul Kharbanda, '*Crypto currency regulation In India: A Brief History*', the centre for internet and society (Oct 3 5:50 Pm) <https://cis-india.org/internet-governance/blog/cryptocurrency-regulation-in-india-2013-a-brief-history>.

<sup>4</sup>Reserve Bank of India 'Prohibition on dealing in Virtual Currencies' – RBI/2017-18/154.

<sup>5</sup>Vipul Kharbanda, '*Crypto currency regulation In India: A Brief History*', the centre for internet and society (Oct 3 5:50 Pm) <https://cis-india.org/internet-governance/blog/cryptocurrency-regulation-in-india-2013-a-brief-history>.

he might get high returns but may meet high losses as well. In month of May 2021 banks sent notice to their costumers warning them about the use of cryptocurrency and stated the notice of 2018 send by RBI prohibiting virtual currencies.<sup>6</sup> Due to which many coins where all time low.

2. **Decentralised Nature:** Since crypto currency are not issued by government bodies like RBI and the factors on which value of crypto coins is associated is still not clearly known. Whereas Banknotes, coins issued by authorities are valued according to gold stored and economic conditions. Decentralised nature of crypto currency is one major factor why still people around the world are reluctant to invest in crypto currency. Like Bitcoin was introduced by Satoshi Nakamoto and no one knows his real identity and Bitcoin has revolutionised the techno-economic world.
3. **Unregulated:** SEBI is regulatory body for stock exchange. It regulates the shares, debentures, mutual funds, CRA's etc. People invest in stock market just because it is regulated even though they are subject to market risk. Investors feel protected that their interest is protected. Whereas in case of crypto currency are not regulated and not backed by government. Indian government doesn't back crypto currency and time and again RBI has issued warning to consumer over high volatility of the VC's. Since it is unregulated the investors money is not safe if exchange shuts down their money is gone.
4. **Frauds and illegal activities:** RBI in 2018 issued notice to banks and other over prohibition of VC's<sup>7</sup> because they were concerned about the various illegal activities which were done using the cryptocurrency on dark web. Money laundering is one of the major concerns of government in relation to crypto currency. In India it is mandatory to have KYC along with PAN and Aadhar card as identity proof to be registered with crypto exchange but it is not the same case with other countries. It is way to easy to do any transaction in any part of the world as there is no legal frame which includes cryptocurrency in it. Like in case one has to send money to another person who lives in another country through bank then he has to comply with taxation law, FEMA, Banking laws etc. Funding terrorism and trafficking is another concern of RBI. Phishing and spoofing another crypto fraud which is getting prevalent in

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<sup>6</sup>Reserve Bank of India 'Prohibition on dealing in Virtual Currencies' – RBI/2017-18/154.

<sup>7</sup>Reserve Bank of India 'Prohibition on dealing in Virtual Currencies' – RBI/2017-18/154.

today's time. Many times, users are redirected to the fake websites and are required to enter into crypto wallet. That's when they are attacked.

5. **Consumer not protected:** Since crypto currency is not regulated the investors who invest their money their interest is also not safeguarded. If today government passes a bill declaring dealing with cryptocurrency as illegal then the money invested in them is completely lost. If exchange shuts down then as well entire money invested through them in crypto will be lost and they will be stuck in a limbo. Here even the RBI and other authorities cannot protect the interest of consumers as they don't have that jurisdiction.

*There are other issues as well associated with cryptocurrency. RBI has been raising red flags in regard to dealing with VC's. If the interest and economy is kept into mind the government should regulate the crypto currency rather than RBI imposing complete ban. Ministry of Finance has said in press release that government is going to ensure that the interest of crypto investors is protected and government is ready to welcome technological change. But main question remains that why should I invest in something which has high risk associated with it and not backed by government?*

### 3. CASE ANALYSIS ON INTERNET AND MOBILE ASSOCIATION OF INDIA VS THE RESERVE BANK OF INDIA<sup>8</sup>

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#### Background and Facts of the case

The abovementioned case revolved around the main issue regarding the validity of virtual currency or crypto currency. The cause of action of the said case arose with the statement issued by The Reserve Bank of India on 5<sup>th</sup> April 2018, which was followed by a circular dated 6<sup>th</sup> April 2018. The para no. 13 of the said circular prohibited the use and dealing in Virtual Currencies or Crypto Currencies by the banks and other financial institutions and such other entities duly regulated by it. Further the institutions were barred from providing

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<sup>8</sup>Writ Petition (Civil) No.528 of 2018. D/d. 04.03.2020

any such services to any individual or entity. The said ban / prohibition resulted a total stop of the channels that converted of Fiat money into Virtual / Crypto Currencies. All accounts maintained in such regard were also non-maintainable. The Reserve Bank of India, since 2013 had been cautioning the banks and the investors about the legal and security risks involved in the Crypto / Virtual Currency Transactions. The major grounds laid down by the RBI for the said ban were:

- i) Hacking
- ii) Recession
- iii) Fraud
- iv) Promotion of terror activities

The reserve Bank of India, since 2013 through its public notices on December 24, 2013, February 01, 2017 and December 05, 2017 had cautioned the investors about the abovementioned threats / risks associated with dealing in crypto / virtual currencies. Further, the investors were against the abovementioned ban as the grounds of ban were already known to them since 2013 and no new grounds were added. The investors were already investing and were ready to invest more and take the risks involved.

