



Gaming revolution

Unraveling the regulatory
transformation in the
online gaming industry

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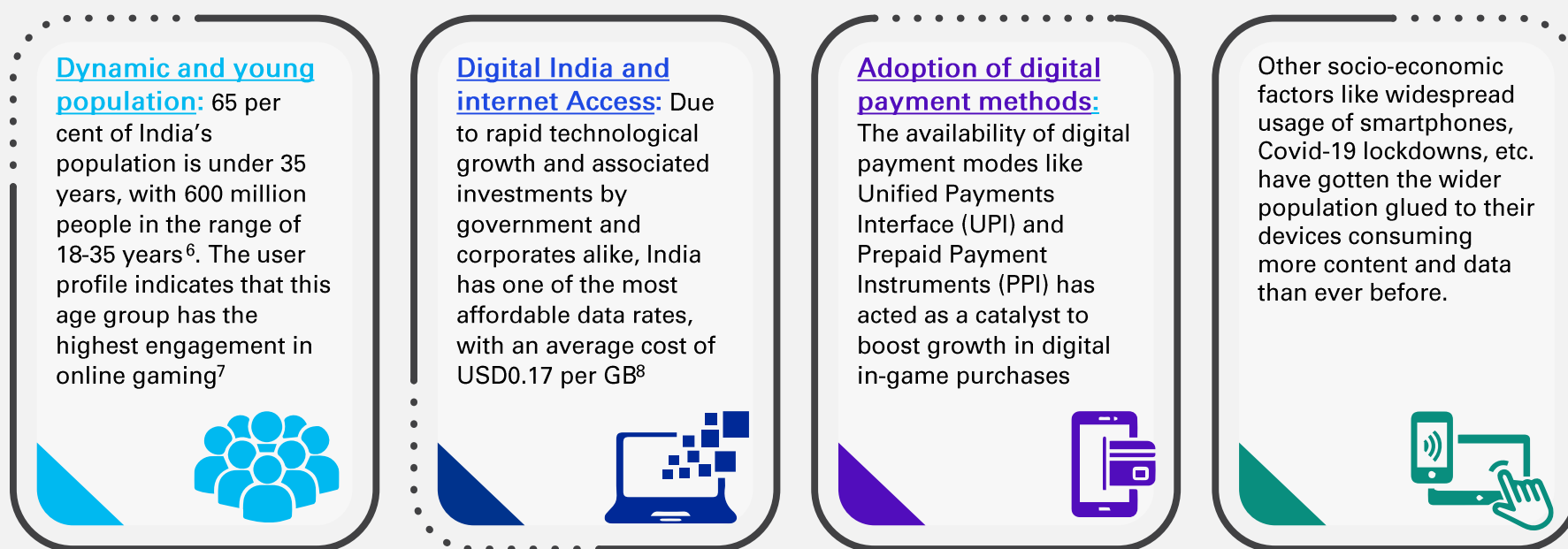
The origin of India's online gaming industry can be dated back to the 2000s, when console and computer gaming brought several Indians on digital gaming platforms¹. The online gaming market in India has seen tremendous growth since, with three gaming companies achieving unicorn status by 2022². Various forms of online games available for users include card games, eSports, battle royale, fantasy sports and casual gaming.

The Government of India recently stated the country's vision to be a trillion-dollar digital economy by 2026³ and the online gaming industry, given its reach to the wider population and tremendous growth in the last few years, has the potential of becoming a key player in driving this vision.

The Indian gaming market is witnessing an unprecedented growth, fueled by various social, economic and technological factors. These factors when combined with appropriate controls could be key levers in driving the next phase of growth in the online gaming industry.

Based on a report released in 2022,⁴ it can be noted that the online gaming industry in India, valued at USD2.6 billion in 2022, is expected to grow at CAGR of 27 per cent and is estimated to be worth USD8.6 billion by 2027. Nearly 57 per cent of the revenue is constituted by real money games (RMG), which is growing at a rate of 25 per cent year-on-year (YOY). India was the largest consumer⁵ of mobile games in the world, with mobile game downloads at 15 billion in FY 2022, growing at CAGR of 35 per cent.

Some of the key drivers to the growth of internet gaming sector are as captured below:



Government of India's Ministry of Electronics and Information Technology (MeitY) has recently issued amendments⁹ in the Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Rules, 2021 towards bringing more clarity in the online gaming industry from a regulatory perspective. The new regulations have the potential to not only promote responsible growth of the industry but can also help in ensuring the protection of consumers' interests and bringing in more transparency in operations. Given the context and anticipated growth in this industry, captured in this document are our key thoughts on the amendments in the online gaming regulations and their impact on stakeholders.

