

# TAXATION OF DIGITAL TRANSACTIONS



## LEARNING OUTCOMES

After studying this chapter, you would be able to -

- ❑ **appreciate** the meaning of e-commerce and how business is transacted through E-commerce;
- ❑ **identify** the issues and problems in taxing e-commerce transactions;
- ❑ **comprehend** the OECD recommendations for taxing e-commerce transactions under Action Plan 1 of Base Erosion and Profit Shifting (BEPS) project;
- ❑ **determine** the income arising on transfer of virtual digital asset and taxability thereof;
- ❑ **examine** the applicability of the provisions of tax deducted at source on transfer of virtual digital asset by a resident assessee.

## CHAPTER OVERVIEW



### E-commerce

- Meaning
- How e-commerce transactions takes place



### Taxation of Virtual Digital Assets



## 12.1 INTRODUCTION

The rapid growth of information and communication technology has resulted in substantial expansion of the supply and procurement of digital goods and services globally, including India. The digital economy is growing at a faster pace than the global economy as a whole.

At present, in the digital domain, business may be conducted without regard to national boundaries and may dissolve the link between an income-producing activity and a specific location. Hence, business in digital domain doesn't actually occur in any physical location but instead takes place in "cyberspace." Persons carrying business in digital domain could be located anywhere in the world. Entrepreneurs across the world have been quick to evolve their business to take advantage of these changes. It has also made it possible for the businesses to conduct themselves in ways that did not exist earlier, and given rise to new business models that rely more on digital and telecommunication network, do not require physical presence, and derives substantial value from data collected and transmitted from such networks.

The growth of e-commerce economy has revolutionised the concept of *brick and mortar* to *click and order*. The need for physical presence in a jurisdiction is consequently getting diminished. Therefore, due to transformed business models, communication with suppliers and customers take place virtually and digitally. Emergence of new age technologies such as 3D printing, sharing economy, internet of things etc. has revolutionised new business models in line with the digital epoch making it difficult to identify the location of source or origin point of a business transaction.

The expansion of business in digital form, give rise to certain tax challenges in relation to nexus, data and characterization of digital transactions. Over the years, to address these tax challenges certain developments are taking place to tax digital transactions which are carried out either by a non-resident non-corporate/ a foreign company or by a resident assessee. This chapter

encompasses these developments introduced in the form of taxation of gains arising on transfer of virtual digital assets by a resident assessee.



## 12.2 WHAT IS E-COMMERCE?

Clause (a) of *Explanation* to Section 194O defines “electronic commerce” to mean the supply of goods or services or both, including digital products over digital or electronic network.

E-commerce or electronic commerce is one of the main components of the Digital Economy. In its widest sense, it encompasses consumer and business transactions conducted over a network, with the help of computers and telecommunications. In other words, e-commerce refers to the exchange of goods or services for value on the internet. E-commerce, *inter-alia*, includes, online shopping, online trading of goods and services, electronic fund transfers, electronic data exchanges and online trading of financial instruments.

<sup>1</sup>OECD defines e-commerce as the sale or purchase of goods or services, conducted over computer networks by methods specifically designed for the purpose of receiving or placing orders. Accordingly, whether a commercial transaction qualifies as e-commerce is determined by the ordering method rather than the characteristics of the product purchased, the parties involved, the mode of payment or the delivery channel. The ordering process is considered as a crucial determinant of an e-commerce transaction in the OECD definition.

E-commerce facilitates trade across borders, increases convenience for consumers, and enables firms to reach new markets. E-commerce reforms have rapidly evolved through the development of new business models, which often integrate new and emerging digital technologies as well as new online payment mechanisms. Many e-commerce business models use online platforms, facilitating purchases between often unknown and dispersed buyers and sellers. Another emerging trend is the growth of subscription e-commerce business models, whereby users access goods and services in a continuous, recurring stream. E-commerce business models integrate digital ordering mechanisms alongside physical infrastructures, including within brick-and-mortar stores.

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<sup>1</sup> OECD (2019), *Unpacking E-commerce: Business Models, Trends and Policies*, OECD Publishing, Paris, <https://doi.org/10.1787/23561431-en>.



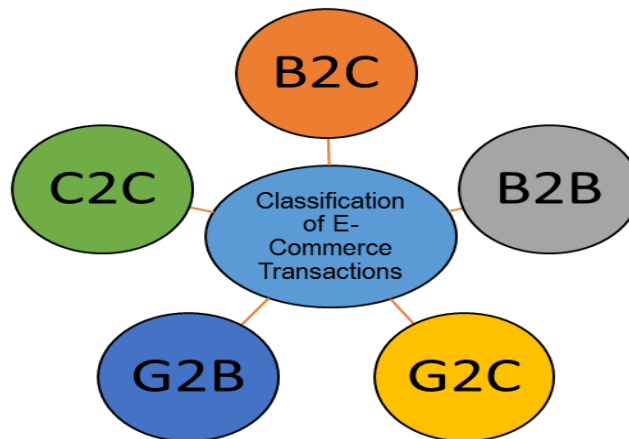
### 12.3 CONDUCT OF BUSINESS IN DIGITAL ECONOMY

E-commerce is a method of conducting business transactions and not a business transaction by itself. Therefore, the contents of a business transaction done through e-commerce means is no different from that of a business transaction carried out through traditional means.