Internet and Mobile Association of India, a Non-Profit Organization which represents the interests of people who are involved in online and digital service industry had filed the abovementioned case against The Reserve Bank of India on the grounds that the Defendants / RBI does not have the power to pass / make any rules in regard to the Virtual Currencies. The petitioners further added that these currencies are mere exchange mediums and not be confused with any kind of legal tender and the RBI has no jurisdiction / power to regulate the same. According to the petitioners the said ban had also infringed Article 19 (i) (g) of the Constitution of India, 1950 which empowers the citizens of the country to practice any profession, occupation or trade of their own choice.

The RBI in the response to the said petition replied stating that; as per the Article 19 (i) (g) of the Constitution of India, 1950 the citizens of the country have a fundamental right to practice any profession, occupation or trade of their own choice, but the said right is not absolute in nature and reasonable restrictions can be imposed over the use of the said fundamental right. It was further added by the RBI that the said ban was reasonable as it protected the larger public interest and these are the preventive measures to safeguard the public from the risks

involved in dealing of Crypto / Virtual currencies. It was further submitted by the RBI that the Crypto / Virtual currencies are accepted as a valid mode of payment / transaction by a number of people and institutions and once a currency is accepted as a valid mode of payment / transaction, it becomes a Legal Tender and the RBI has the power to issue a circular in regard to any legal tender.

### Issues

- i) Whether the RBI encompass within its ambit the power to regulate Crypto / Virtual currencies as they are merely an exchange medium and not a legal tender.
- ii) If RBI has the power to regulate the Crypto / Virtual currencies, the said circular infringed the rights of the petitioner or not.

### Learned Court's findings and judgement

In regard to the *first issue*, the court determined the definition of money. The Id. Court on determining the judgements and findings of the courts of United Kingdom, United States of America, and Singapore asserted four hallmarks to define money. "Money –widely accepted medium of exchange , a unit of account,a store of value and serving final discharge of debt and a. It was added by the Id. court that the first three points social sense characteristics, whereas the fourth is a legal tender characteristic. It was further added by the Id. court that the Crypto / Virtual currencies had the first two characteristics, but it is not widely acceptable. And are not capable of being classified as money in social sense. Further, while equating Crypto currencies to fiat money or a legal tender, the Id. court was reluctant is accepting the contention that Crypto currencies can never be regarded as real money. It is of no doubt that the Crypto / Virtual currencies can be converted into the real money, but the economy of our country cannot support it to become a legal tender. The Id. court added that it is under the RBI being the apex financial system regulator has the power to deal with something that is not equivalent to currency but in certain cases can be functioned as one.

In regard to the *second issue*, the Id. court used the Proportionality Doctrine to determine whether the said circular infringed the rights of the petitioners. With the use of the Doctrine of Proportionality, the court determined whether the extent of restriction imposed and the right are protected by it are proportionate or not. The Id. court further came to the conclusion that the said ban on the use of Crypto / Virtual currencies was an extreme and an unrequired



measure. The Reserve Bank of India had numerous other options to reduce the risks involved in the Crypto / Virtual currencies, the mere regulation and knowledge to the investors and general public would have been enough. The Id. court here referred to the **Report of the European Union Parliament, titled Cryptocurrencies and Blockchain** of July 2018. Which suggested that putting a full ban on the use of Crypto / Virtual currencies is not required when the government of a country has a number of less harsh measures available to deal with the risk and impose restrictions. For instance, The Reserve Bank of India can impose the self-registration clause according to which every investor shall register himself and it would help the RBI to keep a record of the transactions done by that investor. The Id. court had further submitted that the ban imposed by the RBI on the use of Crypto / Virtual currencies is disproportionate and unreasonable and RBI has not even reported one single case of loss or any other adverse effect due to the use of Crypto / Virtual currencies on the entities regulated by the RBI. The Id. court had cited '**State of Maharashtra vs. Indian Hotel and Restaurant Association**'<sup>9</sup> stating that the party has to show some degree of damage in order to get a judgement in their favour.

