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Virtual currencies: A hazard or a boon? A Perspective from the Digital finance ecosystem and associated Legal issues

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Abstract
Digital India is a flagship program of the Government of India with a vision to transform India into a digitally empowered society and knowledge economy. "Faceless, Paperless, Cashless" is one of professed role of Digital India. As part of promoting cashless transactions and converting India into less-cash society, various modes of digital payments have been put out.
Financial market regulators and central banks around the world regularly warn consumers about the risks related to virtual currencies. The Institute for Development & Research in Banking Technology (IDRBT), the research arm of RBI had published a report in which it stated that the time had come to adopt the blockchain technology in India, in the bid to evolve towards a cashless society.
As regards non-fiat crypto currencies, the RBI is not comfortable; the intrinsic value of the VC seems to be a matter of speculation, moreover the legal status is definitely missing, finally, the usage of VCs for illicit and illegal activities in the dark net has been reported to be hitting the roof across the world. The present paper takes into perspective the rapidly evolving Technology of the Digital Virtual Currency landscape from the Indian standpoint and the related Legal Conundrum.

Keywords: digital India, digital payments, virtual currency, dark net, bitcoin, legal issues

Introduction
Virtual currency (also known as digital currency or cryptocurrency) is an electronic currency that acts as an alternative currency that is neither government-funded nor backed by national currency. Virtual currencies allow one to make transactions with really well and services, and does not limit to just the online world. Additionally, its novelty has caused a soar in the value of these currencies, specifically Bitcoins.
Virtual currencies are digital currency or electronic money. They do not physically exist as coins or notes. Many digital currencies (also called crypto currencies) started in online gaming communities or on social media.
Although they can be used as a form of payment if another person is willing to accept them, they are not legal tender. The value of virtual currency can fluctuate significantly, they may not be accepted in many places and they are not guaranteed by any bank or government.
Despite the Reserve Bank of India's repeated calls for caution against the use of virtual currencies', a domestic Bitcoin exchange reported in September 2nd week of 2017 that it was adding over 2,500 users a day and had reached five lakh downloads. The company, launched in 2015, said the increasing downloads highlighted the "growing acceptance of Bitcoins as one of the most popular emerging asset class."
So, what is a Bitcoin? Bitcoin is a cryptocurrency and digital payment system; it is in fact the first decentralized digital currency. It was thrown up on the dark net by an unknown programmer using the pseudo name - Satoshi Nakamoto in 2009 as an open-source software. The system works peer to peer & transactions take place among users directly without intermediary or brokers. Bitcoin transactions are not controlled by any regulatory authority. The transaction can take place from one smart phone to other by verifying digital signature of input owner.
Virtual currencies can be earned or purchased.
They are issued and managed according to unique and complex open source code algorithms. The algorithms are defined by individuals called "miners" using powerful and sophisticated computers. In exchange for their services, miners are awarded virtual currency units that can be exchanged. Someone who wishes to obtain virtual currency units without participating in these "mining" activities must purchase them.

A cryptocurrency has two keys
- The first one, called the "public key," confirms the existence and unique identifier of the virtual currency unit.
- The second one, called the "private key," is the equivalent of a secret code which the owner stores in a digital wallet.

Once the digital wallet is set up using software or platforms intended for this type of trading, users can buy goods or services, and trade or transfer virtual currency. These types of transactions are done pseudo-anonymously due to the keys used.
When making a payment, owners of a virtual currency unit validate their currency unit with the private key. The transaction is then submitted to a network of miners who confirm the owner of the virtual currency unit, validating the transaction and the transfer to the new owner.

Unit of Bitcoins

Symbol used to represent bitcoin is BTC. XBT and (U+20BF). Small units are called millibitco in which is represented as mBTC, microbitcoin is represented as µBTC and satoshi. Named in homage to bitcoin's creator, a satoshi is the smallest amount within bitcoin representing 0.00000001 bitcoin, one hundred millionth of a bitcoin. A millibitcoin equals to 0.001 bitcoin, one thousandth of a bitcoin. One microbitcoin equals to 0.000001 bitcoin, one millionth of a bitcoin.

Initial phase

One of the first supporters, adopters, contributor to bitcoin and receiver of the first bitcoin transaction was programmer Hal Finney. Finney downloaded the bitcoin software the day it was released, and received 10 bitcoins from Nakamoto in the world's first bitcoin transaction.