New business models expand the e-commerce frontier in two ways. First, new business models can enable more transactions to move online in a given market or for a given set of participants. Second, new business models can enable whole new markets to emerge for goods and services that previously could not have been bought or sold online, or allow new participants to enter the market.

Digital technologies enable e-commerce innovations and often serve as the backbone of business model developments. Some of these technologies, like smart assistants enabled by artificial intelligence (AI), constitute new channels for selling or purchasing products over electronic networks. Similarly, online payment innovations can help to unlock e-commerce potential by promoting trusted online transactions between unknown parties.

**Classification of E-commerce based on parties involved in transactions.** Major types are mentioned below:



- (i) **Business to Customers (B2C):** In this type of e-commerce, transactions take place between businesses and consumers. In B2C e-commerce, products or services are sold to end-users (i.e. consumers).

**Examples:** Amazon.in, Flipkart.com, Myntra.com, Snapdeal.com etc. are the examples of B2C e-commerce businesses, where consumers can find almost anything be it books, electronic products like washing machines, USB storage devices, clothes, shoes or personal care etc.

- (ii) **Business to Business (B2B):** In B2B e-commerce, transactions take place between two businesses.

**Example:** IndiaMART, TradeIndia, Alibaba, go4WorldBusiness.com (an online B2B marketplace for global exporters and importers), Amazon, the US-based ecommerce giant etc. are the example of B2B online platforms.

- (iii) **Government to Customers (G2C):** The online platform between a government and its citizens or consumers for paying taxes, registering vehicles, and providing information and services such as filing of income-tax return etc.

- (iv) **Government to Business (G2B)/ Business to Government (B2G):** In G2B/ B2G e-commerce, an electronic exchange of any information between businesses and the government, usually using internet so the cooperation or communication takes place on the internet. In G2B, government agencies and business use websites, procurement marketplaces, applications, web services.

**Example:** Government e-Marketplace (GeM), a one stop portal to facilitate online procurement of common use Goods & Services required by various Government Departments/Organizations / PSUs.

INAM-Pro is a web based application, designed by National Highways and Infrastructure Development Corporation Ltd (NHIDCL) and launched by the Ministry as a common platform to bring cement buyers and sellers together.

- (v) **Customer to Customer (C2C):** When goods or services are bought and sold between two consumers, C2C e-commerce business takes place.

**Example:** Olx, a C2C e-commerce online platform where customer sells his used goods to other customer; eBay, an online marketplace in which an individual sells a product or service to another.

### E-Commerce Business Models

With the advancement of digitalization and emergence of new technologies, new forms of e-commerce business models have evolved. Some of such ways of transacting e-commerce business are discussed here below:

#### Online platform e-commerce business model:

In the context of e-commerce, online platforms act as intermediaries between buyers and sellers to facilitate the exchange of goods and services over the Internet. Buyers benefit due to the presence

of variety of products available with diverse sellers. Likewise, sellers discover many buyers to whom they can sell their products. As compared to the physical stores, digital marketplace deliver variety of goods and service.

***Meaning of Marketplace based model and Inventory based model of e-commerce<sup>2</sup>:***

***Marketplace based model*** of e-commerce means providing an information technology platform by an e-commerce entity on a digital & electronic network to act as a facilitator between buyer and seller.

***Inventory based model of e-commerce*** means an e-commerce activity where inventory of goods and services is owned by e-commerce entity and is sold to the consumers directly.

**Subscription e-commerce business model:** Subscription business model is characterised by regular and recurring payments for the repeated provision of a good or a service. The subscription business model can relate to recurring purchases of digital goods and services, or a combination of both digital and tangible products (such as a newspaper subscription that includes access to digital content). Some current e-commerce subscription business models, such as Spotify or Netflix etc.

**Digital identity and its potential for e-commerce:** Digital identity refers to the set of information used by a computer to authenticate an identity. For example, India's Aadhaar programme issues a unique number to every Indian citizen which is a valid means of identification *vis-à-vis* the government as well as private Internet sites including Airbnb, Uber and digital wallet services.

**Subscription access to tangible and bundled goods and services:** A recent e-commerce trend has been the growth of subscription business models for tangible goods, including in categories like beauty supplies (Birchbox), minerals (Celestial Minerals), groceries (Blue Apron, Hello Fresh), snack foods (Nature Box), cosmetics and self-care products (Dollar Shave Club, Harry's), and many more.

**Online-offline e-commerce business models:** These business models serve as extensions of e-commerce, pushing the edges of online purchases into physical stores. Some business models combine online ordering with offline distribution, which may be useful to enable the online purchase of products whose quality may not be assessed from a distance, such as perishable goods like groceries. Many businesses have taken advantage of the ubiquity of digital technologies to grow business models based on a combination of both online and offline features. Other online businesses are moving offline by adding brick-and-mortar elements to enable the online sale of other goods, like clothing, where fit may be difficult to assess from a distance.