*The court has handed down its decision and upheld the relaxation of the prohibition on the use of crypto and virtual currencies. "The court was of the opinion that although RBI has wide powers and does play an important role in the upliftment of the Indian economy, here they are unable to show any sought of damage suffered by its regulated entities. This is despite the fact that RBI does plays an important role in the upliftment of the Indian economy. Therefore, the recommendations that were issued by the RBI, asking the banks to cease dealing or providing services to the businesses trading in crypto or virtual currencies are unlawful, and as a result, they cannot be enforced.*

#### **4. SCENARIO AFTER UPLIFTMENT OF BAN FROM CRYPTOCURRENCY**

- **Growth of Crypto Currency Market**

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<sup>9</sup>State of Maharashtra vs. Indian Hotel and Restaurant Association(2013) 8 SCC 519.

After upliftment of ban the crypto market can grown exponentially. According to WazirX, Indian Crypto Exchange its trading volume has grown over by 16,000% since March 2020.

- **RBI and bank's reaction on crypto**

SBI and HDFC bank and other regulated entities in month of may 2021 have cautioned their customer against dealing with cryptocurrency by referring to April 2018 notification. Due to this many crypto investors sold their cryptocurrency which led to low time low value of crypto coins. Investors were stuck in limbo as banks were disabling the payment options across crypto exchanges and were sending notices. RBI on 31<sup>st</sup> May 2021, clarified that the banks cannot refer to 2018 notice<sup>10</sup> But stated that banks in carrying out customer due diligence can notify customers to comply with regulations.<sup>11</sup>

On September 2021, SBI blocked its UPI on crypto exchanges from receiving funds. Even HDFC and ICICI banks blocked payment to crypto using their UPI. Despite the SC judgement uplifting the ban the banks are reluctant over providing services for cryptocurrency dealing.

- **Government's stand on cryptocurrency:**

In March 2021, Ministry of Corporate Affairs amended the schedule III of the companies act 2013. It came into effect on 1<sup>st</sup> April 2021. According to this amendment if any company has invested or traded in crypto currency then that company needs to show amount of currency held in its reporting, profit and loss arising out of crypto and deposit or advance for purpose of trading or investing in VC's<sup>12</sup>.

**The cryptocurrency and regulation of official Digital currency bill, 2021** was supposed to be introduced by government in monsoon session but was not tabled in that session. According to bill it would issue a complete ban on cryptocurrency and punish any violation with 10 years imprisonment or fine or both. But the Finance Minister, Smt. Nirmala Sitharaman in recent press release said that government is going to take a 'calibrated approach' regulating crypto currency rather than imposing

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<sup>10</sup>Reserve Bank of India 'Prohibition on dealing in Virtual Currencies' – RBI/2017-18/154.

<sup>11</sup>Reserve Bank of India, 'customer due diligence for transaction in VC's, DOR.AML.REC 18/ 14.01.001/ 2021-22.

<sup>12</sup>Ministry of Corporate Affairs, (Oct 14, 2021 4:31pm)<https://pib.gov.in/PressReleaseIframePage.aspx?PRID=1744542>.

complete ban. There is no complete clarity over what exactly is going to be status of crypto currency in coming future.

Ministry of Finance in Month of September 2021 has **formed a panel to examine the scope of taxation** on income generated from cryptocurrency trading and mining. Panel is to analyse the nature of income from different activities of cryptocurrency. Panel is required to submit report within 6 months.

## 5. TAX IMPLICATION OF CRYPTOCURRENCY IN INDIA

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As we know every person<sup>13</sup> who falls under the tax slab rate has to file the income tax return annually. He is supposed to pay certain rate of tax on his income shown in the IT returns. Tax levied on the “total income” of each assessee<sup>14</sup>. As detailed under **section 14** of IT act Total Income under income tax is computed under five heads: profit and gains from business or profession, capital gains, Salaries, income out of other sources and Income from house property.

There is an exponential growth in the cryptocurrency market in India specially after the upliftment of ban on it. Crypto currency is being mined, it is being used for purchasing or selling, as investment and gains. People are actually making good amount of returns out of crypto currency. Major concern of people is that they are not aware about the tax they have to pay for transactions of crypto currency in India and what is going to be its future here. As Indian government and RBI have been every much reluctant over the acceptance of crypto currency. It has not been recognised as legal tender by RBI. Legal tender is money which is recognised by state as legally valid for payment the debt or any other financial obligation<sup>15</sup> like in India, INR is legally accepted currency. Since it is not recognised and there is no transparency over the tax aspect of cryptocurrency by government.