1. Evolution of Gaming in India, Silicon India.
2. India's gaming sector is spawning unicorns. But the future is uncertain, Forbes India, September
3. We plan to make India \$1 trillion digital economy by 2026: Minister Rajeev Chandrasekhar, Times of India, March 2023
4. India Leveling Up, Lumikai, November 2022

5. India Leveling Up, Lumikai, November 2022
6. Is India's rapidly growing youth population a dividend or disaster ?, Times of India, February
7. KPMG in India industry discussion and secondary research
8. Worldwide mobile data pricing 2022, Cable.UK
9. Amendments to IT Rules 2021 published vide notification G.S.R. 275(E) dated April 2023

1. Summary of recent regulatory guidelines for the online gaming industry



Guidelines issued by MeitY include key provisions that will aid with regulating the gaming industry. Key provisions are captured below:

Constitution of self-regulatory bodies (SRB)

The government has suggested the concept of a self-regulation model for the online gaming sector, wherein it will appoint multiple SRBs comprising industry representatives and other experts (such as child experts, psychology experts, etc.). These SRBs will be responsible for analysing if the online games involve wagering on any outcomes and

confirming if they are permissible as real money games. Criteria for appointment of SRBs has been laid down under rule 4A (2) of the new regulation which includes registration as a Section 8 Company, composition of key stakeholders as the board of director with relevant experience in online gaming, psychology, information technology, amongst others.

Our views:

The efficient implementation of SRB model could help the government in structured regulation of the industry and enhancing the user awareness, by enabling gamers to differentiate between legitimate and fictitious online games. However, government may provide clarifications on a few aspects, including rules for functioning of the SRBs (for co-functioning with other SRBs and reducing the possibility of biasness and favoritism) and constitution of wagering activities (since games like poker, rummy have been classified as game of skill by Indian court.



Due-diligence requirements:

Online gaming intermediaries are required to comply with the due-diligence requirements mentioned in rule 3 of the new regulations. Key additional requirements are captured as below¹⁰:

Publishing key policies

Publish rules and regulations, privacy policy and user agreement on website, mobile based application or both



Compliance to key policies to be informed to users
Inform compliance of rules and regulations, privacy policy and user agreement **to users on periodical basis** and at least once in a year



Changes in key policies to be informed to users
Changes in rules and regulations, privacy policy and user agreement **to be informed to users on periodical basis** and at least once in a year



Retaining user information

Retain user information for a period of **180 days** after any cancellation or withdrawal of registration



Secure computer resources and information
Take reasonable measures to **secure computer resource and information** as prescribed in the Information Technology Rules, 2011.



Information sharing with Government agencies
Provide requisite information to Government agency **within 72 hours** of receipt of order



Reporting of cyber security incidents
Report cyber security incident & share details with Indian Computer Emergency Response Team



Management of certain information
Not host, display, upload, modify, publish, transmit, store, update or share certain information mentioned in Rule 3 (1) (b)



