



Legalization Of Cryptocurrency And Its Impact On Indian Economy: An Overview

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Abstract:-

The monetary part of a country's economy is likely the most well-known but also the least well-understood aspect. The role and history of money has gone through numerous stages since the Babylonian era, starting with barter systems where products and commodities are exchanged in exchange for other commodities through present era digital currency. The scope and future of crypto currencies in the Indian economy should be thoroughly researched. There is a scarcity of literature on how crypto-currency will alter the financial transaction landscape in the coming dynamic decade. In this Paper, Researcher will investigate legal validity of crypto currency in India, whether it will boost up Indian economy?

Key words: crypto currency, legalization, online, Indian economy.

1. Introduction:-

The monetary part of a country's economy is likely the most well-known but also the least well-understood aspect. The role and history of money has gone through numerous stages since the Babylonian era, starting with barter systems where products and commodities are exchanged in exchange for other commodities through present era digital currency.

Cryptocurrency; Definition and Scope

“The term cryptocurrency is an intangible form of non-legal tender which can be used in place for legal tender² and existed in electronic/ digital form used between online/Cryptocurrency members community”³

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²European Central Bank. (2012).Virtual Currency Scheme 2012 report. Retrieved from *available at* <https://www.ecb.europa.eu/pub/pdf/other/virtualcurrencyschemes201210en.pdf> (last visited on 13 feb,2022)

³ Hughes, S. J., &Middlebrook, S. T. (2015). Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries. Yale J. on Reg., 32, 495.

“Virtual currencies are a subset of cryptocurrencies . Bitcoin is a subset of virtual-currency where value of a particular unit is validated through cryptography. virtual-currency generally requires consent of buyer and seller to a transaction.⁴ When a cryptocurrency is not backed by any precious metals but backed by government via giving legal tender status then such a cryptocurrency becomes fiat currency and not a commodity-based currencies or nonlegal tender currency which is simply a cryptocurrency. “Therefore fiat cryptocurrency status of cryptocurrency⁵ transaction would then fall back under the dominion of traditional money transfer regulation”.

The twenty-first century has seen a massive development of technology, as well as an increase in the usage of the Internet and virtual transactions, which has ominously flowered the monetary system, proposing spectacle - virtual currencies.⁶ Because of the growing acceptability of crypto currencies around the world, Venezuela and the Marshall Islands have decided to legalise them. The scope and future of crypto currencies in the Indian economy should be thoroughly researched. There is a scarcity of literature on how crypto-currency will alter the financial transaction landscape in the coming dynamic decade. Cryptocurrencies have showed promise as infrastructure for pseudonymous online mechanisms and anonymity in payments, as well as low-cost remittance, trust-free digital asset exchange, and smart contracts. However, block chain methods have inherent scaling limitations that trade off throughput for inactivity, preventing understanding of its potential⁷. Despite the numerous advantages and opportunities that virtual currencies may provide, it is difficult to overlook the associated risks - virtual currencies, as a form of unregulated market control, may facilitate higher-risk activities such as money laundering, terror financing, and mafia money transfer, to name a few. This paper examines the general study and calculation of risks associated with the rise of crypto currencies, as well as the insufficient, non-unified regulation and the different dangers that come with it⁸. The paper's key conclusions show that crypto currencies have a bright future if suitable procedures are in place to mitigate the risks associated with a well-structured regulatory authority for monitoring, security, and regulation.⁹ One of the most important considerations when discussing money and its capabilities is the distinction between money and riches. Wealth management and money generation, according to T.H. Greco, are two endpoints of a broad continuum that are not interchangeable.

The application of human skill to natural assets that produce valuable commodities, services, and currency can be used to manage wealth. Money generation, on the other hand, is a fundamental requirement of every thriving economy, as it allows money to be channelled in the most efficient way possible to provide the

⁴ Velde, F. (2013). Bitcoin: A primer. Chicago Fed Letter, (Dec).

⁵ New York State Administrative Procedure Act (SAPA) 2015. 23 NYCRR Part 200 Virtual currencies

⁶ Dibrova, Alina. “Virtual currency: new step in monetary development.” *Procedia-Social and Behavioral Sciences* 229: 42-49 (2016).

⁷ Troster, Victor, et al. “Bitcoin returns and risk: A general GARCH and GAS analysis.” *Finance Research Letters* (2018).

⁸ Moore, Winston, and Jeremy Stephen. “Should cryptocurrencies be included in the portfolio of international reserves held by central banks?” *Cogent Economics & Finance* 4.1: 1147119 (2016).