Earlier to March 2021 people were not even sure if they have to pay tax over their crypto activities. Government has been regularly assessing the crypto currency’s impact on economy and growth. In March 2021 **Anurag Singh Thakur** (Minister of state of

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<sup>13</sup>The Income- Tax Act 1969, S. 2(31).

<sup>14</sup>The Income -Tax Act 1969, S. 2(7).

<sup>15</sup>Merriam webster, Legal tender (Oct 3, 2021, 18:32 pm)  
<https://www.merriam-webster.com/dictionary/legal%20tender>.

Finance) clarified in the conference that “*the gains from the crypto currencies are subjected to tax under the head of income depending completing upon the nature of holding of it*”<sup>16</sup>. Even the IT department is in favour of taxing the income generated from it, based upon the activity. As it is going to add up to economic ecosystem of the country.

**RBI Deputy Governor, R Gandhi** said that *payments on crypto currency should be paid through the normal manner, in case not paid through normal manner then it should be considered to be mined and capital gains tax on it must be levied. It should be like a voluntary disclosure and it should be tracked properly through the authorities.*<sup>17</sup>

**It is important to note that ‘All income except which explicitly exempted under IT act are shown and taxed’.**

## 5.1 TAX IMPLICATION UNDER THE IT ACT, 1961

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As earlier stated, that the government and taxation authorities instead of giving full disclosure of information and any official notification have just stated that crypto currency activities are taxable based upon the nature of activity. So, it is important to understand the nature of activities related to crypto- currency in context with heads of income to get better understanding of how it is to be taxed as it is not exempted under the act.

**CAPITAL GAINS: As detailed under section 45** of the IT act any gain which arise from capital asset transfer during previous year is to be taxed under head of capital gains. Conditions under 45<sup>th</sup> section are that there should be capital asset<sup>18</sup>. Secondly, it should be transferred by the assessee<sup>19</sup> and transferred must have taken place during previous year<sup>20</sup>. Thirdly, profit or gain must arise as result of the transfer done by assessee.

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<sup>16</sup>Miamnsa Verma, ‘Thinking of buying cryptocurrencies? Be ready to pay taxes on your investment gains’ Scroll.in, (Oct 9, 2021 4:30pm) <https://scroll.in/article/1004892/thinking-of-buying-cryptocurrencies-be-ready-to-pay-taxes-on-your-investment-gains>.

<sup>17</sup>Ruchi Bhatia, ‘India looking to tax crypto trades, ecosystem (Oct 05 ,2021 10:53 am) <https://www.timesnownews.com/business-economy/economy/article/india-looking-to-tax-cryptocurrency-trades-ecosystem/811388>.

<sup>18</sup>The Income Tax Act 1969 Section 2(14).

<sup>19</sup>The Income Tax Act 1969 Section 3 "previous year" means ‘the financial year, immediately preceding the assessment year: Provided that, in the case of a business or profession newly set up, or a source of income newly coming into existence, in the said financial year, the previous year shall be the period, beginning with the date of setting up of the business or profession or, as the case may be, the date on which the source of income newly comes into existence and ending with the said financial year’.

<sup>20</sup>-----tax book \_\_\_\_

*Capital assets are of two type long term and short-term capital asset.*

If a person is holding up the crypto currency for **purpose of investment**, then any gain arising out of it will be considered as capital gain as it will be treated as capital asset. Holding period is very important under capital gains. **Crypto currency can only be taxable as long term capital gains if they are held for a period of 3 years or more.** If an assessee receives a gain after holding a crypto currency for less than (3 years) 36 months then it would be taxable as short-term capital gains. Tax on short term gains is paid according to the tax slab rate notified by the income tax authorities. Whereas, tax for long term gains is paid at rate of **20% with benefits of indexation.**<sup>21</sup> The tax rate can decline after indexation benefit has been applied as it allows the investor to adjust, for inflation during the period crypto currency was held as investment. Under the income tax act capital assets are also defined to be property of any kind and it is likely to cover crypto currencies as discussed earlier.

As a result of clarifications provided by the Central Board of Direct Taxes with regard to the classification of shares as capital assets or stock-in-trade, it may be possible to take the view that crypto currency sold by consumers is a capital asset. This is because the classification of shares as capital assets or stock-in-trade was previously unclear. Despite the fact that a merchant may potentially see them as stock in trade, and if they are regarded as stock-in-trade, then taxes would need to be paid on the consideration received under the category of commercial income.<sup>22</sup>

## 5.2 PROFIT AND GAINS FROM BUSINESS AND PROFESSION

Under **Section 2(13)** of the Income Tax Act, the definition of **business** includes “any trade, commerce, manufacturing, or concern of such nature”. Continuous activity in nature of trade of crypto currency does fall under definition of business. *Profits from business or income derived from the trade is chargeable to tax under the head of “profits and gains of business and profession”.*<sup>23</sup> So it can be said that when a person **substantially and frequently** does transaction of the crypto currency then it can be said that he is trading in crypto currency. Income from the sale of the cryptocurrency is taxable under this head of income.

