

# INTERNATIONAL JOURNAL OF LAW MANAGEMENT & HUMANITIES

[ISSN 2581-5369]

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Volume 7 | Issue 3

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2024

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# Law & Policies Related to Digital Currency; An Analytical Study from an Indian Perspective

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## ABSTRACT

*Cryptocurrency is seen as a digital virtual currency and cryptography which provide strong security to its dealing. Digital currencies include cryptocurrencies and central banks. Digital currencies play a vital role in reshaping the global financial system. The study focuses on examining the legal and policy framework surrounding digital currencies in India. It also highlights the regulatory developments and their socioeconomic implications. The journey of cryptocurrency in India began in 2013 followed by the advisories issued by the Reserve Bank of India. Highlighting the risk associated with cryptocurrency delays and further imposing bans on cryptocurrency. Which was further overturned by the Supreme Court in 2020. This judgement led to the proposal of the new crypto regulation bill in Lok Sabha. The focus was on banning private cryptocurrency and encouraging government-issued cryptocurrency. The central banking digital currency holds the potential for transformation of India's financial landscape. Due to recent developments and a massive increase in online users, there is a rapid growth of information and communication technology which introduced the concept of cryptocurrency in the market, involving transactions such as selling, buying and trading. In recent years, the concept of virtual currency has been in trend and used in a variety of systems. There are very limited countries that have a regulatory framework for dealing with cryptocurrency due to which most of the governments refuse to use it in their economic activities. The article is about the taxation and regulatory framework of the government of India and the future steps to be taken for better regulations. It also highlights the hazards and drawbacks of investing in cryptocurrency. India aims to balance innovation with financial stability in its regulatory framework. The evolving nature of digital currency is important to be monitored by India for harnessing the benefits of digital currency and positioning the country as a significant player in the global digital economy.*

**Keywords:** *cryptocurrency, taxation, challenges and evolution of cryptocurrency.*

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## **I. INTRODUCTION**

Indians are captivated by cryptocurrency, which is a digital or virtual form of currency that presents an innovative framework for conducting financial transactions and investments. In a nation renowned for its technologically proficient populace and rapidly expanding digital economy, cryptocurrencies have materialised as a disruptive entity that contests established financial conventions and frameworks.

Though there are doubts and uncertainty in the regulatory framework of Cryptocurrencies in India, it gained a lot of attention from investors in the market. This attention is caused due to various factors including a sudden increase in investment in the financial market, easy access to the internet, reduced cost of smartphones and the high return earned by the investors in the market. This all leads to the widespread attention of Indian investors in digital assets, Bitcoin or cryptocurrency.

In India cryptocurrency has experienced a combination of regulatory obstacles and ardour. Cryptocurrency is linked with various potential hazards about which The Reserve Bank of India (RBI) had previously cautioned investors. Due to increasing uncertainty in cryptocurrency RBI also imposed a ban on cryptocurrency which was initially removed by the SC in 2020.

Uncertainty in the regulatory framework continues to be an obstacle for the Indian cryptocurrency market. Issues faced by the investors such as investor protection, consumer safety, and the practice of illegal activities, lead to ongoing discussions on cryptocurrency regulations and frameworks by the policymaker.

Despite these obstacles cryptocurrency market has thrived in India and attracted a lot of individuals in the market. As India plots its course in the sphere of digital finance, the country holds a lot of promises for the future.

## **II. EVOLUTION OF CRYPTOCURRENCY IN INDIA**

Cryptocurrency in the Indian market is continuously growing Despite the ambiguity in the regulatory framework. Data from several local cryptocurrency exchanges it is estimated that 17% of Indian investors have invested in the stock market. Over 120 million investors were registered in 2019 and 2023 according to NSE data. As per BSE, in 2024 nearly 161 million investors were registered. A change in the investing paradigm is seen with the rising no of investors in the market, as the investors tend to invest in gold and safer assets more than crypto. The path to cryptocurrency, ahead of the highly anticipated Official Digital Currency Bill is as **In 2008** origin of cryptocurrency in India took place when a paper was published with the title

'Bitcoin: a peer-to-peer electronic cash system' by a pseudonymous developer by the name of Satoshi Nakamoto who was credited with inventing Bitcoin. This was the first time the concept of digital assets was introduced in India.

**In 2010**, the investors became aware of this concept of investing in digital assets which led to the first sale using crypto which secured a monetary value to bitcoin. The first Indian cryptocurrency trading platform was CoinSwitch, after which a surge of Bitcoin started with 2 crore registered users.

