

# Taxability of Virtual Digital Assets - An Overview

Defining Virtual Digital Assets and their taxability under the new provisions of the Income Tax Act.

## Introduction

Virtual Digital Assets, especially cryptocurrencies & Non - Fungible Tokens (NFTs), have gained tremendous popularity in recent times and the volumes of cryptocurrency trading has increased substantially. To bring clarity on such asset classes, the government has proposed to define virtual assets, provided for taxation rules on such assets, viz., taxes on income arising out of virtual assets, and TDS in the recent Union Budget 2022.

Virtual Digital Assets - Defined

Virtual Digital Assets (VDA) shall include

1. any information or number or token, generated through cryptographic means or otherwise, providing a digital representation of value exchanged with or without consideration, with the promise or representation of having inherent value or
2. 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.
3. Also, includes a non - fungible token or any other token of similar nature; and
4. any other digital asset, as the central government may by notification specify it in the official gazette.

**Income from transfer of any virtual digital assets shall be taxable at the rate of 30%.**

## Taxation on Virtual Digital Assets Transfer

In the Finance Bill 2022, a new Section 115 BBH has been proposed to be introduced with regard to taxation of Virtual Digital Assets.

1. In Section 115 BBH, the income from transfer of any virtual digital assets shall be taxable at the rate of 30%.
2. No deduction in respect of any expenditure except cost of acquisition shall be allowed while calculating tax under Section 115 BBH. Hence the word cost of acquisition has been used in Union Budget 2022 so no indexation would be allowed in case virtual digital asset is held by assessee more than thirty six months.
3. No set off of any loss from transfer of the virtual digital assets shall be allowed against income computed under any other provision of the act.
4. No loss on account of digital virtual asset shall be carried forward to succeeding assessment years.
5. Also, gifting of virtual digital asset shall be chargeable as income in the hands of the recipient under the head Income from other sources. Gifting of virtual digital asset may also result in taxation in the hands of transferor at the rate of 30% in the absence of any exemption.

# Withholding Tax on Virtual Digital Asset

Another aspect which was considered in the Finance Bill 2022 with regard to Virtual Digital Asset was of withholding tax to be charged on Virtual Digital Assets. Thus, a new Section 194S has been proposed under the Finance Bill 2022 .

1. As per Section 194S, any person responsible for paying to a resident, any sum of money by way of consideration for transfer of virtual digital Asset, shall deduct TDS at the rate of 1%. Deduction shall be made at the time of credit of such sum to the account of resident or at the time of payment of such sum by any mode, whichever is earlier.
2. The TDS shall be deducted for only such transactions that are of value exceeding INR 50,000/- in the financial year. A provision w.r.t. transactions with specified persons are also dealt with. In case consideration is payable by a person other than specified person, then no tax shall be deducted where consideration value does not exceed INR 10,000/- during the financial year.

*\*Specified persons means a person being an individual or HUF, whose total sales, receipts or turnover from the business does not exceed INR 50 Lakhs during the financial year immediately preceding the financial year in which such virtual digital asset is transferred.*

## Overriding effect of provision

Where a transaction is subject to TDS under Section 1940 and 194S, tax shall be deducted under Section 194S. Further, a transaction in respect of which tax has been deducted under this provision, no tax shall be deducted or collected under any other provisions.

**The government proposes that with effect from 01 July 2022, tax is to be deducted on payment for transfer of virtual digital asset to a resident at the rate of 1% of consideration.**



## Taxability under section 56(2)(X)

The Government has also proposed an amendment to Section 56(2)(X) of the Income Tax Act, 1961 to bring Virtual Digital Assets under the definition of Property.

In case VDA is transferred to a person without any consideration then section 56(2)(x) shall be triggered and the recipient of such VDA shall now be liable to pay tax on the fair market value in case the fair market value of such asset exceeds INR 50,000/-.

In case VDA is transferred to a person for a consideration and the consideration is less than the fair market value and the difference between consideration and the fair market value is more than INR 50,000/- then such difference will also be taxable in the hand of recipient of such asset. In both the above cases, VDA will be taxable under the head "income from other sources" and the same will not be taxed under section 115BBH. It will be taxable under prevalent tax rates on such individuals.

### Our View

A booming VDA market has prompted the Government to bring in measures to make transactions in such assets transparent and under the tax regime. India is perhaps one of few countries in the world to bring out tax regime for such products. We believe it is a welcome move. This move by the government has clearly indicated that trading in Virtual Digital Asset is not illegal but may never be recognized as legal tender (Apart from those VDAs issued by the government).