<sup>21</sup> Amit Gupta, ‘Investing in cryptocurrencies? Know the tax implications’, Economic Times (Oct 10, 2021 05:20 PM) [https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-taximplications/articleshow/84113085.cms?utm\\_source=contentofinterest&utm\\_medium=text&utm\\_campaign=cppst](https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-taximplications/articleshow/84113085.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst).

<sup>22</sup> Nishchal Joshipura & Meyyappan Nagappan, ‘Crypto currency – regulatory & taxation issue’, 4 The Chamber’s International Tax Journal 86, 89 (2018).

<sup>23</sup> The Income- Tax Act 1969, S. 28.

If treated as business income then sale of crypto currency needs to be reported under ITR-3 part A- Trading account under sales of goods. Net profit or loss from sale of cryptocurrency after reducing the permissible expenses is to be reported under “net profit before taxes”.

As earlier stated, if crypto currency is treated as stock-in-trade even then the taxes payable on consideration received under business income.<sup>24</sup>

Crypto currency if received for on sale of good and services will also be taxed under the business income. Like recently Rapper Raftaar announced that he is accepting crypto currency for his services. For example, if he receives crypto currency for his services then that income has to be taxed and according to me after analysing the above section it is to be reported under profits and gain from business and profession.

**OTHER SOURCES:** As defined under section 56 of the ITA any income which does not fall under any other income head comes under other source of income. Under this head crypto through mining and receiving cryptocurrency as a gift is discussed. The gift is one of the eleven incomes which is always taxed under the head “income from other sources”.<sup>25</sup>

- **Receiving the Cryptocurrency as a gift:** Section 56 (2)(5) of ITA states that if money is received without consideration by any person<sup>26</sup> will be considered as a gift and that will be taxed under the other source of income if the gift received is worth Rs 50,000 or more. It is taxed at individual slab rates if more than Rs 50,000.
- **Mining of Crypto Currency:** Cryptocurrency if mined is a self generates capital assets, then it is supposed to be taxed under capital gains but section 55 of ITA deals with the cost of acquisition and cost of improvement of capital assets and doesn't include mining in any sense under the section<sup>27</sup>. It is not covered under salary, profits or gains from business and profession, income from the house so only left income is “income from other sources”. Even though it is seen as a

<sup>24</sup>Amit Gupta, 'Investing in cryptocurrencies? Know the tax implications', Economic Times (Oct 10, 2021, 05:20 PM) [https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-tax-implications/articleshow/84113085.cms?utm\\_source=contentofinterest&utm\\_medium=text&utm\\_campaign=cppst](https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-tax-implications/articleshow/84113085.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst).

<sup>25</sup>The Income Tax Act 1969 S.56.

<sup>26</sup>The Income- Tax Act 1969, S. 2(31).

<sup>27</sup>The Income Tax Act 1969 S.55(2).

capital asset if generated but as of now it cannot be covered under sections 55 and 45 of ITA.

### 5.3 ADDITIONAL REPORTING REQUIREMENT UNDER INCOME TAX RETURN

If a taxpayer has net taxable income exceeding Rs 50 lakh then he is required to disclose their assets and liabilities in schedule assets and liabilities along with the cost acquisition. If we consider cryptocurrency as assets then taxpayers also have to include cryptocurrency in the schedule.

Currently, there is no guidance on requirement to report cryptos in schedule AL of the currently notified ITR forms.<sup>28</sup> Taxpayers who are resident and ordinary resident have to disclose foreign assets and income from it under Schedule FA "Details of Foreign Assets and Income from any source outside India"<sup>29</sup>. Again, we need to keep in mind that there are no clear guidelines given by authorities whether crypto is to be considered as foreign assets or not.

- ❖ *These are to be considered as opinion and not a professional advice.*
- ❖ *Clarity is still needed over this aspect from authorities as above-mentioned paras are mere analysis of activities related to cryptocurrency in context with the heads of income. As we know that Indian government and concerned authorities are still analysing overall effect of crypto currency if legalised. Government needs to notify how it is going to categorise the activities under various heads of income soon as there is widespread use of crypto currency. It is also important to note down here that paying tax over the income from crypto currency doesn't mean it is legalised in India.*

### 5.4 TAX IMPLICATION UNDER GST, 2017

Firstly, it is important to analyse the nature of crypto currency to know under which category does it fall in. According to CGST Act section 2(101) which says that "**securities**" will have

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<sup>28</sup>Homi Mistry, 'How to report profits and losses in income tax return', Economics Times (Oct 3, 2021 10:53 pm) [https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-tax-implications/articleshow/84113085.cms?utm\\_source=contentofinterest&utm\\_medium=text&utm\\_campaign=cps...](https://economictimes.indiatimes.com/markets/cryptocurrency/investing-in-cryptocurrencies-know-the-tax-implications/articleshow/84113085.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cps...)