**In 2011**: with the rising interest of investors in the market other cryptocurrencies began to emerge which included Litecoin, Namecoin and Swiftcoin

**In 2012-2016**: the steady gain in crypto transactions which was 5\$ in 2012 was almost \$1000 at the end of 2017. With increasing popularity bitcoin is embroiled in controversy over various claims like the dark web, the security of investors frauds etc. due to which RBI issued a circular alerting investors about the securities-related dangers and usage of virtual currency. As also stated virtual currencies are not backed by central banks as their values are a matter of speculation. The boom era of crypto was in 2016 when demonetisation took place and the concept of digital payment online suffering was at its peak which drove the tech-savvy customers to a cryptocurrency exchange.

**In 2017-2018**: RBI repeated these concerns related to cryptocurrency again and with the increasing risk, PILs were filled in SC asking to ban the buying and selling of cryptocurrencies in India. RBI also compared it with the Ponzi scheme which was one of the biggest scams of crypto in India. Some were with the ban some investors were opposing it to the fullest and the hashtag was on trend #indiawantscrypto but a sudden circular which was issued by RBI prevented commercial banks, NBFCs and payment system providers from dealing in currencies or providing any services that led to 99% fall overnight in trading volume, against which several exchange files writ petitions to SC.

**IN 2020**: Supreme Court Strikes Down the Ban on Crypto, one of the reasons given by the Supreme Court is that cryptocurrency is not illegal in India though it is unregulated. After this ruling, the price of bitcoin jumped to 700% recovering all the losses that were incurred during the ban on crypto to the investors therefore crypto exchange surged back to life.

**IN 2021**: the government of India announced that it would introduce a new crypto bill that would give the government the sovereign power to create a digital currency while simultaneously banning all private cryptocurrencies, the recommendation was given by a high-level Inter-Ministerial committee (IMF) as also suggested future actions.

**IN 2022:** The government took a historical step by officially categorising digital assets and proposing section 115BBH in the budget 2022. Before this, there was no regulatory framework to govern the taxation of cryptocurrency as they were not subject to taxation before. This introduced a framework for regulation of tax in income earned by cryptocurrency as any profit arising out of it will be subject to taxes which is 30% (plus 4% cess). Various provisions related to transfer, crypto mining, and profit from blockchain networks and other sources are liable to be taxed under the Income Tax Act 1961.

### III. COMPLEXITY IN TAXATION POLICIES

Cryptocurrency has completely changed the financial landscape With its potential for profitable investments and a decentralised approach to wealth management. On the other hand, a multiple complexity can be seen which is very challenging for the investors in the crypto market. The biggest challenge is the implication of tax for both the investors and the companies are many, some of them are listed below;-

**Complicated Record-Keeping:** it is an obligation on the companies under PMLA 2002 that a comprehensive record is to be kept of every Crypto transaction including dates, amounts, and counterparties involved, to comply with tax compliance regulations. This becomes a challenge Because cryptocurrencies are decentralised and have several platforms and wallets, which makes it difficult to maintain records. **Uncertainty in Tax Regulations:** the history of crypto is not very long in India, for cryptocurrency investors, the most significant obstacle is the lack of clarity in tax laws. India still doesn't have any proper regulatory framework and is still unclear about its stand on cryptocurrency. Since they are a relatively new asset class, rapid evolution can be seen which makes it difficult for tax authorities throughout the globe to come up with a uniform solution.

**Insufficient Tax Reporting Tools:** bitcoin taxes require special programs for data collection and exports of data which can't be done with traditional tax software. the traditional tax software programs force the investor to enter data by Hand, Due to the inability of many tax preparation programs to import data directly from different cryptocurrency exchanges and wallets, investors are forced to enter data by hand, which increases the chances of error and makes it easy for the hackers to commit a crime.

**Global Taxation Complexity:** cryptocurrency has a global market not restricted to national boundaries. With rapid evolution and uncertainty in the market, it's difficult for tax authorities globally to come up with a uniform regulatory framework. Tax evasion, the security of traders, and regulations related to tax are some of the biggest issues. Due to its frequent change in price

velocity and fluctuating nature, it is hard to determine the tax as there is no precise capital gain on which tax is to be charged

**Means of money laundering:** Failure to record all transaction data is prohibited under Section 12 of the PMLA, which requires banks, financial institutions, and intermediaries to keep and maintain records. For illicit operations like money laundering, bitcoins are undoubtedly the best safe refuge due to their accessibility and anonymity. Money laundering is one of the main concerns while dealing with taxation on cryptocurrency. As the biggest crypto fraud in the history of India is due to money laundering. The crime rate of money laundering is highest in dealing with crypto, hence proved as the biggest drawback of taxation in cryptocurrency.