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<sup>2</sup> Consolidated FDI Policy Circular of 2017, dated 28.8.2017 read with Press Note dated 26.12.2018

**Mobile technologies - Helping e-commerce to flourish in brick-and-mortar stores:** Mobile technologies empower consumers to perform a range of digital activities, including online shopping. Consumers use digital technologies throughout the commercial process, but smartphones enable buyers to compare prices, to do research and finally make transactions from any networked location.

**Online groceries – e-commerce frontier:** Many businesses are successfully selling perishable food and groceries online. Some online business models offer direct shipping of purchased groceries alongside guarantees related to quality and customer satisfaction to give consumers confidence in the purchase of perishable goods and services.

**Innovative payment mechanisms:** Safely and remotely exchanging money online, including across borders, is fundamental to e-commerce. Safe and effective online payment mechanisms facilitate trusted online transactions, boosting the growth of e-commerce between unknown buyers and sellers. Many online payment mechanisms are closely associated with the rise of e-commerce. In fact, one of the earliest online payment models is “Paypal”, which is emerged in combination with the pioneering online auction house and e-commerce platform eBay, to enable safe online payments between the parties involved.

**Digital wallets:** An online payment can be broadly considered to be a “purchase order placed using devices connected to the Internet”, a definition that is relevant to many forms of e-commerce. One mechanism of enabling online payments includes the use of digital wallets, also known as “e-wallets” or “electronic wallets”.

Digital wallets allow e-commerce by enabling trusted transactions online, without which most e-commerce purchases would not be possible. Consumers may be more willing to do a transaction online using a digital wallet as opposed to directly sharing financial information with online retailers.

**Mobile money - Extending e-commerce to the unbanked:** Another form of payment innovation that enables e-commerce is the rise of a specific form of mobile payment, also known as “mobile money”, particularly for unbanked people (i.e. those without access to financial services). Mobile money differs from digital wallets insofar that the mechanism for payment is conducted via mobile communication networks, and does not necessarily require an existing relationship with a financial services provider.

Mobile money is facilitated by mobile network operators who use a system of agents to accept regular currency in the form of cash and store an equivalent value in a digital wallet, which can then be transferred to other users or can be withdrawn later. Mobile money is connected with a mobile phone number and often uses two-factor authentication through a personal identification number issued at the point of registration. Mobile money can be transferred to others who are also registered

with the same mobile money system, exchanged with merchants for goods and services, or can be withdrawn as cash from a mobile money agent. Mobile money can therefore act as a means of storing and transferring value in a secure and convenient way for unbanked people.

**Resources:** *The discussion on E-commerce Business Models in this chapter is essentially based on the text published in “Unpacking E-commerce: Business Models, Trends and Policies, OECD Publishing, Paris” available at <https://doi.org/10.1787/23561431-en>.*



## 12.4 TAXATION ISSUES RELATING TO DIGITAL ECONOMY

These new business models have created new tax challenges. The typical taxation issues relating to digital economy are:

- (i) the difficulty in characterizing the nature of payment and establishing a nexus or link between taxable transaction, activity and a taxing jurisdiction,
- (ii) the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

The digital business, thus, challenges physical presence-based permanent establishment rules. If permanent establishment principles are to remain effective in the new economy, the fundamental PE components developed for the old economy i.e. place of business, location, and permanency must be reconciled with the new digital reality. Further, characterizing the income as technical services becomes difficult since the technical services rendered digitally does not involve human intervention, as the digital platforms operate on sophisticated artificial intelligence mechanism. Hence the new digital business models gives rise to ‘stateless income’ and thereby going completely tax free.



## 12.5 OECD RECOMMENDATIONS UNDER ACTION PLAN 1 OF THE BEPS PROJECT

Due to the tax challenges arising from digitalization, the G20-OECD BEPS Action Plan Committee as part of its 2015 Action 1 Report identified a number of broader tax challenges raised by digitalisation, notably in relation to nexus, data and characterisation.



The Action Report 1 analysed the following three options, namely -

- (i) a new nexus rule in the form of a “**significant economic presence**” test,
- (ii) **a withholding tax** which could be applied to certain types of digital transactions, and
- (iii) **an equalisation levy**, intended to address a disparity in tax treatment between foreign and domestic businesses where the foreign business had a sufficient economic presence in the jurisdiction

The OECD has recommended several options to tackle the direct tax challenges which include:

- (1) Modifying the existing definition of permanent establishment to provide for whether an enterprise engaged in fully de-materialized digital activities would constitute a PE, if it maintained a significant digital presence in another country's economy.
- (2) Introducing the concept of a virtual fixed place of business in the concept of permanent establishments i.e., creation of a permanent establishments when the enterprise maintains a website on a server of another enterprise located in a jurisdiction and carries on business through that website.
- (3) Imposition of a final withholding tax on gross basis in case of certain payments made for digital goods or services provided by a foreign e-commerce provider or imposition of a equalisation levy on consideration for certain digital transactions received by a non-resident from a resident or from a non-resident having permanent establishment in other contracting state.

