

## NEWS FLASH

### Withholding tax under Section 194S

24 June 2022

The Finance Act, 2022 has inserted Section 194S in the Income-tax Act, 1961 ('the Act') which casts a tax withholding obligation at the rate of 1% with effect from 1 July 2022, on any person paying to a resident any sum by way of consideration for transfer of a Virtual Digital Asset<sup>1</sup> ('VDA'). Tax withholding is applicable if the consideration payable by a specified person<sup>2</sup> as defined, exceeds INR 50,000 per Financial Year ('FY'); in any other case, tax is required to be withheld if the consideration exceeds INR 10,000 per FY. Tax is required to be withheld even in case of a barter transaction for VDA.

The extent and nuances of this provision have been intensely debated. The Central Board of Direct Taxes ('CBDT') has issued Circular No. 13 of 2022 dated 22 June 2022 ('the Circular') providing guidelines for the removal of difficulties relating to the application of the Section when the transfer of a VDA takes place on or through the 'Exchange'<sup>3</sup>. In a case where a VDA is transferred directly (i.e. not via Exchange) between the buyer and the seller, the provisions of Section 194S shall apply to the buyer.

The Team at JMP Advisors is pleased to summarise below the key clarifications provided in the Circular.

➤ **Case 1: Where the consideration for transfer of VDA through Exchange is not in kind**

- A VDA can be transferred via an Exchange wherein the consideration may flow from the buyer to an Exchange (directly or through a Broker) and then from the Exchange to seller (directly or through a Broker).

Sr.No.	Particulars	Person responsible to withhold Tax		
		Broker	Buyer	Exchange
<b>I.</b>	<b>VDA is owned by any person (including Broker) other than Exchange</b>			
1	Owner of VDA is the seller and credit/payment is made to such seller			✓
2	Owner of VDA is a Broker (seller) and credit/payment is made to the Broker (seller)			✓
3	Owner of VDA is the seller and credit/payment to the seller is through a Broker:			
	- If there is a written agreement between Broker and Exchange that Broker shall withhold tax on such credit/payment	✓		
	- Where no such agreement exists	✓		✓

<sup>1</sup> VDA has been defined in the section 2(47A) of the Act to mean inter-alia any information or code or number or token generated through cryptographic means or otherwise, by whatever name called, a non-fungible tokens, and any other digital asset as may be notified by the Central Government.

<sup>2</sup> Specified person has been defined in section 194S to mean:

- Individual/Hindu Undivided Family ('HUF') whose total sales or turnover or gross receipts do not exceed INR 10 million in case of business or INR 5 million in case of profession during the immediately preceding FY;
- Individual/HUF not having any income from business or profession

<sup>3</sup> The term 'Exchange' has been defined in the Circular as any person that operates an application or platform for transferring of VDAs, which matches buy and sell trade and executes the same on its application or platform.

Sr.No.	Particulars	Person responsible to withhold Tax		
		Broker	Buyer	Exchange
II	<b>VDA is owned by Exchange</b>			
	Where credit/payment is made by the buyer or his Broker:			
	- If there is a written agreement between Exchange and buyer or his Broker			✓
	- Where no such agreement exist	✓	✓	

➤ **Case 2: Where the consideration for transfer of a VDA is in kind or in Exchange for another VDA**

- The Section provides that where a VDA is transferred for consideration in kind or for another VDA, the person responsible for paying such consideration is required to ensure that tax has been paid, before releasing such consideration.
  - To Illustrate, where VDA 'A' is being exchanged with VDA 'B', one person is a buyer for 'A' and a seller for 'B' and the other person is a buyer for 'B' and a seller for 'A'. Therefore, both need to withhold tax from the consideration payable for the transfer of VDAs.
  - If such transaction is carried out through an Exchange, it is clarified that tax may be withheld by the Exchange based on a written contractual agreement with buyers/sellers.
  - In the aforementioned cases, where the transfer of a VDA is in kind or for another VDA, tax is required to be withheld in kind. The Circular provides for detailed guidelines for conversion and payment of such tax withheld in kind.
  - It is further clarified that tax will not be required to be withheld at the time of converting the tax withheld in kind (in the form of VDA) into INR.
- Where tax is withheld under Section 194S of the Act, provisions of Section 194Q of the Act would not apply.
- Tax is required to be withheld on the net consideration excluding GST/ other charges levied by the deductor for rendering service.
- The payment gateway will not be required to withhold tax under Section 194S.
- VDAs transferred on or before 30 June 2022, would not be subjected to withholding tax under Section 194S. However, while computing the aggregate value of the consideration for VDAs transferred during FY 2022-23, value of the consideration paid/credited from 1 April 2022 to 30 June 2022 is to be included.

**JMP Insights:** This Circular provides welcome clarifications on several aspects relating to persons responsible for withholding tax under various situations and casts the onus of compliances on Exchanges. It appears that the withholding compliances are also required to be carried out by Exchanges located outside India.

Should you wish to discuss any of the above issues in detail or understand the applicability to your specific situation, please feel free to reach out to us at [coe@jmpadvisors.in](mailto:coe@jmpadvisors.in).

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