International Journal of Enhanced Research in Management & Computer Applications
ISSN: 2319-7471, Vol. 11 Issue 8, August, 2022, Impact Factor: 7.751

Digital Currency and Taxation in India

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ABSTRACT

According to new Global Trends research by Cullen International, most of the surveyed countries do not apply direct taxes on the digital economy, while they all apply value added tax (VAT) on the digital economy. Among the monitored countries, only **India** and **Turkey**, as well as a few individual EU member states, have legislation about digital services taxes (DSTs). **Brazil** published a bill to tax the digital economy that is under debate. Other monitored countries do not apply direct taxes on digital services, either because they are still evaluating imposing DSTs (the **EU**, **Japan**), considering possible studies in the future (**China**), or focusing their work at OECD/G20 level (**Australia**, the **EU**, **Korea**, **South Africa,** the **US**).
The Organisation for Economic Co-operation and Development (OECD) announced in July 2021 that 130 countries agreed on a statement establishing a new framework for international tax reform. However, there is still a long way to go before this might be implemented, which is unlikely before 2023 at the earliest.
Brazil and the **US** only apply VAT on the digital economy at the state or local level. The other monitored countries apply VAT at a national level, including both domestic and cross-border transactions.

Keywords: Crypto, Digital Assets, CBDC (Central Board of Digital Currency), blockchain, cryptocurrencies, virtual currency, peer-to-peer (P2P).

INTRODUCTION

The Bill, titled "The Cryptocurrency and Regulation of Official Digital Currency Bill, according to a Parliament bulletin, "The stated intent of the Bill is to create a facilitative framework for creation of the official digital currency to be issued by the Reserve Bank of India."

The Bill also seeks to prohibit all private cryptocurrencies in India. However, it allows for certain exceptions to promote the underlying technology of cryptocurrency and its uses.2021", will be up for introduction and passing in Parliament.

Is Cryptocurrency legal in India?

Finance Minister Nirmala Sitharaman virtually gave legal sanction to cryptocurrencies in the country by labelling them as "**digital assets**" and not currency and taxing income gains from their transactions at a high rate of 30%.

Nirmala Sitharaman's announcement in the budget presentation largely ends the uncertainty over the future of cryptocurrencies in India. It comes a day after principal **economic advisor Sanjeev Sanyal** said the government would take a balanced view on crypto.

What Nirmala Ji said on cryptocurrency

"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 that any income from transfer of any virtual digital asset shall be taxed at the rate of 30 per cent," **Finance Minister** said.

She also announced that the **Reserve bank of India** (**RBI**) will introduce its digital currency in 2022-23.

How cryptocurrencies will be taxed?

The Finance Minister also said that the 30% tax on virtual assets cannot be mentioned as a replacement of any other income (meaning it cannot be claimed for deduction), in addition to a 1% TDS that will be charged on payments made using digital assets in order to keep a track on transactions.

RBI on cryptocurrency

So far, the central bank pushed for a complete ban on investments in cryptocurrencies as it fears that these can harm the macroeconomic stability in the economy. **The central board of the RBI** had recently discussed various aspects, including the status, of the central bank digital currency. RBI officials informed the board that a pilot project for the introduction of **CBDC** (**central bank digital currency)** will be launched soon.

What is CBDC

CBDCs are the virtual or electronic form of fiat currencies (currencies like Indian rupee of US dollar). A CBDC is the legal tender issued by a **central bank in a digital form.** It is the same as a fiat currency and is exchangeable one-to-one with the fiat currency, only its form is different.

There are several models proposed by technology experts and evangelists on how the Digital Rupee could be transacted, but a formal announcement by the Reserve Bank of India will likely detail how the Digital Rupee will be transacted by citizens. One chief difference will be that Digital Rupee transaction will be instantaneous as opposed to the current digital payment experience.

The crypto Bill

India's booming crypto market was roiled at the end of last year when the central government proposed to introduce a bill in the Winter session of parliament which, among others, sought to prohibit all private cryptocurrencies in the country.

That bill was however, not introduced with government sources suggesting that whenever a bill is brought, it would be referred to the parliamentary standing committee for wider deliberations with stakeholders.

Is crypto really legal now?

According to **Purushottam Anand**, Founder of **blockchain law firm Crypto Legal**, taxing income from cryptocurrencies does not necessarily and explicitly legalise cryptocurrencies beacsuse income tax is not concerned about the manner or means of acquiring the income.