It was concluded that countries could introduce any of these options in their domestic laws as additional safeguards against BEPS, provided they respect existing treaty obligations, or in their bilateral tax treaties. The above options can be resorted to as an interim measure until a clear solution emerges on taxing digital economy.

Taking into consideration the potential of new digital economy and the rapidly evolving nature of business operations, it becomes necessary to address the challenges in terms of taxation of such digital transactions. In order to arrive at a long term solution, the OECD along with the BEPS Inclusive Framework is working on arriving at a consensus based solution to tackle the tax challenges arising out of the digital economy as part of a 'Unified Approach' under Pillar One.

Consequent to the BEPS Action Report 1, a committee was constituted by the CBDT to evaluate the alternatives suggested in the BEPS Action Report 1 for addressing the challenges arising on taxing the digital economy. Pursuant to the recommendations of the Committee, Chapter VIII of the Finance Act, 2016, titled "Equalisation Levy" was introduced. It provides for an equalisation levy @6% of the amount of consideration for specified services received or receivable by a non-resident

not having PE in India, from a resident in India who carries out business or profession, or from a non-resident having PE in India.

In order to widen and deepen the equalisation levy net beyond online advertisement, its scope had been extended by the Finance Act, 2020 to consideration received or receivable for e-commerce supply or services made or provided or facilitated on or after 1.4.2020.

However, some stakeholders have raised concerns that the scope of equalisation levy on e-commerce supply or services made or provided or facilitated is ambiguous and as a result it leads to compliance burden. In view of this it is proposed that this equalisation levy shall not be applicable to consideration received or receivable for e-commerce supply or services, on or after the 1st day of August 2024. Further, vide Finance Act, 2025 the equalisation levy on specified services also abolished.



## 12.6 TAXATION OF VIRTUAL DIGITAL ASSETS

There has been a phenomenal increase in transactions in virtual digital assets. Further, a market is emerging where payment for the transfer of a virtual digital asset can be made through another such asset. Accordingly, for the taxation of virtual digital assets, a scheme has been introduced by the Finance Act, 2022.

### **Meaning of virtual digital asset [Section 2(47A)]**

It means -

- (a) any information or code or number or token (not being Indian currency or foreign currency),
  - generated through cryptographic means or otherwise, by whatever name called,
  - providing a digital representation of value exchanged with or without consideration,
  - with the promise or representation of having inherent value, or
  - functions as a store of value or a unit of account including its use in any financial transaction or investment, but not limited to investment scheme; and
  - can be transferred, stored or traded electronically;
- (b) a non-fungible token or any other token of similar nature, by whatever name called;

The non-fungible token means such digital asset as may be notified by the Central Government.

Accordingly, the Central Government has, vide notification no. 75/2022 dated 30.6.2022, specified a token which qualifies to be a virtual digital asset as non-fungible token. However, it shall not include a non-fungible token whose transfer results in transfer of ownership of underlying tangible asset and the transfer of ownership of such underlying tangible asset is legally enforceable.

- (c) any other digital asset, as may be notified by the Central Government.
- (d) ***any crypto-asset being a digital representation of value that relies on a cryptographically secured distributed ledger or a similar technology to validate and secure transactions, whether or not such asset is included in point (a) or (b) or (c) above.***

However, the Central Government may, by notification, exclude any digital asset from the definition of virtual digital asset subject to specified conditions.

Accordingly, the Central Government has, vide notification no. 74/2022 dated 30.6.2022, notified that the following virtual digital assets would be excluded from the definition of virtual digital asset–

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

#### **Taxability of income from transfer of virtual digital assets [Section 115BBH]**

- (1) **Tax rate on transfer of virtual digital asset** – Where the total income of an assessee includes any income from the transfer of any virtual digital asset, such income would be taxed @30% under section 115BBH.
- (2) **No deduction allowed** – In computing the income from transfer of virtual digital asset, no deduction would be allowed under any provisions of the Act in respect of any expenditure or allowance except cost of acquisition, if any. Further, no set off of any loss is allowed to the assessee from such income.
- (3) **Set off or carry forward of loss from transfer of virtual digital asset not allowed** – Loss from transfer of virtual digital asset would **not** be allowed to be set off against income computed under any provision of this Act to the assessee and such loss would not be allowed to be carried forward to succeeding assessment years.
- (4) **Virtual digital asset need not to be a capital asset** - The definition of “transfer” under section 2(47) would apply to any virtual digital asset, whether it is a capital asset or not.

### Taxability of receipt of virtual digital asset as gift or for inadequate consideration

#### [Section 56(2)(x)]

In order to tax gift of virtual digital asset in the hands of the recipient, section 56 has been amended to include virtual digital asset within the definition of “property”.

Accordingly, if virtual digital asset is received by any person from any person

- (i) **Without consideration:** The aggregate fair market value of such virtual digital asset on the date of receipt would be taxed as the income of the recipient, if it exceeds ₹ 50,000.
- (ii) **For inadequate consideration:** If the difference between the aggregate fair market value and such consideration exceeds ₹ 50,000, such difference would be taxed as the income of the recipient.