<sup>29</sup>Id.17.

same meaning as assigned under section 2(h) of SCRA,1956 which says that securities include shares, bonds, debenture stock or other securities of any incorporated company, derivatives, govt. securities, units issued under mutual fund scheme. *Through this definition we can clearly see that crypto currencies cannot fall under the definition of securities.* Cryptocurrency are not issued by the central authorities who undertakes to repay the value represented by the unit of cryptocurrency.<sup>30</sup>

According to Section 2(52) of CGST “**goods**” means every kind of movable property other than money and securities.<sup>31</sup>As already discussed crypto currency is not a security and it cannot be money as well since it is not recognised as legal tender by Indian government. Movable property is property which can be moved from one place to another and which is not fixed. Cryptocurrency does fall under definition of securities or money. But since it is movable and not immovable in nature and definition of goods clearly mentions “*every kind of movable property*”<sup>32</sup>. **Crypto Currencies are likely to qualify as goods as per definition under CGST.**

Now if we look at the definition of the “**Consideration**” in relation to supply of goods or services given under Section 2(31)<sup>33</sup> it says that payment made or to be made whether in money or otherwise....”<sup>34</sup> The word otherwise in the definition indicates that payment can be made in kind. We can say that transaction can be like barter. So, paying a person for receipt of supply of goods and service in crypto currency will come under definition of consideration. Accordingly, the GST will be applicable.

There is little illumination on the barter transaction due to the fact that the GST legislation in India is still in the process of developing. There are problems that come up when something is qualified as a barter transaction. In practise, if an Indian consumer pays for goods or services using crypto currency, the Goods and Services Tax (GST) can apply on two levels:

- i. the customer is responsible for paying GST on the acquisition of crypto currency upon payment, and

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<sup>30</sup>Sudipta Bhattacharjee & Onkar Sharma, ‘Cryptocurrency: Key GST Aspects in India and Path Ahead’, Taxsutra, (Oct 5, 2021 00:46 am) [https://www.khaitanco.com/sites/default/files/2021-04/Cryptocurrency\\_%20Key%20GST%20Aspects%20in%20India%20and%20Path%20Ahead.pdf](https://www.khaitanco.com/sites/default/files/2021-04/Cryptocurrency_%20Key%20GST%20Aspects%20in%20India%20and%20Path%20Ahead.pdf).

<sup>31</sup>The Central Goods and services Tax Act 2017 S 2(52).

<sup>32</sup> Id. 20

<sup>33</sup>The Central Goods and services Tax Act 2017 S 2(31).

<sup>34</sup>The Central Goods and services Tax Act 2017 S 2(31).



- ii. GST can be applicable on the purchase of goods or services that have been paid for using crypto currency.<sup>35</sup>

Due to the fact that crypto currency does not have a physical location, it will be impossible to determine if the supply of cryptocurrency is coming from another state or from inside the same state. This is one of the key problems. Taxation and commerce would both be affected as a result of this.

According to reports, the government is reportedly contemplating imposing a 2 percent equalisation charge on transactions conducted with international cryptocurrency exchanges. The Goods and Services Tax (GST) is equivalent to the trading cost that users of cryptocurrency exchanges in India are required to pay. This arrangement is comparable to that of stock brokerages.<sup>36</sup>

## 6. INTERNATIONAL TAX PRACTICE

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- ❖ Australia: Capital gain tax is levied on cryptocurrency in Australia. When a person disposes of its cryptocurrency in manner of sell, gift, trade, exchange converting crypto currency into Fiat currency or using it for the goods/services then CGT is levied. When a person disposes it, capital gain received is basically taxed. a digital wallet containing different types of cryptocurrencies, each cryptocurrency is a separate CGT asset<sup>37</sup>.Holding crypto currency as investment for 12 month or more then person is entitled to CGT deduction.A new crypto held in business for sale or exchange for daily course of business then it is to be treated as trading stock.
- ❖ United Kingdom: In the United Kingdom, cryptocurrencies are regarded as assets. The HMRC had only lately made available a guide to cryptography. This guide provides an accurate explanation of how crypto assets should be handled. Manual should also

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<sup>35</sup>Sudipta Bhattacharjee & Onkar Sharma, 'Cryptocurrency: Key GST Aspects in India and Path Ahead', Taxsutra, (Oct 5, 2021 00:46 am) [https://www.khaitanco.com/sites/default/files/2021-04/Cryptocurrency\\_%20Key%20GST%20Aspects%20in%20India%20and%20Path%20Ahead.pdf](https://www.khaitanco.com/sites/default/files/2021-04/Cryptocurrency_%20Key%20GST%20Aspects%20in%20India%20and%20Path%20Ahead.pdf).