Bitcoin digital transactions are logged in a ledger called blockchain, instead of having a central administrator such as bank or government, blockchain systematizes data in batches called blocks. These data batches use cryptographic validation to link themselves together. In other words, each block identifies and references the previous block by a hash value forming an unbroken chain.

Blockchain solves two most challenging problems of digital transactions controlling the information and avoiding duplication. Computers all over the world then compete to confirm the operation by solving complex mathematical equations. The first to figure out the answer and validate the block receives a reward in bitcoins this process is called mining.

According to a research by Cambridge University there were between 2.9 million and 5.8 million unique users using a crypto currency wallet, as of 2017, most of them using bitcoin. The number of users has grown significantly since 2013, when there were300,000 to 1.3 million users as per latest figures.

In 2016, the number of merchants accepting bitcoin exceeded 100,000. Instead of the 2–3% on transaction value typically imposed by credit card processors, merchants accepting bitcoins often pay fees in the range from 0% to less than 2%. Firms that accepted payments in bitcoin as of December 2016 included PayPal, Microsoft, Dell *et al.*

There are no bitcoins, only records of bitcoin transactions

Here's the funny thing about bitcoins: they don't exist anywhere, even on a hard drive. We talk about someone having bitcoins, but when you look at a particular bitcoin address, there are no digital bitcoins held in it, in the same way that you might hold pounds or dollars in a bank account. You cannot point to a physical object, or even a digital file, and say "this is a bitcoin".

Instead, there are only records of transactions between different addresses, with balances that increase and decrease. Every transaction that ever took place is stored in a vast public ledger called the block chain. If you want to work out the balance of any bitcoin address, the information isn't held at that address; you must reconstruct it by looking at the blockchain.

What does a transaction look like?

If Alice sends some bitcoins to Bob, that transaction will have three pieces of information:

- An input. This is a record of which bitcoin address was used to send the bitcoins to Alice in the first place (she received them from her friend, Eve).
- An amount. This is the amount of bitcoins that Alice is sending to Bob.
- An output. This is Bob's bitcoin address.

How is it sent?

To send bitcoins, you need two things: a bitcoin address and a private key. A bitcoin address is generated randomly, and is simply a sequence of letters and numbers. The private key is another sequence of letters and numbers, but unlike your bitcoin address, this is kept secret.

Think of your bitcoin address as a safe deposit box with a glass front. Everyone knows what is in it, but only the private key can unlock it to take things out or put things in.

When Alice wants to send bitcoins to Bob, she uses her private key to sign a message with the input (the source transaction(s) of the coins), amount, and output (Bob's address).

She then sends them from her bitcoin wallet out to the wider bitcoin network. From there, bitcoin miners verify the transaction, putting it into a transaction block and eventually solving it.

Current uses of bitcoins in India

People are buying bitcoins from digital currency exchanges by the credit card Coinbase.com and Coindesk.com are the most popular exchanges. They also offer tutorials on digital currencies.

In India purchase of bitcoin from Zebpay exchange, Zebpay has android and apple ios apps which links the bank account for quick transfer, there is a KYC requirement to do so.

Unocoin another exchange in India allows people to trade in bitcoins the company claims it has 1,50,000 customers in India. Post demonetization, leading Bitcoin exchanges in India witnessed a rise in user base by up-to 250 %.

Value of Bitcoins

The decentralized virtual currency that took the world by storm has witnessed a 300 % rise in value in just one year. Its value hit an all-time high when Japan passed a law to accept bitcoin as a legal payment method.

Despite RBI's reluctance to recognize the cryptocurrency, the interest in Bitcoins in India has not waned. After Prime Minister Narendra Modi's demonetization move, Ahmedabad-based bitcoin trading start-up Zebpay witnessed a 25 per cent surge in revenue.

Can Bitcoins be considered as Securities?