However, the exclusions from the applicability of section 56(2)(x) will apply to gift virtual digital asset also. For example, if virtual digital asset is received as a gift by an individual from his relative, the value of the same would not be treated as income.

#### TDS on payment on transfer of virtual digital asset [Section 194S]

- (1) **Applicability and rate of TDS** – Section 194S requires any person who is responsible for paying to any resident any sum by way of consideration for transfer of a virtual digital asset to deduct tax @1% of such sum.
- (2) **Time of deduction** – The deduction is to be made at the time of credit of consideration to the account of the resident or at the time of payment of such sum by any mode, whichever is earlier.

Where consideration is credited to any account in the books of account of the person liable to pay such sum, such credit of the sum is deemed to be the credit of such sum to the account of the payee and tax has to be deducted at source. The account to which such sum is credited may be called “Suspense Account” or by any other name.

- (3) **Cases where the consideration for transfer of virtual digital asset is wholly in kind or partly in kind and partly in cash** – In a case where the consideration for transfer of virtual digital asset is

- wholly in kind or in exchange of another virtual digital asset, where there is no part in cash; or
- partly in cash and partly in kind but the part in cash is not sufficient to meet the liability of deduction of tax in respect of whole of such transfer,

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

- (4) **Non applicability of TDS under section 194S** – No tax is required to be deducted under section 194S, where the consideration is payable by the person referred to in column (2) of the table below and aggregate value of such consideration during the financial year does not exceed the threshold limit in the corresponding row of column (3) of the table below:

| (1)  | Consideration is payable by<br>(2)                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | Threshold limit<br>(3) |
|------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------|
| (i)  | Specified person, being an individual or a Hindu undivided family <ul style="list-style-type: none"> <li>- whose total sales, gross receipts or turnover from his business or profession does not exceed ₹ 1 crore in case of business or ₹ 50 lakhs in case of profession, during the financial year immediately preceding the financial year in which such virtual digital asset is transferred; or</li> <li>- not having any income under the head “Profits and gains of business or profession”.</li> </ul> | ≤ ₹ 50,000             |
| (ii) | Other than specified person mentioned in (i) above                                                                                                                                                                                                                                                                                                                                                                                                                                                              | ≤ ₹ 10,000             |

- (5) **Due date of remittance to Government Account [Rule 30] and Furnishing statement and certificate of TDS u/s 194S [Rules 31A and 31]**

| Sl. No. | (1)<br>Particulars                                          | (2)<br>Specified Person                               | (3)<br>Exchange                                                                                                                                          | (4)<br>Any other person |
|---------|-------------------------------------------------------------|-------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------|
| (i)     | <b>Rule 30</b> – Time of payment to Government Account      | 30 days from the end of the month of deduction        | In case of tax deducted in March, on or before 30 <sup>th</sup> April.<br>In any other case, on or before 7 days from the end of the month of deduction. |                         |
| (ii)    | <b>Rule 31A</b> – Furnishing of Statement of TDS u/s 200(3) |                                                       |                                                                                                                                                          |                         |
|         | <b>Form</b>                                                 | Form 26QE                                             | Form 26QF                                                                                                                                                | Form 26Q                |
|         | <b>Time</b>                                                 | Within 30 days from the end of the month of deduction | Common for Exchange and any other person                                                                                                                 |                         |
|         |                                                             |                                                       | <b>Qtr ending</b>                                                                                                                                        | <b>Due date</b>         |
|         |                                                             |                                                       | 30 <sup>th</sup> June                                                                                                                                    | 31 <sup>st</sup> July   |
|         |                                                             |                                                       | 30 <sup>th</sup> Sep                                                                                                                                     | 31 <sup>st</sup> Oct    |
|         |                                                             |                                                       | 31 <sup>st</sup> Dec                                                                                                                                     | 31 <sup>st</sup> Jan    |
|         |                                                             |                                                       | 31 <sup>st</sup> March                                                                                                                                   | 31 <sup>st</sup> May    |

|       |                                  |                                                                                                     |                                                                                                              |
|-------|----------------------------------|-----------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|
| (iii) | <b>Rule 31 – TDS Certificate</b> | Form 16E to be furnished within 15 days from the due date of furnishing TDS statement in Form 26QE. | Form 16A to be furnished within 15 days from the due date of furnishing TDS statement in Form 26QF/Form 26Q. |
|-------|----------------------------------|-----------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|

**ILLUSTRATION 1**

Compute the net income-tax payable by Mr. Abhinav, aged 32 years, who has the following income for the A.Y.2026-27:

- (i) Interest on fixed deposits with SBI (Gross) ₹ 1,10,000
- (ii) Interest on savings bank account with SBI ₹ 35,000
- (iii) Consideration for transfer of VDA ₹ 4,62,000
- (iv) Cost of acquisition ₹ 21,000
- (v) Expenses on transfer of VDA ₹ 1,000

Mr. Abhinav has exercised option to shift out of section 115BAC.