<sup>36</sup>Miamnsa Verma, 'Thinking of buying cryptocurrencies? Be ready to pay taxes on your investment gains' Scroll.in, (Oct 9, 2021 4:30pm).

<sup>37</sup>Australian Taxation Office, 'Transacting cryptocurrency' (Oct 12,2021 01:56 am) [to.gov.au/general/gen/tax-treatment-of-crypto-currencies-in-australia---specifically-bitcoin/?page=2#Exchanging\\_crypto\\_currency\\_for\\_another\\_crypto\\_currency](https://www.ato.gov.au/general/gen/tax-treatment-of-crypto-currencies-in-australia---specifically-bitcoin/?page=2#Exchanging_crypto_currency_for_another_crypto_currency).

clarify how taxes are applied to crypto assets. When they sell their crypto tokens, individuals who hold crypto as an investment may be liable to capital gains tax. The manual makes it quite clear that VAT must be paid on any and all products and services received in return for cryptocurrency exchange tokens. There will be no need to pay VAT on the transaction of the token, and the value of the supply of goods or services for which VAT must be paid will be determined by the value of the pound sterling at the time of the transaction.

- ❖ USA: In the United States of America, it is mandatory for taxpayers to report any transactions that include bitcoin. The IRS has made it clear that every transaction, regardless of its size or value, must be recorded. The Internal Revenue Service (IRS) has indicated, in its report, that taxpayers who provide inaccurate information about their income might face fines or possibly criminal prosecution. In the United States of America, crypto money is considered an asset. Any gain derived from the holding of crypto currency for less than a year is subject to taxation at the highest marginal tax rate applicable to taxable income. Any loss may be used to offset income tax up to a maximum of three thousand dollars, and any further losses are carried over to the next year. If crypto assets holding period is more than 1 year then the tax rate is lower, between 0% to 20%.<sup>38</sup>
- ❖ Germany: In Germany the cryptocurrency is viewed as private asset.<sup>39</sup> It attracts income tax rather than a Capital Gains Tax. Important point in Taxation of Cryptocurrency in Germany is that tax is levied only if crypto currency is sold within the year of buying it. Basically, Germany taxes the gains from short term gains under German Tax Act. Mining and staking are also taxed in Germany. What sets Germany aside from other countries like USA, Canada, Australia etc is that here crypto currency is classified as 'other assets' and not as a property. Selling it falls under 'private sale' and private sale of assets holds tax benefits in Germany like holding the crypto for more than one year then gains from sale are exempted from tax<sup>40</sup>. Holding period of crypto is very important. Another key point in German Taxation is that profits from

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<sup>38</sup>Sneha Kulkarni, 'How bitcoin is taxed around the world', (Oct 12,2021 2:21 am) <https://www.goodreturns.in/personal-finance/taxes/how-bitcoin-and-other-cryptocurrencies-are-taxed-around-the-world-1213422.html>.

<sup>39</sup>Germany Crypto Tax Guide, 2021' (Oct 12,2021 3:45 am) <https://koinly.io/guides/crypto-tax-germany>.

<sup>40</sup> Sneha Kulkarni, 'How bitcoin is taxed around the world', (Oct 12,2021 2:21 am).

crypto sales up to 600 euro per year remains tax free<sup>41</sup>. Crypto Mining is viewed as business activity.

Tax free activities of crypto currency in Germany includes buying crypto, coin swaps and transaction of crypto currency from one wallet to another if one owns it as gift or donation.

- ❖ Singapore: country doesn't have capital gain tax which means that individual or companies holding cryptocurrency are not liable to pay any tax on it. But companies who does regular transaction in cryptocurrency in form of accepting payments or in trading then such company is suppose to report such income and income tax is levied over such income. But authorities consider cryptocurrency as 'intangible property' and not treat it as a legal tender as discussed earlier in context of India as well that transaction from 'intangible property' will form part of a barter transaction here goods and services are taxed not the token<sup>42</sup>.
- ❖ China: In China all VC's transaction are illegal since 24 sept 2021.