The term "securities" is defined in section 2 (h) of the Securities Contracts (Regulation) Act, 1955 in the following manner: "securities" include — (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company

or other body corporate; (ia) derivative; (ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes; (ic) security receipt as defined in clause (zg) of section 2 of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002; (id) units or any other such instrument issued to the investors under any mutual fund scheme; (ii) Government securities; (iia) such other instruments as may be declared by the Central Government to be securities; and (iii) rights or interest in securities;" It is clear from a bare reading of this definition that Bitcoin does not come within any of the parts of the definition of securities

The following risks are related to the use of virtual currency

Volatility risk

The value of a virtual currency is determined by the public's interest in it and is based strictly on supply and demand. Media coverage of a virtual currency can have a major impact on its value over a short period of time without any official organization or mechanism controlling the volatility. For example, at the end of August 2017, Bitcoin was worth US$4,748, but decreased at US$3,320 on September 13, 2017 (source: blockchain.info).

Liquidity risk

It can be difficult to trade a virtual currency for money that is legal tender. The trading channels such as platforms are not overseen by official regulators or central banks. The bid-ask spread is often very wide due to speculative trading in virtual currencies.

Technological and operational risk

Virtual currency may be exposed to hacking and theft.

The security of digital wallets and virtual currency trading and transaction platforms is not guaranteed. Users may be exposed to theft and total loss of assets.

Legal risk

Virtual currencies are not regulated. There is also no legal framework to protect consumers who buy goods or services using virtual currency.

INTERPOL Global Complex for Innovation (IGCI) is the agency's first digital crime center and research and development capabilities the Interpol's new international anti-cybercrime center located in Singapore to boost cyber security and countering cybercrimes created its own cryptocurrency.

The Internal Revenue Service (IRS) in USA issued guidance to taxpayers in 2015 on how to treat Bitcoin and other virtual currency for federal income tax purposes. This notification indicated that bitcoin and other 'convertible' virtual currencies are to be treated as a capital asset, for tax payers, this means that bitcoin and other similar virtual currency will be subject to capital gains rules for any applicable gains and losses.

Can Bitcoins be considered as a Derivatives or a Negotiable Instruments?

The definition of "derivative" under the SCRA is (ac) "derivative" includes— (A) a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security; (B) a contract which derives its value from the prices, or index of prices, of underlying securities;

Bitcoin is not a security and therefore would not satisfy the first part of the definition of "derivative" within the SCRA. Further since Bitcoin is only a voluntary currency based on two parties deciding that the code itself has some value, therefore Bitcoin can also not be described as a contract which derives its value from the prices or index of prices of underlying securities. Therefore, it is clear that Bitcoin would not satisfy the requirements of being a derivative under the SCRA.

Under Indian law, another definition of the term derivative is provided under the Reserve Bank of India Act, 1934 which defines "derivative" in section 17(6A) to mean: an instrument, to be settled at a future date, whose value is derived from change in one or a combination of more than one of the following underlying, namely:-(a) interest rate, (b) price of securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government, (c) price of foreign securities, (d) foreign exchange rate, (e) index of rates or prices, (f) credit rating or credit index, (g) price of gold or silver coins, or gold or silver bullion, or (h) any other variable of similar nature.

Since Bitcoins are used as currency because Bitcoin users think it has inherent and not because its value is derived from any other underlying thing or object, therefore Bitcoin cannot be said to fall under the definition of "derivative" under the Reserve Bank of India Act, 1934 either. The term negotiable instrument on the other hand is defined in the Negotiable Instruments Act, 1881 and defines a negotiable instrument as a "promissory note, bill of exchange or cheque payable either to order or to bearer". Since the terms promissory note, bill of exchange or cheque are easily understood in trading parlance, there is no need to go into the definitions of these instruments as provided under the Negotiable Instruments Act, 1881, suffice it to say that Bitcoins do not fall under the definitions of any of these terms under the Act.

Can Bitcoin be classified as a Prepaid Payment Instrument?

The enactment of the Payment and Settlement Systems Act, 2007 has brought the payment systems involved in the issuance of prepaid payment instruments under the regulatory jurisdiction of the RBI. In exercise of its powers under Section 18 of the Payment and Settlement Systems Act, 2007 the RBI on April 27, 2009 issued policy guidelines governing institutions issuing prepaid payment instruments such as mobile wallets, PayPal, etc. In these guidelines the term Prepaid Payment Instrument is defined in the following words: Pre-paid payment instruments are payment instruments that facilitate purchase of goods and services against the value stored on such instruments. The value stored on such instruments represents the value paid for by the holders by cash, by debit to a bank account, or by credit card…