**SOLUTION**

Total income (excluding Income from transfer of VDA) is below the basic exemption limit of ₹ 2,50,000. Therefore, tax on income, other than income from VDA, is Nil. Income of ₹ 4,41,000 (₹ 4,62,000 – ₹ 21,000) from transfer of VDA would be taxable@30% (plus cess of 4%). The tax on income from transfer of VDA would be ₹ 1,37,592, being 31.2% of ₹ 4,41,000. The expenses on transfer of VDA is not allowable as deduction.

Section 194S provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of 1% of consideration. Hence, the transferee would have deducted tax of ₹ 4,620, being 1% of ₹ 4,62,000.

Tax@10% under section 194A would have been deducted by SBI from ₹ 1,10,000. TDS u/s 194A = ₹ 11,000

Net tax payable by Mr. Abhinav would be ₹ 1,21,972 [₹ 1,37,592 – ₹ 11,000 (TDS u/s 194A) – ₹ 4,620 (TDS u/s 194S)].

**ILLUSTRATION 2**

Compute the net income-tax payable by Mr. Siddhanth, aged 24 years, who has the following income for the A.Y.2026-27

|       |                                                 |            |
|-------|-------------------------------------------------|------------|
| (i)   | Income from Salaries (computed)                 | ₹ 8,40,000 |
| (ii)  | Interest on savings bank account with Axis Bank | ₹ 12,000   |
| (iii) | Consideration on transfer of VDA to Mr. Harsh   | ₹ 50,000   |
| (iv)  | Cost of acquisition of VDA transferred          | ₹ 5,000    |

Mr. Harsh is employed with ABC Ltd. on a monthly salary of ₹ 50,000. In addition, he has interest on savings bank account with Bank of India.

Mr. Siddhanth has not exercised option to shift out of section 115BAC. Ignore TDS on income other than VDA.

**SOLUTION****Tax payable by Mr. Siddhanth for A.Y. 2026-27**

| Particulars                                                                                                                                                                                                                                                                                                         | Amount in ₹     |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| Total income (excluding income from transfer of VDA) [₹ 8,40,000 + ₹ 12,000]                                                                                                                                                                                                                                        | 8,52,000        |
| Income from VDA (₹ 50,000 – ₹ 5,000)                                                                                                                                                                                                                                                                                | 45,000          |
| <b>Total Income</b>                                                                                                                                                                                                                                                                                                 | <b>8,97,000</b> |
| Tax on income other than VDA                                                                                                                                                                                                                                                                                        |                 |
| Upto ₹ 4,00,000                                                                                                                                                                                                                                                                                                     | Nil             |
| ₹ 4,00,001 to ₹ 8,00,000 @5%                                                                                                                                                                                                                                                                                        | ₹ 20,000        |
| ₹ 8,00,001 to ₹ 8,52,000 @10%                                                                                                                                                                                                                                                                                       | ₹ 5,200         |
| Tax on income from VDA @30%                                                                                                                                                                                                                                                                                         | 13,500          |
|                                                                                                                                                                                                                                                                                                                     | 38,700          |
| Less: Rebate u/s 87A                                                                                                                                                                                                                                                                                                | 25,200          |
|                                                                                                                                                                                                                                                                                                                     | 13,500          |
| Add: Health and education cess @ 4%                                                                                                                                                                                                                                                                                 | 540             |
|                                                                                                                                                                                                                                                                                                                     | 14,040          |
| Less: TDS under section 194S [Mr. Harsh is a specified person since he does not have income under the head "Profits and gains of business and profession" and the consideration payable by him does not exceed ₹ 50,000. Accordingly, Mr. Harsh need not deduct tax u/s 194S on consideration payable to Siddhanth] | Nil             |
| <b>Net tax payable</b>                                                                                                                                                                                                                                                                                              | <b>14,040</b>   |

**ILLUSTRATION 3**

Compute the net income-tax payable by Mr. Raj, aged 32 years, who has the following income for the A.Y.2026-27

|       |                                           |              |
|-------|-------------------------------------------|--------------|
| (i)   | Business loss                             | (₹ 3,18,000) |
| (ii)  | Interest on fixed deposits with HDFC Bank | ₹ 18,000     |
| (iii) | Consideration on transfer of VDA          | ₹ 6,20,000   |
| (iv)  | Cost of acquisition of VDA transferred    | ₹ 20,000     |

**SOLUTION**

As per section 71, business loss of the current year can be set off against income from other sources of that year. Therefore, business loss of ₹ 3,18,000 can be set off against interest of ₹ 18,000 from fixed deposits.

As per section 115BBH, business loss cannot be set off against income from transfer of VDA. Therefore, balance business loss of ₹ 3,00,000 cannot be set off against Income from VDA of ₹ 6,00,000 (₹ 6,20,000 – ₹ 20,000). The same has to be carried forward to A.Y.2027-28 for set-off against business income of that year.

Tax on Income from VDA would be ₹ 1,87,200 (i.e., 31.2% of ₹ 6 lakh).