⁹ Andrews, Leo John Baptist, and Linesh Raja. “A study on m-health Inline with the sensors applying for a real time environment.” *Journal of Statistics and Management Systems* 20.4: 659-667 (2017).

best results.¹⁰ While I fully appreciate such thinking, the focus of this article will be on understanding different perspectives on money, particularly in terms of cash. It can be agreed that while discussing widely radiated currencies that are classified and broadly related to national alliances, a union understanding and standards have been created. Nonetheless, owing to Rogajanu and Badea's fame, the address in nineteenth century the question of private currency saw substantial development.

When it comes to the financing of illegal substances, private money emission is a possibility. Regardless of the drawbacks that virtual currency has, it has managed to significantly expand the acceptance. Various features of virtual currencies will be summarised in the scope of this article. This paper will do a literature and statistical analysis to determine whether new types of currencies have the potential to diversify their usage options in the future, and whether virtual money could reduce the function of nationally issued money in any way. Above all, potential legal incentives for the growth of virtual currencies will be discussed.

2. Indian Acts on Cryptocurrency:-

Let's look at the regulations that might apply to cryptocurrency technology and its many goods in India, to see whether Bitcoin is under the scrutiny of the central government.

- **RBI Act, FEMA(Foreign Exchange Management Act, 1999) and Constitution Of India Act:**

The subject matter to foreign exchange, legal tender, legislate currency, checks, promissory notes, coinage, legislate currency, legal tender and bills of exchange other such instruments by the State governments and Center government in India is provided under Article 246¹¹ of the Indian Constitution, as well as under Entry 36¹² and 46¹³ of List I of the VII Schedule of Indian constitution. The test is whether Bitcoin satisfies any of the aforementioned instruments' requirements, allowing the central authority to regulate. When it comes to currency, we must first comprehend The Reserve Bank Of India Act. Surprisingly, The Reserve Bank Of India Act does not define currency; rather, the Foreign Exchange Management Act of 1999 (FEMA) defines it as "all currency notes, postal notes, postal orders, money orders, cheques, draughts, travellers' cheques, letters of credit, bills of exchange and promissory notes, credit cards, or such other similar instruments, as may be notified by the Reserve Bank" in Section 2 (M). One rupee and RBI-issued

¹⁰ Corbet, Shaen, et al. "Exploring the dynamic relationships between cryptocurrencies and other financial assets." *Economics Letters* 165: 28-34 (2018).

¹¹ Article 246 of Constitution Of India,1949

(1) Notwithstanding anything in clauses (2) and (3), Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule (in this Constitution referred to as the "Union List").

(2) Notwithstanding anything in clause (3), Parliament, and, subject to clause (1), the Legislature of any State 1 *** also, have power to make laws with respect to any of the matters enumerated in List III in the Seventh Schedule (in this Constitution referred to as the "Concurrent List").

(3) Subject to clauses (1) and (2), the Legislature of any State 1 *** has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List II in the Seventh Schedule (in this Constitution referred to as the "State List").

(4) Parliament has power to make laws with respect to any matter for any part of the territory of India not included 2 [in a State] notwithstanding that such matter is a matter enumerated in the State List.

¹² Entry 36 of List I of the VII Schedule, Currency, coinage and legal tender; foreign exchange

¹³ 46 of List I of the VII Schedule. Bills of exchange, cheques, promissory notes and other like instruments.

notes are defined as legal currency under the Currency Ordinance 1940, and Bitcoin does not fit into this category because it is not legal tender.

This view is also supported by Section 22, According to Section 26 of the RBI Act, the Reserve Bank of India has sole jurisdiction to issue bank notes, and bank notes are legal tender in India. Bitcoin is not cash, but it does have some features of currency or legal tender, making it "such other similar instruments" as defined by Section 2(h) of the RBI Act and susceptible to notification by the RBI, according to this study. As a result, the RBI must decide whether to recognise certain electronic records claiming to be "Decentralized Digital Currency" or "Virtual Currency," such as Bitcoin, litecoins, bbqcoins, and dogecoins, as well as other similar instruments, as such.

- **Payment System Rules and Operating Standards in India**

The Reserve Bank Of India is empowered to regulate¹⁴, supervise,¹⁵ and clear or settle payments between payers and beneficiaries in the payment system, Section 18 of the Payment System and Settlement Act (PSSA) 2007¹⁶ was enacted. Bitcoin cannot be regarded as a payment system under PSSA due to its inability to clear or settle transactions. According to RBI guidelines, an instrument contains the value stored in it, and the possessor must pay that value in a transaction. Bitcoin trading, on the other hand, has no such requirements while dealing, and its value is speculative, established by a market that fluctuates and fails to meet the aforementioned conditions.