Since Prepaid Payment Instruments have a definite value stored on them which is equal to the amount paid by the holders in cash or by debit or credit card, it seems that Bitcoins cannot be classified as Prepaid Payment Instruments

since there is no static value stored in Bitcoins, rather they have an inherent value

Bitcoins cannot be classified as regular financial instruments such as 'currency', 'security', 'derivative' or 'negotiable instruments' as these instruments are currently defined under Indian law. Bitcoins are essentially lines of code which create the system of transfer of Bitcoin currency from one account to another. The Indian Copyright Act defines the term "computer programme" as "a set of instructions expressed in words, codes, schemes or in any other form, including a machine readable medium, capable of causing a computer to perform a particular task or achieve a particular result". Based on this definition as well as the generally understood meaning of computer programme it would be fairly safe to say that Bitcoins would fall under the definition of the term "computer programme".

Now the General Clauses Act, 1897 defines the term movable property as property of every description, except immovable property. Immovable property has been defined to include land, benefits arising out of land or things attached to the earth or permanently fastened to anything attached to the earth. Clearly a computer programme would not fit into the definition of immovable property and relying upon the broad definition of movable property in the General Clauses Act, 1897 it can be said that a computer programme and by logical extension Bitcoins should be considered as movable property. Further the Forward Contracts (Regulation) Act, 1952 also defines goods to mean "every kind of movable property other than actionable claims, money and securities". It would seem that on a bare reading, Bitcoins would also fulfil this condition and be generally defined as goods under Indian law.

Now that we have determined that Bitcoins would in all likelihood be treated as goods or movable property under the current legal regime in India, it would be beneficial to discuss what laws would regulate the various Bitcoin transactions that occur in general practice, for the purposes of this paper we shall limit our discussion to the following transactions: i) Mining of Bitcoins; ii) Transfer of Bitcoins from one person to another within the territory of India; iii) Exchange of Bitcoins for Indian Rupees, provided the entire transaction is based in India; iv) Transfer of Bitcoins from one person to another where the person sending the Bitcoins is not resident in India; v) Exchange of Bitcoins for Indian Rupees, where the exchange is based outside India.

Although Bitcoins can currently be classified only as movable property and more specifically as computer software, this position is not tested in a Court of law. Further it appears from the analysis of the definitions of 'currency' and 'prepaid payment instrument' that the government has the power to bring Bitcoins into the definition of either currency or prepaid payment instrument by just amending the regulations, which is not a very cumbersome process since financial regulations, by their very nature, are quite fluid and prone to changes. Even so it is worth noting that even as the legal regime stands now offering of derivative products in Bitcoins might require registration and approval under the Forward Contracts Regulation Act.

Risk

Money Laundering & Dubious Crimes

India concerned over the adverse impact of virtual currencies such as bitcoin had setup a commission to examine and decide framework & to regularize the fast-growing segment to halt money laundering. This comes from the amid move that black money hoarders may have restored to virtual currencies and bitcoins to launder their cash, during the demonetization drive in November2016. The bitcoins have banned in some countries, counting Russia, since it could be used for money laundering or financing terrorism.

The Finance Minister has said that the circulation of virtual currencies which are also popular as digital and crypto currencies has been a cause of concern, RBI issued a notification in 2013, to caution users, holders, traders of virtual currencies such as bitcoins, about the potential financial, operational, legal, customer protection and security risks.

A number of reports have pointed out about a surge in domestic bitcoin trade and moving of black economy to the Dark Internet. The surveillance and policing requirements are challenging and the government and RBI are ill-equipped, currently, to deal with this. The finance ministry has constituted an inter-disciplinary committee chaired by special secretary (economic affairs) and representatives from DEA, department of financial services, department of revenue (CBDT), home ministry, ministry of electronics and information technology, RBI, NITI Aayog and State Bank of India.

Also, developments on crypto currencies are in the headlines, they are becoming the latest rage in country and the increase in prices allegedly give a return on investment that no investment can match, the bitcoin is also being used for dubious purposes such as arms, and narco/ drugs trafficking in India.

As awareness and adoption of bitcoin grow in India, there are concerns among authorities about the potential for abuse by tax evaders and money launderers.