An income earned from both legal or illegal activities can be taxed under Income Tax Act, he added.
"However, looking from a broader context, specific tax provisions for cryptocurrencies are a step towards legalization."

The government has not made crypto legal under the Finance Bill, but it made the gains from it as taxable. "The right way to look at it is that the government has the fight to tax unaccounted money, the same way it has the right to tax gains from crypto be it legal or illegal," said **Harry Parikh**, Associate partner, BDO India.

Further, it is also highly unlikely that the government will collect tax from cryptocurrency transactions and will then introduce a bill to make cryptocurrencies illegal, Anand said.

Crypto
What is cryptocurrency and how it works?
We have seen how **cryptocurrencies** have grown in a couple of years and it was one of the hot topics of the year 2021, we have seen how many people invested in it saying it is the future.

But some of us do not know about cryptocurrencies completely yet, so for them in this post we have discussed **what is cryptocurrency and how it works?** we will discuss all the topics around it.

Now to understand the actual functioning of cryptocurrency we have to understand answers of the following questions.

What is cryptocurrency?
In simple words, cryptocurrency is a **virtual currency** or asset that uses **blockchain** technology and is used as a medium of exchange, it is similar to the online payments we do without using any papermoney.
The first cryptocurrency was **Bitcoin** which was introduced by **Satoshi Nakamoto** in 2009.

A statue in Budapest dedicated to Satoshi Nakamoto

How cryptocurrency works?
To understand how cryptocurrency works we have to understand **blockchain technology** and how it is secured by the **peer-to-peer (P2P) networks.**

What is Blockchain technology?
Cryptocurrency is based on blockchain technology but what is blockchain technology?
Blockchain is a chain of blocks which contains the information, now this technique was first introduced in 1991 and it was originally intended to timestamp (a digital record of the time of occurrence of a particular event) digital documents so that it's not possible to tamper them. But it was not used until it was adapted by Satoshi Nakamoto in 2009 to create the Bitcoin.

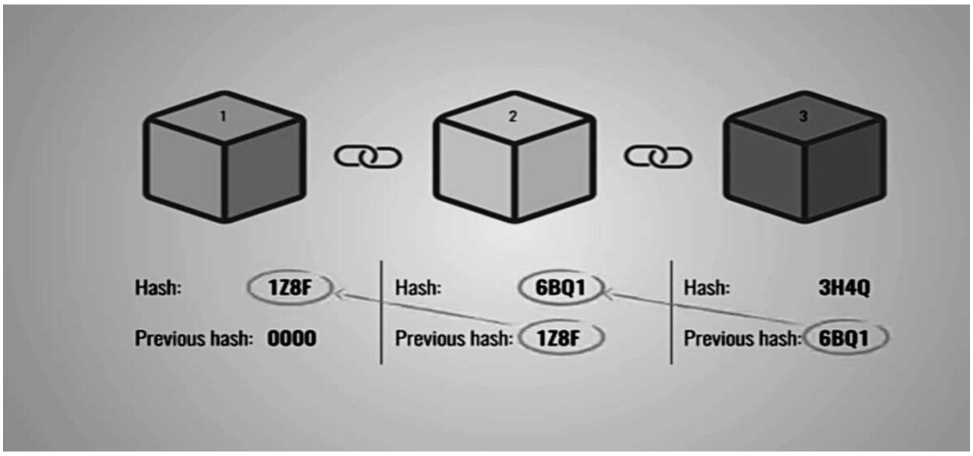
A blockchain is a distributed **ledger** that is completely open to anyone. It was used by Satoshi because of it's property that once any data is stored in these blocks then it becomes very difficult to change it.

The data that is stored inside a block depends on the type of blockchain. Bitcoin blockchain stores the details about a transaction in a block such as the details of sender, receiver and number of coins. A block contains three types of elements 1. Data, 2. hash, 3. hash of previous block. Now we will try to understand about hash.

Hash is a unique code and it is different for every single block just like people having individual fingerprint.
Once a block is created, it's hash is being calculated and after that if you change something inside that block it will cause the hash of that block to change. That's why hashes are very useful when you want to detect changes in blocks. If hash of a block changes it's no longer a same block.

After a block is filled with data then another new block gets linked with it for new data, and like this for every new data a new block is created making a chain of blocks that's why it is known as blockchain technology.