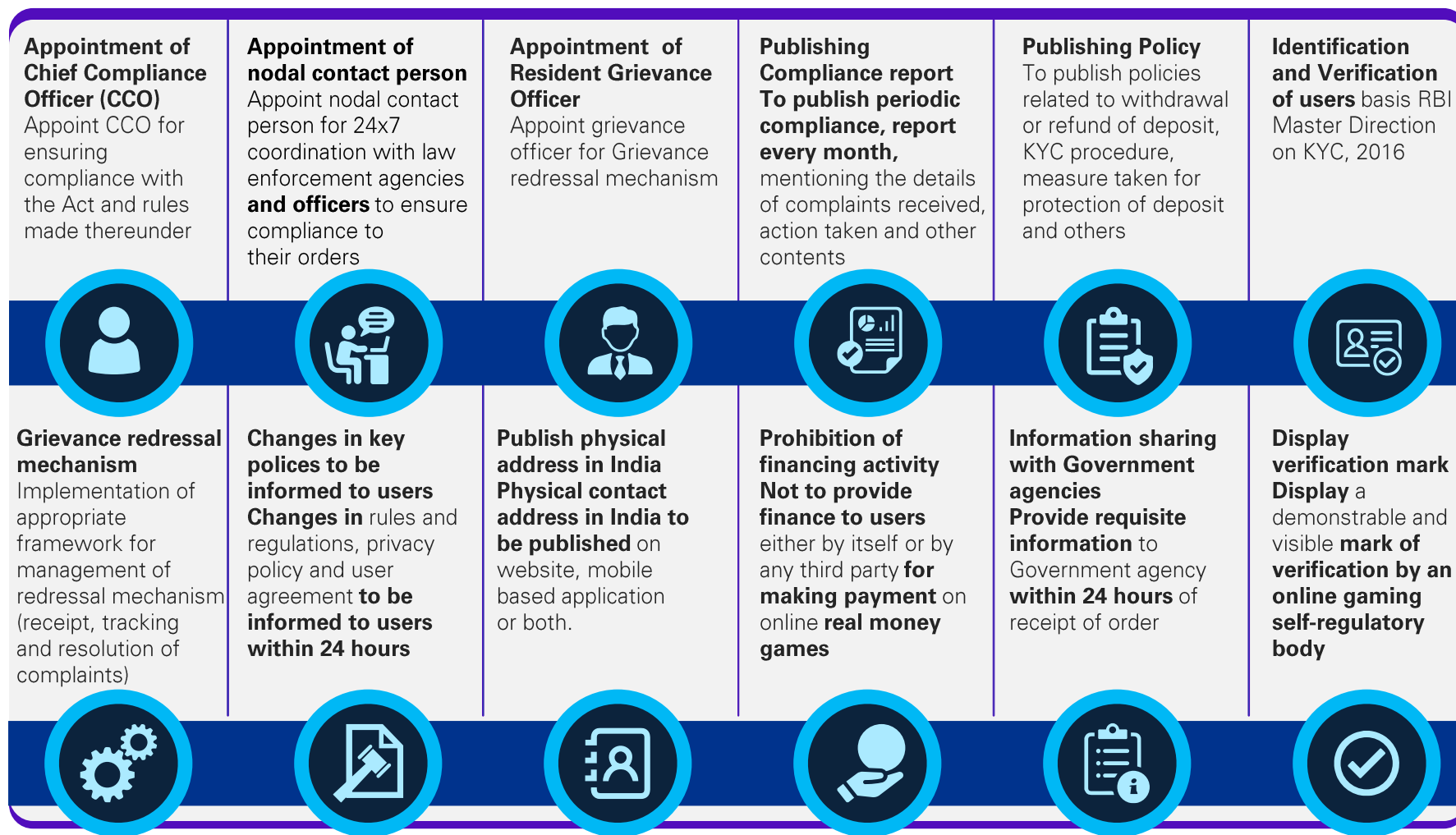
Shall **respect** all the **rights** accorded to the citizens under the Constitution




10. KPMG' in India summarization of amendments to IT Rules 2021

In addition to the pointers captured earlier, online gaming intermediaries providing real money games shall conduct additional due diligence activities like the appointment of key managerial personnel (chief compliance officer, nodal officer and grievance officer), publishing of compliance report, identification and verification of user basis RBI Master circular, etc. Key additional requirements are as captured below¹¹:

Additional due diligence by Real Money games



Our views:
The above-mentioned due-diligence activities could help online gaming intermediaries to augment their operational effectiveness and create a robust governance framework. Further, appropriate disclosure of key policies and other relevant information are likely to boost trust and enable transparency with users and financial institutions.



11. KPMG summary of amendments to IT Rules 2021 published vide notification G.S.R. 275(E) dated April 2023

Grievance redressal mechanism

Given the reach in terms of audience, their maturity levels and other sensitivities, the government has placed a major focus on setting up a grievance redressal mechanism for the resolution of consumer complaints. Online gaming intermediaries shall implement its own framework for receiving, tracking and resolving consumer disputes, which shall be managed by their Grievance Officer. Further, the timelines are also defined in regulations for the resolution of these complaints. Captured below are key aspects included in the regulation for grievance redressal mechanism¹²:

Resolution by Online gaming intermediary



Display Grievance redressal mechanism on website, along with name and contact details of Grievance Officer



Implementation of appropriate framework for management of redressal mechanism



Acknowledgment of complaint within 24 hours



Remove or disable access to the content within 24 hours of receipt complaint of special nature



Acknowledge order received from Government agency / Grievance Appellate Committee



Resolve complaint within 72 hours / 15 days for real money games / other games

Framework

Process

12. KPMG summary of amendments to IT Rules 2021 published vide notification G.S.R. 275(E) dated 6 April 2023

Additionally, the government shall form Grievance Appellate Committees wherein appeals can be filed by any person aggrieved by the decision of the Grievance Officer of online gaming companies. The framework for constitution of the committee and the process of appeal has been laid down in regulation, and a summary of the same is below¹³:

Appeal to Grievance Appellate Committee



Consist of a chairperson and 2 whole time members (one member to be ex-officio and other two members as independent)



Adopt an online dispute resolution mechanism wherein the entire appeal process shall be conducted through digital mode



Order passed by Appellate Committee shall be complied with and uploaded on website



Make an endeavor to resolve the appeal within 30 days from the date of receipt of the appeal.