Income tax authorities and the Enforcement Directorate, an economic law enforcement and intelligence agency, are specially looking into significant investments into buying the crypto currency. A 'Special Investigation Team' (SIT) on black (laundered) money – specially appointed by the Supreme Court of India – is reportedly drawing up a draft report of what it has learned and is even suggesting 'curbs' in trading.

"There are concerns on the way it operates…Some unaccounted money could be owing into these," an unnamed social was cited as saying.

As reported by CCN in July, India's Supreme Court demanded the government and the Reserve Bank of India (the country's central bank to check bitcoin transactions so as to ensure they aren't used for money laundering or terrorism funding.

Legal Framework

At present, bitcoin is almost valued around Rs. 3,88,000/-,

India is not exactly a laggard as far as bitcoins are considered; India bitcoins exchanges have come up and a few restaurants across the country accept the coins as payment.

Apart from Singapore bringing its own cryptocurrencies in circulation, to curb the use of cryptocurrency and bitcoin, Japan has recognized it as a legal currency (since the inventor of bitcoins 'Satushi Nakamoto' has a Japanese connection) after applying anti-money laundering rules and capital requirements to the cryptocurrency. Japan also developed accounting standards for reporting bitcoin transactions.

China authorities have recently ordered to cease operation of Beijing based cryptocurrency exchanges to stop trading and immediately notify users of their closure.

Saurabh Agrawal, CEO of Zebpay has said that he appreciates the concern. However, he was sure that the Indian government being progressive would ensure right growth through positive regulations on digital currencies and will support the growth of the technology.

Bitcoin Is Legal & Regulated In USA

Financial Crimes Enforcement Network (FinCEN), United States Department of the Treasury has classified bitcoin as a convertible decentralized virtual currency in 2013.

Global Advisors Bitcoin Investment Fund (GABI) is the first regulated bitcoin hedge fund to receive regulatory approval from the Jersey Financial Services Commission (JFSC).

New York State Department of Financial Services (NYSDFS) started issuing Bit License to businesses related to virtual currency activities.

Coin base launched the first regulated bitcoin exchange in the U.S.

Winklevoss brothers' bitcoin exchange, Gemini, had been granted a license by the New York State Department of Financial Services.

European Union

European Union's top court, European Court of Justice, ruled that exchanging bitcoin should be exempt from value-added tax in the same way as traditional money.

Bit stamp to be the first fully licensed bitcoin exchange in Europe, w.e.f. July 1, 2016. It has been granted the license by Luxembourg Financial Industry Supervisory Commission (CSSF).

Japan

Japan has officially recognized bitcoin and digital currencies as money w.e.f April 1, 2017. Japan has a new law that will make bitcoins usable as legal tender.

Singapore

Inland Revenue Authority of Singapore (IRAS) has issued tax guidelines for Bitcoins stating that businesses that choose to accept virtual currencies such as Bitcoins for their remuneration or revenue are subject to normal income tax rules.

Switzerland

Zug becomes the first town in which you can pay city fees (taxes) in bitcoin.

Swiss National Railway SBB sells bitcoins at all its offices.

South Korea

The South Korean Central Bank fails to see Bitcoins or other cryptocurrencies as currency but recognises it as a commodity. South Korea is the world's third-largest market for cryptocurrency trading. Speaking at National Assembly of South korea, Noh Jae-hyun, Governor at the Bank of Korea said that the bank does not see cryptocurrency trading as money but merely a commodity, according to a Korean daily, Yonhap News.

While a formal statement from the bank is yet to be released, Noh said, "It is difficult to look at the example of the International Settlement Banks (BIS) in terms of money. However, its regulation is appropriate because it is regarded as a commodity."

In the past five years, despite Bitcoin Cash and Bitcoin Gold hard-fork, Bitcoin trading at $7.5 in 2012 has registered an unprecedented growth of more than 76,000%. However, the love and hate relationship with the authorities across the world continues. Strangely, while most of the economists and governments across the world agree to the fact that blockchain is the most transparent, trustable and distributed ledger, they proclaim Bitcoins which is based on the very same technology as a private entity. And thus the founder of Bitcoins and blockchain, Satoshi Nakamoto is yet to be given his due credit.