#### **IV. PROVISION RELATED TO TAX IN CRYPTOCURRENCY**

Cryptocurrencies are taxable in India since they are regarded as virtual digital assets. Before 2022 cryptocurrency was not subject to taxation under Indian law after the introduction of the 2022 budget the government imposed a 30% plus 4% cess on profits from trading cryptocurrency. Some of the provisions are listed below under the Income Tax Act 1961. a taxable asset also has a higher standing in a nation like India where murky areas in legislation and regulations wind up becoming pain points for exchanges and associated platforms. That stated, there was a large fall (60-80%) in trading volumes among legitimate Indian exchanges as investors switched to utilizing non-compliant foreign ones for their transactions.

**As to Section 115BBH of the Income Tax Act**, gains derived from trading cryptocurrencies are subject to a 30% tax rate plus a 4% cess. Further, it is clearly stated that any investor who transfers an asset and earns profit out of it is subject to taxation under the IT Act. **Section 194S** mandates that 1% Tax Deducted at Source (TDS) on the transfer of cryptocurrency assets if the transactions total more than ₹50,000 (or even ₹10,000 in some circumstances) within the same fiscal year. This is for both gains whether short-term or long-term gain, the tax rates would be the same.

The government put a 30% tax on crypto income in the 2022 budget and 1% TDS on sales was also established. For a mostly unregulated industry, the tax announcement delivered the first crumb of optimism that some regulation was in the offing. The taxation on cryptocurrency is a matter of union government and can only be imposed by the union, not the state.

In 2023, the government decided to place the crypto industry within the ambit of the Prevention of Anti-money Laundering Act, 2002 (PMLA). As per the Act, crypto companies are under the obligation to record transaction and customer data, monitor compliance, and report any suspicious actions that are found. This surely shows that the government is not aiming to ban

crypto but to provide a regulatory framework for its working. Under PMLA, KYC and additional due diligence are needed for the regulation of crypto. The positive news is that crypto exchanges can engage with the authorities on red-flagging questionable transactions. In this sense, crypto exchanges will also operate as reporting companies.

**Section 194S of the Income Tax Act** charges 1% Tax Deducted at Source (TDS) on the transfer of crypto assets which was also introduced in the 2022 budget, if the transactions reach ₹50,000 (or even ₹10,000 in certain situations) in the same financial year.

Cryptocurrency tax applies to all financiers, whether private or commercial, who are engaged in the transfer of digital assets throughout the year.

Thus, profits from trading, selling, or exchanging cryptocurrencies will be taxed at the same rate regardless of whether the revenue is regarded as capital gains or commercial income.

30% tax on crypto income as per Section 115BBH effective from April 1, 2022

1% TDS on the transfer of VDAs as per Section 194S effective from July 1, 2022

No deduction is permitted, save the cost of purchase.

## **V. CRYPTOCURRENCY FRAUD IN INDIA**

Scams using cryptocurrency are constantly evolving, tricking millions of investors. The scam artists persuade investors with their clever language and convincing demeanour. It often functions well. After defrauding a few investors, they repeat the same operation under a new guise. Crypto scams are similar to other scams in general, except instead of stealing your money, the scammers target your crypto assets. They aim to coerce investors into sending digital assets to the scammer's account or disclosing personal information. P Vasudevan, an executive director of the Reserve Bank of India, said that cryptocurrencies cannot be referred to as "currencies" as they lack intrinsic value at a panel discussion hosted by IIM-Kozhikode. Bitcoins and other new-age currencies have drawn criticism from the RBI, which claims they represent a systemic danger to the financial institutions.

### **(A) India's biggest crypto scams**

#### **The Scam of GainBitcoin Ponzi Scheme**

This scam is recognised as one of the biggest crypto scams, where 1 lakh investors suffered financial loss. In 2018, there was a Ponzi scheme fraud using GainBitcoin. Businessman Amit Bhardwaj conned around 8,000 people out of a total of INR 2,000 crore and overall 40 FIR. Where he introduced the GainBitcion MLM scheme offering mining contracts with a 10%

return on investment for 18 months. He created a multi-level marketing fraud in which he deceived and persuaded investors to convert their Bitcoins for big rewards. These all allegations were made under the Money Laundering Act, 2002 (PMLA)

### **Morris Coin Fraud**

In 2022, the Morris Coin Scam came to light. It was also the most recent scam using cryptocurrency in India. More than nine hundred investors are said to have been duped by a website advertising a phoney cryptocurrency called Morris coin, a total of INR 1,200 cr was stolen by offering staggering returns of up to 3% a day on an investment. The victims were lured into the trap by conducting several promotional events. The fund was raised for the creation of a new coin.