Appeal to be made by any person who is aggrieved by decision of Grievance Officer



Appeal to be made in case grievance not resolved by Grievance Officer within period specified above

Framework

Process

Our views:

Formation of a grievance redressal mechanism could help in curtailing the risk of non-governance in the gaming industry, since it provides an opportunity to oppressed users to raise their complaints and obtain resolution from the grievance officer / appellate committee. It further empowers the gaming industry and financial institutions to address the concerns of dubious claims raised by users, which is likely to promote healthy corporate governance in the industry.



13. KPMG summary of amendments to IT Rules 2021 published vide notification G.S.R. 275(E) dated 6 April 2023

Key safeguards implemented by other countries

The concept of safeguarding children and users against risk of gaming addiction, financial loss and fraud has been introduced in the new regulation, along with identification/verification of users and due diligence activities. While the Indian government requires online gaming intermediaries and SRBs to formulate measures for the aforementioned, other countries (like China) have mandated stricter guidelines¹⁴, including (but not limited to) the following:

- a) Implementation of real name identification system across all games, wherein players are required to register using their ID number. Online gaming companies have launched new methods, such as facial recognition technology and algorithms, to curb the misuse of ID numbers.
- b) Implementation of age rating systems in online games, to provide guidance to parents and minors about which games are suitable and unsuitable
- c) Limiting the amount of time spent by minors, wherein young

gamers are allowed to play only on public holidays, Fridays, Saturdays, and Sundays from 8.00 p.m. to 9.00 p.m.

- d) Implementing limits on the spending of minors in online games
- e) Self-regulation of games by online gaming companies, by an independent editorial team that will check the content of games before submitting them for approval.
- f) Foreign game companies to work with domestic game publishers for operating the game in the country.

These measures have assisted in reducing the risk of addiction and financial loss among the younger population and better regulation of the industry. Having said that, certain research¹⁵ indicates that users have been able to circumvent existing restrictions through the use of virtual private network (VPN), illegal websites and other software. Further, the stricter guidelines have also resulted in the reduction of online gamers (especially minors).



14. "Game regulations in China: everything you need to know, Niko, February 2020a- and "What to Make of the New Regulations in China's Gaming Industry, China Briefing, November 2021"

15. "Game regulations in China: everything you need to know, Niko, February 2020 and "What to Make of the New Regulations in China's Gaming Industry, China Briefing, 1November 2021"



2. Recent taxation amendments for the online gaming industry



The impact of taxes – both direct tax and indirect taxes – is likely to play a major role in the continuing attractiveness of this industry. The recent proposals on the levy of GST and withholding taxes has the potential impact of disrupting the industry and pushing the industry back by a few years.

Levy of GST

The news surrounding the levy of GST on this industry has been featuring in the headlines in the recent past, first with an INR21,000 crore proposed tax demand on one of the industry players followed by a proposal to levy GST at the rate of 28 per cent on the contribution made by players¹⁶ in real money games.

While the proposed tax demand has been set aside by the Karnataka High Court¹⁷, the proposal to levy GST on the contribution made by the players is to be implemented by 1 October 2023. Currently, the industry is levying GST at 18 per cent on the rake fee / Gross Gaming Revenue earned by it from the players, which could typically be a certain percentage (say, 5 per cent - 20 per cent) of the contribution made by the players.

Our views:

International practice of levying GST either on the rake fee or by giving a deemed credit of winnings (effectively levying taxes on the sum representing contributions received less payouts to winners) could be considered as a precedence for levy of GST. At the same time, gaming platforms may need to come up with offers/options/structures that could keep the participants interested in the games, in light of the high tax incidence.

The clarity provided on the mechanics of tax withholding is welcome for the required certainty and uniformity in operational aspects.



This significant increase in the incidence of taxation is expected to hit the industry hard and with the intention of seeking relief, the industry continues to represent its case to the government for a reasonable tax incidence.

Withholding tax

Net winnings from online games are subject to income tax in the hands of the player at a flat rate of 30 per cent plus applicable surcharge and cess. The proceeds are subject to tax withholding at source by the payer. A recent clarificatory circular issued by the Central Board of Direct Taxes provides guidance on the mechanics of the tax withholding for various practical situations such as multiple user accounts, deposits, withdrawals, bonuses, etc. In line with the government's stance towards the industry, the circular provides a miniscule threshold of monthly winnings of INR100 for relief from tax withholding. The threshold however applies only on withdrawal. At year-end, tax will need to be deducted on the entire winnings.