- **Deposit Taking and Deposit Insurance**

Accepting deposits is a heavily regulated industry in India, according to Section 5(b) of the Banking Regulation Act¹⁷, 1949. When a bank fails or is unable to refund the full amount of a deposit, the depositors' deposit is guaranteed to be recovered up to Rs. 1 lakh, regardless of the higher amount put by the depositor in his account with the bank.¹⁸ Because Bitcoin is not issued or held by a bank, the sum held in cryptocurrency could be classified as deposits. However, because Bitcoin is not issued or held by a bank, it does not meet the RBI's criteria. As a result, because Bitcoin is a non-legal money that can be held by non-bank entities, the following regulations do not apply to the amount held or represented by it.

- **Counter-Terrorism and Anti-Money Laundering (AML)**

Financing Due to criminals' access to and misuse of financial assets for various reasons, financial security is a major concern at both the international and national levels at all times. To put a stop to these illegal acts, international law enforcement authorities are collaborating closely. It is imperative for all authorised

¹⁴ Banking Regulation Act. 1949. S. 6(2). (Ind.)

¹⁵ Banking Regulation Act. 1949. S. 5(b). (Ind.)

¹⁶ Summers, B. J. (2012). Payment Systems: Design, governance and oversight: Central Banking Publ.

¹⁷ (1) This Act may be called the Banking 1[Regulation] Act, 1949. [(2) It extends to the whole of India 4[***.] (3) It shall come into force on such date³ as the Central Government may, by notification in the Official Gazette, appoint in this behalf., available at < <https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/BANKI15122014.pdf>> (last visited on 14 feb,2022)

¹⁸ RBI Deposit Insurance and Credit Guarantee Corporation General Regulations. 1961.RBI Deposit Insurance System (DIS). (Ind.)

payment system operators and service providers in India to follow the Know Your Customer guidelines¹⁹ and to identify suspicious transactions to the Financial Intelligence Unit-India under the Prevention of Money Laundering Act (PMLA) 2002 and the Prevention of Money Laundering Regulations, 2008²⁰ (FIU-India).²¹ In contrast to the previous, the Bitcoin system's structure eliminates this necessity and ensures that the identities of merchants and purchasers remain anonymous. Consequently, the Bitcoin system does not meet the standards outlined above, which need customer information in order to build and maintain an account on the Bitcoin platform.

- **Securities Exchange Board of India (SEBI):-**

In the financial markets, people who help with cryptocurrency exchanges are called broker-dealers. This is one method to control cryptocurrency exchanges. Whenever Cryptocurrency is kept as an investment or when a share amount is paid in Virtual currency, the SEBI has a key role. If a broker-dealer has a customer's money in the stock market in the form of cryptocurrency, the Securities and Exchange Board of India Act 1992 and the Securities Contracts Regulations (SCRA) 1996²² must be accompanied. As required by SEBI (Stock-Brokers & Sub-Brokers) Regulations, 1992²³ (as amended in 2006) to ensure investor protection, rights and liabilities of parties involved in transactions, a dispute redressal mechanism for investors, and all standard procedure and compliance requirements under PMLA Rules, Maintain a robust client identification, anti-money laundering,²⁴ and economic sanctions programme, for example. As a result, if Bitcoin exchanges wish to provide Bitcoin services for investment or dividend purposes, they must comply with the aforementioned requirements, leaving Bitcoin customers vulnerable to exploitation and making AML and KYC compliance nearly impossible.

- **Taxation Law on Cryptocurrency:**

The Ministry of Finance has begun to regulate cryptocurrency for revenue purposes through the Department of Revenue. While concentrated on "Income from Capital Gains (both short and long term) and income from other sources," we attracted the application of the Income Tax on virtual currency trades, and the gain from it will be taxed. If you often buy and sell cryptocurrencies, the profits from such trading must be reported as trading income on your tax return (ITR). The tax treatment may differ if you do not trade in such currencies. Long-term capital gains, are taxed at a fixed rate of 20%, with indexation advantages (inflation-adjusted) on investments of more than 3 years, just like all other investment tools. Furthermore, investments lasting less than three years should be treated as short-term capital gains and taxed according to your tax bracket.