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## 7. RECENT PROPOSAL RELATED TO TAXATION IN INDIA

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Recently, the Central Economic Intelligence Bureau (CEIB) has made a suggestion to the Central Board for Indirect Taxes and Customs (CBIC) to include cryptocurrency exchanges and platforms under the scope of the Goods and Services Tax (GST). The following are some of the most important aspects from the publicly accessible CBIC proposal:-

- The proposal suggests that mining cryptocurrencies might be considered a supply of service since it results in the creation of new crypto money and qualifies as an intangible asset, which is subject to a GST rate of 18 percent. This is because mining creates new crypto currency.

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<sup>41</sup> 'Germany Crypto Tax Guide, 2021' (Oct 12, 2021 3:49 am) <https://koinly.io/guides/crypto-tax-germany>.

<sup>42</sup> Adriana hamacher & Stephan Graves, '11 countries who don't tax crypto', decrypt (Oct 12 08:42 pm) <https://decrypt.co/43513/countries-that-dont-tax-bitcoin-gains>.

- The proposal also recommended that individuals who mine cryptocurrencies as cryptocurrency miners would be forced to register under GST if their yearly income is more than 20 lakh. This requirement would apply to cryptocurrency miners.
- Activities such as storing, transferring, accounting, and selling of crypto are also likely to be recognised as an act of supply and might be taxed in the future. The transaction fee on currency that is being mined will be subject to GST. Cryptocurrency mining will be subject to GST.
- In situations in which both the buyer and the seller are registered as Indian residents and operators, the transaction that is carried out between them should be regarded as a supply of software. On the other hand, international transactions carried out by companies registered in India will be regarded as either the import or export of goods, and IGST will be applied to such transactions because they are subject to taxation if they meet the requirements.<sup>43</sup>
- One of the main reasons to bring crypto currency under GST umbrella is to prevent money laundering and other illegal activities.

*Some points mentioned in proposal are not in sync with global tax practice. Indian government should provide clarity over the taxation issue. There is need of robust taxation system in relation to crypto currency. Taxpayers cannot evade from paying taxes as it is penal offence. Like UK, Australia, Germany and others hope clear guidelines will be issued soon to taxpayers so that crypto currency investors are aware of the tax implication over various activities involving cryptocurrency.*

*It will give force to 'crypto currency wave'. This will ensure stability and taxes from cryptocurrency can add to economy and the development of the country.*

The Finance Bill of 2022 has inducted Section 194S in the Income Tax Act, 1961, according to which 1% TDS will be levied on any consideration which will be paid for the transfer of Virtual Digital Assets (VDA) like Crypto. The same shall be made applicable from July 1<sup>st</sup>, 2022 and TDS will be deducted in trade wherein Crypto is exchanged for another Crypto Asset or INR.

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<sup>43</sup>Sudipta Bhattacharjee & Onkar Sharma, 'Cryptocurrency: Key GST Aspects in India and Path Ahead', Taxsutra, (Oct 5, 2021 00:46 am).

In simpler words, the person buying Crypto by the use of INR, need not pay any TDS. But on the other hand, the seller of such Crypto is liable to pay the applicable TDS amount. In case both the parties use Crypto asset to complete the transaction, the seller and the buyer, both are liable to pay TDS. While in P2P transactions, at the time of placing the sell order before the USDT, TDS will be deducted, but the same shall not be payable by the USDT buyer.

According to Section 206AB of the Income-Tax Act, 1961, if in the last two years the user has not filed an Income Tax Return and the TDS amounts to be ₹50,000 or more in both the individual year, then in such situation 5% TDS shall be deducted for such crypto related transactions.

The amounts deducted as TDS shall now only be visible after a period of 48 hours from the transaction. Furthermore, in case an order is placed before July 1<sup>st</sup>, 2022, but the same is executed after the said date, TDS will be applicable.

## 8. CONCLUSION

Cryptocurrency is coming future of the world. As we are moving more and more towards technology and digitalisation. Accepting of virtual currency innear future is definitely possible. If in 90's anyone would have told that after a decadeinstead of having currency we could do net banking and transfer money just with a click no one would have believed similarly if we deny that virtual currency is not going to be accepted and has no future then, I feel we are wrong because despite all the issues associated with crypto currency yet its growth is tremendous. Government should try to regulate it instead of banning it. If a country puts a ban and other countries accept it then it will a step backward from developing and growing of country in term of technology and economy. Time and again Indian government this year has specified that they are going to protect the crypto exchange interest and investors interest as well. Which point into the direction that government may take a middle path rather than imposing blanket ban.

If government regulates the cryptocurrency number of investors will increase. As investors in stock market feel safe despite market risk because it is regulated by SEBI and in case of any dispute investor can go to SEBI or Court to resolve its matter. Investors will have more trust on crypto currency which is not possible when there is absence of legal frame work.

Whereas if we talk about taxation aspect, as per the Finance Bill of 2022 has already levied 1% TDS on Crypto transactions.