Unprecedented growth in the online gaming sector has not only boosted the economy but has also presented certain threats to gaming intermediaries and other key players in the financial services sector (banks and other institutions onboarding gaming intermediaries as merchants). This includes potential threats of money laundering, terrorist financing, cyber security, ghost users, etc. Given these threats, online gaming intermediaries and other key players in the financial services sector have been advised to develop a risk-based framework for conducting transaction monitoring, screening and periodic independent testing to identify and reduce such risks. A summary of key threats posed by online gaming are as below¹⁸:

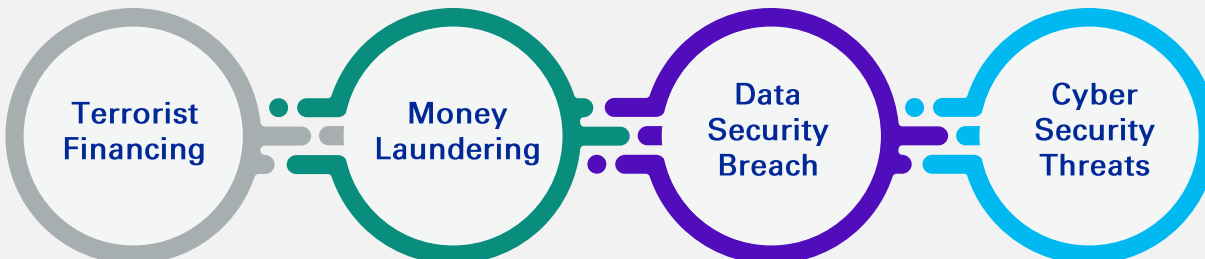
16. "The Council also recommended that valuation of supply of online gaming .. may be done based on the amount paid or payable to or deposited with the supplier, by or on behalf of the player (excluding the amount entered into games/ bets out of winnings of previous games/bets) and not on the total value of each bet placed "

17. Karnataka HC quashes Rs 21,000 crore GST notice against Gameskraft, online gaming industry cheers verdict; Economics Times; May 2023

18. KPMG industry discussion and secondary research



Customer Onboarding Threats	Merchant (' Online Gaming Company') Threat	Transactional Threats
Non-validation of KYC documents	Business involved in wagering / gambling activities	Illegitimate source of funds of customer
Non-verification of user's bank account / UPI used for transactions	Process Gaps in implementation of policy	Customer deposit blocked / not reflected in wallet
Non verification of mobile number / email id of customer	Disclosure requirements not complied by Merchant	Different customers using same bank account number
Non-identification of duplicate records (mobile number, email id, KYC documents, etc.) of customer	Inadequacies in grievance redressal mechanism	Preferential treatment to selected customers
	Non-identification of duplicate / ghost users	Chargeback / claims not settled by merchant
	Financing options provided by Merchant to Customer	Dubious chargeback claims by customer
	Non-availability of policy required under new regulation	Winnings of customer not reflected in wallet
	Lack of information sharing between merchant and banks	Anonymous beneficiary details and end use of funds
	Non-compliance with due diligence activities under new regulation	Lack of adequate procedures to reconcile settlement of transactions
	Non retention of user information for specified period required under regulation	Restriction on withdrawal of winnings of customer
		



Considering the growth envisaged in this sector, the risks posed due to potential non-compliance and associated regulatory requirements, it is recommended that each entity (online gaming intermediary) have a mechanism in place to track adherence to laid down procedures.

Key elements which may be considered are captured below:



While organisations strive to build profitable ventures, compliance to laid down regulations is equally important. It is recommended that organisations ensure transparency in operations while keeping long term objectives in mind and frame policies accordingly. In conclusion, organisations can be better prepared to demonstrate compliance to regulations as regulators may come knocking their doors anytime.

Key definitions

Online real money game:

online games where a user makes a deposit in cash or kind with the expectation of earning winnings on that deposit'. However, online games that are involved in wagering on any outcome will not be classified as real money games.

Winnings:

Prize, in cash or kind, which are distributed or intended to be distributed to a user based on the performance and in accordance with the rules of the online game.

Online gaming intermediary:

it means any intermediary that enables the users of its computer resource to access one or more online games.

Online games:

games that are offered on the internet and are accessible to users via computer resource or intermediaries.

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30 years
and beyond

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