Regulation of Virtual Currency

Taxation of transactions where consideration is paid in Bitcoins

While the general acceptability of bitcoins in India is pretty low, it is not unusual to and savvy businesses accepting bitcoins as consideration for the sale of goods and services. The typical transactions, in this case, would be as follows:

A is a Delhi-based dealer in antiquities, he sells a vintage table to R, a Russian businessperson who thinks the table would complete the look of his new London apartment. R ores to pay A in bitcoins, which A gladly accepts. As consideration for the shipment, R pays A 10 bitcoins. How would "A" be taxed on this income in India?

Similarly, say B is a web developer who has provided his services from India. His client S, based in San Francisco pays him a retainer, on a monthly basis in bitcoins. How would "B" be taxed on this income in India?

From an Indian tax perspective, this transaction is like a barter. A traded one commodity for another by accepting bitcoins in exchange for his table. And B trader a service in exchange for bitcoins. In both cases, the sellers / services providers accepted bitcoins instead of cash in a barter transaction.

In so far as the tax code in India is concerned income, profits and gains are taxable even if they are received in money's worth instead or real money or currency. Therefore, the value of bitcoins received would also be considered income in India in the hands of the recipient and the profits on such income subject to tax at the rates applicable to both A and B.

Therefore, A's profit on the transaction would be equal to the INR value of bitcoins received less the cost of the table and similarly, B's profits would be equal to the value of bitcoins received less any deductible expenses incurred while rendering the services.

Conversion of Bitcoin and taxation thereon

Given the limited adoption of bitcoin, it is obvious that the need will arise where the holders of such bitcoins will have to convert them into rupees to be able to spend them on the open market. At such point of time, the deference in the value of the bitcoin when it was rest received and when it was converted shall be taxable in the hands of the holder. To illustrate this using an example, if A the furniture exporter was to convert his 10 bitcoins into Rupees he would receive as on date today (1.5.2016) a sum of roughly around Rs 2,90,000 at a conversion rate of 29,762 Rupees per bitcoin. The taxable value of bitcoin held by him would be calculated as per the following

Value of Bitcoin when received as consideration20,000 (assumed)

Value of Bitcoin when converted 29,762

Taxable Value in hands of holder 9,762

Total tax liability (X10) 97,672

Hence, at the time of conversion, a sum of 97,672 will be taxable as capital gains in the hands of the holder of such bitcoins

USA

Recently, the Internal Revenue Service (IRS) clarified the tax treatment of Bitcoin and Bitcoin transactions.

Bitcoin is the most widely circulated digital currency or e-currency as of 2017. It's called a convertible virtual currency because it has an equivalent value in real currency. The sale or exchange of a convertible virtual currency — including its use to pay for goods or services — has tax implications. The IRS answered some common questions about the tax treatment of Bitcoin transactions in its recent Notice 2014-21. Tax treatment depends on how Bitcoins are held and used.

Bitcoin used to pay for goods and services taxed as income If you are an employer paying with Bitcoin, you must report employee earnings to the IRS on W-2 forms Bitcoin used to pay for goods and services taxed as income If you are an employer paying with Bitcoin, you must report employee earnings to the IRS on W-2 forms.

You must convert the Bitcoin value to U.S. dollars as of the date each payment is made and keep careful records. Wages paid in virtual currency are subject to withholding to the same extent as dollar wages.

Employees must report their total W-2 wages in dollars, even if earned as Bitcoin. Self-employed individuals with Bitcoin gains or losses from sales transactions also must convert the virtual currency to dollars as of the day earned, and report the figures on their tax returns.

Bitcoins held as capital assets are taxed as property If you hold Bitcoins as a capital asset, you must treat them as property for tax purposes. General tax principles applicable to property transactions apply.

If the Bitcoins are held as a capital asset, like stocks or bonds, any gain or loss from the sale or exchange of the asset is taxed as a capital gain or. Otherwise, the investor realizes ordinary gain or loss on an exchange.

Bitcoin miners must report receipt of the virtual currency as income some people "mine" Bitcoins by using computer resources to validate Bitcoin transactions and maintain the public Bitcoin transaction ledger.

According to the IRS, when a taxpayer successfully "mines" Bitcoins and has earnings from that activity whether in the form of Bitcoins or any other form, he or she must include it in his gross income after determining the fair market dollar value of the virtual currency as of the day he received it. If a bitcoin miner is self-employed, his or her gross earnings minus allowable tax deductions are also subject to the self-employment tax.