A block also contains hash of previous block and if anyone try to manipulate a block this causes the hash of that block to change as well. In turn that will make the next block and all following block invalid because they no longer store the hash of the previous block.



The first block in every chain is called as **Genesis Block**.
So changing a single block will make all following blocks invalid. But using hash technique is not enough to prevent manipulation of data, computers these days are very first and calculate thousands of hashes in seconds. Anyone can effectively manipulate a block and recalculate the hashes of other blocks to make your blockchain valid again. To prevent this blockchains uses proof-of-work, it's a mechanism that slows down the creation of new blocks.

For example:- In Bitcoins it takes 10 minutes to calculate the required proof-of-work and add a new block to the chain. This makes manipulating a block tough as you will need to recalculate the proof-of-work for all the following blocks.

Now Blockchain uses one more way that makes it nearly impossible to manipulate it.
This mechanism is known as P2P or peer-to-peer network.

What is Peer-to-Peer (P2P) in cryptocurrency?

Peer-to-Peer (P2P) is another way that is used in blockchains to secure it, instead of using a central entity to manage the chain, blockchains use a peer-to-peer network in which everyone is allowed to join. When someone joins this network, he gets the full copy of the blockchain. The Nord (**either a redistribution points or a communication endpoint**) can use this to verify that everything is still in order.

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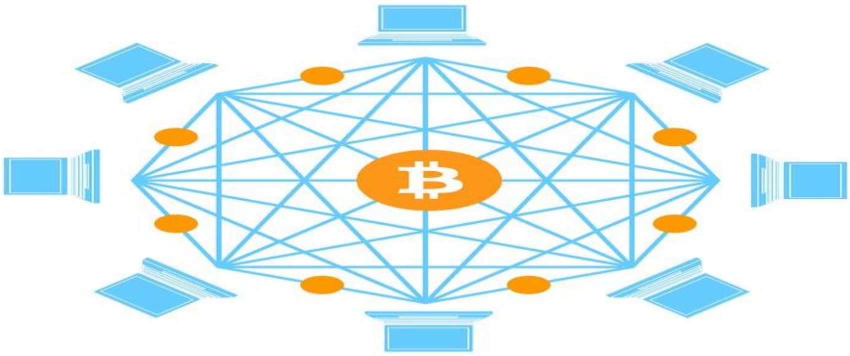

So if someone want to manipulate a blockchain he have to manipulate all the blocks on the chain, redo the proof-of-work for each block and take control of more than 50% of the peer-to-peer network which makes it near to impossible.

Now most of us will think if manipulation of cryptocurrencies is that hard then how are miners earning and for those who have started or going to start their crypto investment journey you should follow these crypto investment rules to gain profit.

What is Crypto Mining?

Crypto mining is one of the key elements which allow cryptocurrencies to work as decentralized P2P network. It is a process in which transaction between users are verified by miners and they add this information to the blockchain public ledger, and they get reward for doing this.

Instead of centralizing the records of transactions just like banks, Satoshi Nakamoto gave it in hands of millions of people through blockchain. The person who has the system can participate in it and after a successful entry he will get some amount of crypto coin as a reward.

How Crypto Mining Works?

So in the process of crypto mining, you don't have to do the calculations, you just have to install your system and leave it, it has an automated algorithm which will run itself, so this is how crypto coins are generated. And the people who run automatic algorithms by installing their systems are called miners.

What is cryptocurrency in simple words?

In simple words, cryptocurrency is a **virtual currency** or asset that uses **blockchain** technology and is used as a medium of exchange.

Which was First Cryptocurrency?
Bitcoin was first cryptocurrency which was introduced in 2009 by Satoshi Nakamoto

Who is founder of Bitcoin?
Satoshi Nakamoto is the founder of bitcoin, he introduced bitcoin in 2009.

When was Blockchain technology was founded?
Blockchain is a chain of blocks which contains the information, now this technique was first introduced in 1991 and it was originally intended to timestamp (a digital record of the time of occurrence of a particular event) digital documents so that it's not possible to tamper them.

CONCLUSION

As cryptocurrency is officially introduced in India through finance bill and government has taken a step to leavy tax on sale and purchase transactions and also TDS was introduced first time in Budget 2022 to deduct tax on Digital currency transaction. It shows that even the Government has not officially permitted to transact in crypto but leavy tax on crypto transactions.

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