Section 194S provides for deduction of tax on payment on transfer of virtual digital asset to a resident at the rate of 1% of consideration. Hence, the transferee would have deducted tax of ₹ 6,200, being 1% of ₹ 6,20,000.

Net tax payable by Mr. Raj = ₹ 1,87,200 – ₹ 6,200 = ₹ 1,81,000.

- (6) **Non-applicability of section 203A** - The provisions of section 203A containing the requirement of obtaining TAN would not be applicable in case of specified person referred in 4(1).
- (7) **Cross application of section 194-O and section 194S** - In case of a transaction where tax is deductible under section 194-O along with the section 194S, then, the tax shall be deducted under section 194S and not section 194-O.
- (8) **Power of the CBDT to issue guidelines** – In case any difficulty arises in giving effect to the provisions of this section, the CBDT is empowered to issue guidelines, with the prior approval of the Central Government, for the purposes of removing the difficulty.



Every guideline issued by the CBDT shall be laid before each House of Parliament and shall be binding on the income-tax authorities and on the person responsible for paying the consideration on transfer of such virtual digital asset.

Accordingly, the CBDT has, with the prior approval of the Central Government, vide Circular no. 13/2022 dated 22.6.2022, issued the following guidelines. These guidelines would apply only in cases where transfer of virtual digital asset is taking place on or through an Exchange. In other cases (like peer to peer and others) provisions of section 194S would apply.

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

**Answer:** According to section 194S, any person who is responsible for paying to any resident any sum by way of consideration for transfer of virtual digital asset is required to deduct tax.

Thus, in a peer to peer (i.e., direct buyer to seller) transaction, the buyer (i.e., person paying the consideration) is required to deduct tax under section 194S. The tax so deducted is required to be deposited with Government in accordance with the time and procedure prescribed in the Act read with the relevant provisions of the Income-tax Rules, 1962.

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

It may be clarified that the TDS shall be on consideration for transfer of virtual digital asset less GST. **[Clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions not conducted on or through Exchange]**

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

- (i) **In a case where the transfer of virtual digital asset takes place on or through an Exchange and the virtual digital asset being transferred is owned by a person other than the Exchange:** In this case, buyer would be crediting or making payment to the Exchange (directly or through a broker). The Exchange, then, would

be required to credit or make payment to the owner of virtual digital asset being transferred, either directly or through a broker. Since there are multiple players, to remove difficulty it has been clarified that:

1. Tax may be deducted under section 194S only by the Exchange which is crediting or making payment to the seller (owner of the virtual digital asset being transferred). In a case where broker owns the virtual digital asset, it is the broker who is the seller. Hence, the amount of consideration being credited or paid to the broker by the Exchange is also subject to tax deduction under section 194S.
2. In a case where the credit/ payment between Exchange and the seller is through a broker (and the broker is not seller), the responsibility to deduct tax under section 194S shall be on both the Exchange and the broker. However, if there is a written agreement between the Exchange and the broker that broker shall be deducting tax on such credit/ payment, then broker alone may deduct the tax under section 194S. The Exchange would be required to furnish a quarterly statement (in Form 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962.

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

To remove this difficulty, it has been clarified that while the primary responsibility to deduct tax under section 194S, in this case, remains with the buyer or his broker, as an alternative the Exchange may enter into a written agreement with the buyer or his broker that in regard to all such transactions, the Exchange would be paying the tax on or before the due date for that quarter. The Exchange would be required to furnish a quarterly statement (in Form 26QF) for all such transactions of the quarter on or before the due date prescribed in the Income-tax Rules, 1962. The Exchange would also be required to furnish its income tax return and all these transactions must be included in such return. If these conditions are complied with, the buyer or his broker would not be held as assessee in default under section 201 for these transactions.

**Meaning of certain terms:**

- (i) The term “Exchange” means any person that operates an application or platform for transferring of virtual digital assets, which matches buy and sell trades and executes the same on its application or platform.
- (ii) The term “Broker” means any person that operates an application or platform for transferring of virtual digital assets and holds brokerage account/accounts with an Exchange for execution of such trades.

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

**Answer:** In the above situation, the buyer will release the consideration in kind after seller provides proof of payment of such tax (e.g., Challan details etc.). In a situation where virtual digital asset “A” is being exchanged with another virtual digital asset “B”, both the persons are buyer as well as seller. One is buyer for “A” and seller for “B” and another is buyer for “B” and seller for “A”. Thus, both need to pay tax with respect to transfer of virtual digital asset and show the evidence to other so that virtual digital assets can then be exchanged. This would then be required to be reported in TDS statement along with challan number. Form 26Q has included provisions for reporting such transactions. For specified persons, Form 26QE has been introduced. **[Also clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions not conducted on or through Exchange]**

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

If such an alternative mechanism is exercised,

- (i) the Exchange would be required to deduct tax for both legs of the transactions and pay to the Government. In the Form 26Q it will need to report it as tax deducted on both legs of the transaction.
- (ii) the buyer and seller would not be independently required to follow the procedure prescribed under proviso to section 194S(1) i.e., to ensure that the tax required to be deducted has been paid by the other person, before releasing the consideration.