¹⁹ RBI Direction on Know Your Customer (KYC) Direction, 2018 (updated)

²⁰ Prevention of Money Laundering Act. 2002. S. 18 read with S. 10(2)(Ind)

²¹ Prevention of Money Laundering Act. 2002. S. 12(Ind.)

²² Short title, extent and commencement. (1) This Act may be called the Securities Contracts (Regulation) Act, 1956. (2) It extends to the whole of India. (3) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint

²³ SEBI (Stock-Brokers & Sub-Brokers) Regulations. 1992. Regulations 3, 17, 18 & 18A. (Ind.)

²⁴ SEBI. (2008). Master Circular on Anti Money Laundering and Combating Financing of Terrorism (AML and CFT) Standard. (ISD/AML/CIR-1/2008). Retrieved from available at <https://www.sebi.gov.in/sebi_data/attachdocs/1332320892543.html> (last visited on 12 Feb, 2022)

3. Financial Issues and Challenges:

- **Stability:** Because the cryptocurrency market is less stable in nature, it carries a high level of financial risk. As can be seen, bitcoin dropped by almost 50% in the third quarter of 2017 compared to the same quarter the previous year. One of the biggest difficulties in this sector is stability, crypto-currency Nature's ephemeral: The most important financial issue in modern transactions is the volatility nature of cryptocurrency. This instills negative feelings in the minds of Indian investors.²⁵
- **Contradict the traditional transaction:** Contrary to popular belief, the crypto-currency market differs significantly from traditional trading techniques. However, this feature is viewed as both a curse and a market differentiator.²⁶ In this transaction that strengthens the platforms, the mediator players are not involved.
- **No regulatory authority:** Because the higher authorities of any country's regulatory system are not involved in the crypto-currency market, the price is established by them. This increases transaction and transparency in the system.
- **All players agree on the pricing:** The price and transaction cost are agreed upon by all parties participating in the transaction. This raises the market risk as well as the risk of losing purchasing power.
- **Financial risk:** Compared to other traditional currencies, bitcoin carries a higher financial risk. Because it is very volatile in nature, the risk and return are both increased. Exchange risk is also connected with cryptocurrencies because there is no middleman in the transaction, hence the price of crypto-currency is determined by market supply and demand.
- **Market risk:** It is dynamic and fluctuates dramatically. The market risk linked with the CC has an impact on its value. It is a difficulty that CC must tackle as well.
- **Liquidity risk:** The CC market isn't particularly liquid. It is a problem for the CC market. Investors suffer difficulties as a result of this risk. Every investor wishes for a portion of his investment to remain liquid.
- **Operational risk:** The CC market operates on a block-chain basis, which has some limitations and concerns. With the support of a well-trained crew working in the background, the operational risk can be decreased. The effective platform and staff can simply reduce the weaknesses in the system.

²⁵ Durugkar, Santosh, and Ramesh C. Poonia. "Optimum utilization of natural resources for home garden using wireless sensor networks." *Journal of Information and Optimization Sciences* 38.6: 1077-1085 (2017).

²⁶ Liu, Weiyei. "Portfolio diversification across cryptocurrencies." *Finance Research Letters* (2018).

4. Conclusion:-

Because of the economic ups and downs in India during Covid-19, as well as the increasing popularity of E-commerce, India should adopt a bold and decisive decision to regularise and legalise cryptocurrencies in India. The regulation is concerned with regulating the technology platform models utilised by cryptocurrency and intermediaries in the provision of various services. The RBI and the Central Government will have to decide whether cryptocurrencies should be recognised as legal tender and traded against fiat currency. Keeping in mind that the cryptocurrency industry does not pose a threat to the banking system, the RBI should not dismiss it as a viable new technology solution with potential financial applications. Rather, the RBI should investigate how to employ Distributed Ledger Technology (DLT) to benefit India's financial services and broader economy. Blockchain's application in trading, finance, lending, and other financial operations will usher in a new era of fintech products and services in India's economy. As a result, the centralised or decentralised distributed ledger, a technologically new platform, has the potential to improve India's financial system's efficiency and inclusiveness. The digitally empowered society, and also the Digital India Program and the knowledge economy, will benefit from the cryptocurrency platform. This effort will be a push to guarantee that electronic banking services are covered by E-Government. Product design that is user-friendly, technological advancements, job opportunities for young people, and the Indian economy's overall inclusive growth India can use this payment ledger technology to break down socioeconomic boundaries and enable widespread financial access.