### **The Bitcoin Scandal in Karnataka**

The year 2021 saw the Karnataka Bitcoin controversy occur. In November 2021, the Central Crime Branch, a specialist investigative section of the Karnataka Police, seized 31 Bitcoins worth INR 9 crore from a hacker residing in Bengaluru and a police inspector. The hacker had siphoned off 11 crore by hiking gaming companies and converting that money into bitcoin.

### **STA Coin scam**

STA Token, a firm that raised INR 1,000 cr via fictitious cryptocurrency investments by tricking over 20,000 people. The State Crime Branch exposed this as a nationwide Bitcoin fraud. This was done using the STA (solar techno alliance) token which scammed over 10000 people in India as it was also found that STA was not even authorised by RBI or any other authorised to collect deposits as it was done by all illegal means.

The reason behind these crypto scams is the lack of regulatory framework in India. India is still unclear about the provisions related to cryptocurrency, how they should be taxed, precautions that should be taken, and policies that should be implemented to avoid these scams. The main concern is money laundering which is also mentioned earlier as the complexity which is faced by India.

## **VI. PENALTY FOR TAX EVASION**

In India, the severity of the violation and the amount of tax evaded determine the severity of the penalty. Nevertheless, tax avoidance is prohibited by law, and the Income Tax Act of 1961's Chapter XXII makes this explicit. Several fines have been instituted under the Income Tax Act for those who try to avoid paying income taxes. Such actions carry heavy fines, which may equal 100% to 300% of the tax on unreported income. Fulfilling the tax obligation is essential



to avoid the tax penalty.

**Under section 270A of the Income Tax Act**, there is a maximum seven-year jail term for under-reporting or misreporting income in India, in addition to a fine ranging from 50% to 200% of the tax owed. Interest and late fines are assessed for failing to deduct TDS or to deposit TDS with the government after deduction. Penalties for underreporting and misreporting are significantly different. The penalty for underreporting income on your income tax return is 50% of the amount of tax owed. In the meantime, the penalty for underreporting income on your ITR is 200% of the amount of tax owed. A taxpayer who intentionally tries to avoid paying taxes faces a term of imprisonment ranging from six months to seven years, in addition to a fine if the amount of taxes avoided exceeds Rs25 lakhs.

**Section 139(4)Income Tax Act**, this provision talks about late filing of the income tax return as failing such can result in an interest charge of 1% per month on the due amount of tax which is to be paid and a late fee of up to Rs 1000 to 5000 and also may subject to imprisonment upto 7 years.

**under section 192 to 196D Income Tax Act**, this provision talks about if the assessee is liable to pay TDS and does not pay TDS then he will be liable under this section and would face a penalty under section 271C which can be equal to TDS if he failed to pay under Income Tax Act.

**Under section 271H of the Income Tax Act**, the penalty is imposed by the assessing officer on the person who fails to file the TDS statement within the due date with a minimum penalty of Rs 10000 may extend to Rs 1,00,000.

## VII. CONCLUSION

From the discussion above, it can be concluded that the history of crypto is not very long in India hardly 16 years but the number of ups and downs seen is numerous within a short period, as still more to come with the changing scenarios and regulation which is to be introduced shortly. The most historical years were 2019 when the cryptocurrency prohibition law was introduced and 2020 when SC removed the ban on trading cryptocurrency. The potential that cryptocurrencies carry is great, and the presentation of the Union Budget 2022–2023 on February 1st, 2022, clearly provides a regulatory framework for cryptocurrency tax. The investor's response to this budget regarding 30%tax on gains is still to be observed. RBI also plans to introduce a new digital currency of its own and analysing the impact of such action is crucial. Regarding cryptocurrency, the government doesn't have a proper framework, still, some fields are to be explored and policies to be made as a lot of uncertainty can be seen. The

biggest drawback of cryptocurrency is its stability, it's very unstable and very steady, which makes it harder for the government to make a stable regulatory framework for it.

Globally, the crypto market is increasing day by day many countries are in favour of trading in crypto and some are completely against it, a large number of institutional investors are investing in crypto like US hedge funds and industry heavyweights like Square and PayPal.

As India remains unclear about its stand on crypto, it might adopt a similar regulatory framework from the countries that have passed legislation governing the trade of cryptocurrencies. India may attain its \$5 trillion GDP in this manner. Nonetheless, the Indian government must act to promote the widespread use of cryptocurrencies and provide the necessary financial infrastructure. Analysts forecast increased usage of cryptocurrencies in India in the coming years.

The globe is making progress with blockchain technology, and if India fully legalizes cryptocurrencies, then blockchain advancements there will soon occur. Cryptocurrencies have enormous potential for acceptance and development in emerging countries like India, from both an individual and commercial standpoint. Remittance payments, international commerce, and peer-to-peer financing will all grow significantly as cryptocurrencies reduce transaction costs and time.

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