Global Countries where bitcoin is legal

Aland Islands, Australia, Austria, Belgium, Brazil, Brunei Darussalam, Bulgaria, Canada, Chile, Congo, Croatia, Cuba, Cyprus, Czech republic, Denmark, Estonia, Finland, France, Georgia, Greece, Germany, Hongkong, Hungary, Iceland, Iran, Ireland, Isle of Man, Israel, Italy, Japan, Jersey, Kenya, Kuwait, Latvia, Lebanon, Liberland, Lithuania, Luxembourg, Malta, Monaco, Mongolia, Netherlands, New Zealand, Nicaragua, Norway, Pakistan, Philippines, Poland, Portugal, Reunion, Romania, San Marino, Serbia, Singapore, Slovakia, Slovenia, South Africa, South Korea, Spain, Sweden, Switzerland, Taiwan, Thailand, Turkey, Ukraine, United Arab Emirates, United Kingdom, USA, Uzbekistan & Zimbabwe.

Global countries where bitcoins are illegal

Afghanistan, Bangladesh, Ecuador, Bolivia & Republic of Macedonia.

Risk of participating in criminal, terrorist or fraudulent activities or money laundering

Virtual currencies have been associated with fraud, money laundering and criminal or terrorist activities

Benefits of Virtual Currency

Transactions in virtual currencies can be cheaper, faster, more secure and more transparent, the blockchain technology can be regarded as a kind of regulatory technology, which enables laws to be enforced more transparently and more efficiently, which in turn solves the problem of who watches the watcher.

User secrecy

Bitcoin purchases are discrete. Unless a user voluntarily publishes his Bitcoin transactions, his purchases are never associated with his personal identity, much like cash-only purchases, and cannot be traced back to him. In fact, the anonymous Bitcoin address that is generated for user purchases changes with each transaction.

End to Third-party Interruptions

One of the most widely publicized benefits of Bitcoin is that governments, banks and other financial intermediaries have no way to interrupt user transactions or place freezes on Bitcoin accounts. The system is purely peer-to-peer; users experience a greater degree of freedom than with national currencies.

No Tax on Purchase

Since there is no way for third parties to identify, track or intercept transactions that are denominated in Bitcoins, one of the major advantages of Bitcoin is that sales taxes are not added onto any purchases.

Extremely Low Transaction Fees

Standard wire transfers and foreign purchases typically involve fees and exchange costs. Since Bitcoin transactions have no intermediary institutions or government involvement, the costs of transacting are kept very low. This can be a major advantage for travelers. Additionally, any transfer in Bitcoins happens very quickly, eliminating the inconvenience of typical authorization requirements and wait periods.

Mobile Payments

Like with many online payment systems, Bitcoin users can pay for their coins anywhere they have Internet access. This means that purchasers never have to travel to a bank or a store to buy a product. However, unlike online payments made with U.S. bank accounts or credit cards, personal information is not necessary to complete any transaction.

Conclusion

The government has the sovereign right to bring virtual currencies like Bitcoins into the classification of either currency or prepaid payment instrument by just modifying the regulations, which is not a very burdensome process since financial regulations, by their very nature, are quite fluid and prone to changes. Even so it is worth observing that even as the legal regime stands now offering of derivative products in Bitcoins might require registration and approval under the Forward Contracts Regulation Act.

It is worth perceiving that unlike other digital currencies such as e-gold, liberty reserve, etc. Bitcoin is a peer to peer network based currency which does not have one centralized agency and therefore a quarrel is made that even if the government wants to regulate or shut it down they will not physically be able to do so as there is no nodal institution that the authorities can go after.

However, this quarrel is fallacious to a certain extent in that the authorities can go after online exchanges which are websites or portals run by individuals or entities which have a physical manifestation. They would have names, addresses, bank accounts, etc. and the authorities could easily go after the major exchanges to cut off the supply or cash into the Bitcoin system by attacking the source where cash or 'real currency' enters or leaves the system thereby severely reducing the efficacy of Bitcoins.

Looking at the relatively insignificant number of people who use PayPal or other e-wallets in India, it would not be entirely unlikely that the regulations to govern Bitcoin, whenever they come, would be a reaction to a particular event and whether these regulations are enabling or disabling in nature would probably depend upon the nature of the event to which they are reacting.

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