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

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

**Question 3: Whether the provision of section 194Q is also applicable on transfer of virtual digital asset?**

**Answer:** Without going into the merit whether virtual digital asset is goods or not, it is clarified that once tax is deducted under section 194S, tax would not be required to be deducted under section 194Q. **[Also clarified by the CBDT vide circular no. 14/2022 dated 28.6.2022 for all other transactions also not conducted on or through Exchange]**

**Question 4: Whether the consideration for transfer of virtual digital asset shall be on Gross basis after including GST/commission or it shall be on “net basis” after exclusion of these items.**

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

**Question 5: In transactions where payment is being carried out through payment gateways, there may be tax deduction twice. To illustrate that a person “XYZ” is required to make payment to the seller for transfer of virtual digital asset. He makes payment of ₹ 1,00,000 through digital platform of “ABC”. On these facts liability to deduct tax under section 194S may fall on both “XYZ” and “ABC”. Is tax required to be deducted by both?**

**Answer:** In order to remove this difficulty, it is provided that in the above example, the payment gateway will not be required to deduct tax under section 194S on a transaction, if the tax has been deducted by the person (“XYZ”) required to make deduction under section 194S. Hence, in the above example, if “XYZ” has deducted tax under section 194S on ₹ 1,00,000, “ABC” will not be required to deduct tax under section 194S on the same transaction. To facilitate proper implementation, “ABC” may take an undertaking from “XYZ” regarding deduction of tax.

## TEST YOUR KNOWLEDGE

### Questions

1. *Explain the core reasons for difference between the e-commerce transactions and the traditional business transactions causing difficulty to tax the income of e-commerce transactions.*
2. *E-commerce transactions have replaced concepts generally associated with international transactions traditionally. Discuss briefly the taxation issues involving such transactions.*
3. From the following details compute the taxable income of Mr. Mohan for the sale and purchase of Bitcoins and NFT made during the year:

| Date            | Particulars                          | Units | Amount (₹) |
|-----------------|--------------------------------------|-------|------------|
| June 15, 2025   | Purchase (Bitcoin)                   | 5000  | 50,000     |
| July 15, 2025   | Sale (Bitcoin)                       | 2500  | 25,500     |
| July 20, 2025   | Sale (Bitcoin)                       | 2500  | 28,750     |
|                 | Expenses Incurred on Sale of Bitcoin |       | 15,000     |
| August 1, 2025  | Purchase (NFT)                       | 10000 | 1,50,000   |
| August 16, 2025 | Sale (NFT)                           | 6000  | 89,000     |
| August 31, 2025 | Sale (NFT)                           | 4000  | 56,000     |
|                 | Expenses Incurred on Sale of NFT     |       | 18,000     |

### Answers

1. The core reasons for difference between e-commerce transactions and traditional business transactions causing difficulty to tax the income from e-commerce transactions under the Income-tax Act, 1961 are absence of national boundaries, no requirement of physical presence of goods and no requirement of physical delivery (in certain cases). Since e-commerce transactions are completed in cyberspace, it is often not clear as to the place where the transaction is effected, thereby causing difficulty in implementing source rule taxation.

2. The typical taxation issues relating to e-commerce are:

- (1) the difficulty in characterizing the nature of payment and establishing a nexus or link between taxable transaction, activity and a taxing jurisdiction,
- (2) the difficulty of locating the transaction, activity and identifying the taxpayer for income tax purposes.

3. **Computation of Taxable Income of Mr. Mohan**

|                                                                                       | ₹            |
|---------------------------------------------------------------------------------------|--------------|
| <b>Sale of 2500 Bitcoin 15.07.2025</b>                                                |              |
| Sale Consideration                                                                    | 25,500       |
| Less: Cost of Acquisition (2500 x 50000/5000)                                         | 25,000       |
| <b>Gain</b>                                                                           | <b>500</b>   |
| <b>Sale of 2500 Bitcoin 20.07.2025</b>                                                |              |
| Sale Consideration                                                                    | 28,750       |
| Less: Cost of Acquisition (2500 x 50000/5000)                                         | 25,000       |
| <b>Gain</b>                                                                           | <b>3,750</b> |
| <b>Sale of 6000 NFT 16.08.2025</b>                                                    |              |
| Sale Consideration                                                                    | 89,000       |
| Less: Cost of Acquisition (6000 x 150000/10000)                                       | 90,000       |
| <b>Loss on Sale of NFT [Neither setoff of loss nor carry forward of loss allowed]</b> | <b>1,000</b> |
| <b>Sale of 4000 NFT 31.08.2025</b>                                                    |              |
| Sale Consideration                                                                    | 56,000       |
| Less: Cost of Acquisition (4000 x 150000/10000)                                       | 60,000       |
| <b>Loss on Sale of NFT [Neither setoff of loss nor carry forward of loss allowed]</b> | <b>4,000</b> |
| <b>Taxable income</b>                                                                 | <b>4250</b>  |

**Note:** VDA income would be taxed @30% under section 115BBH without any deduction of expenses.