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Supreme Court on Cryptocurrency

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This article is based on **Illogical ban, Cryptocurrency: Looking ahead, Figuring out risks posed by cryptocurrencies, Digital currency is back in the Indian market.** It talks about the implications of the recent Supreme Court's order on Cryptocurrency.

Recently, the Supreme Court **struck down** a circular of Reserve Bank of India, which bans financial institutions from enabling deals in digital or cryptocurrencies. The ban that came into force in April 2018, had crippled the Indian cryptocurrency industry.

This ban was challenged by the **Internet & Mobile Association of India (IAMA)** in the Supreme Court, the IAMA pleaded that dealing and trading in cryptocurrency was a legitimate business activity and that the RBI did not have jurisdiction over it **as these assets could be classified as commodities rather than currency.**

CryptoCurrency or Crypto-Assets

- The money that we use (fiat currency) is a product of lending by institutions (commercial banks).
 - Its credibility comes from the backing given by the central bank of a country.
 - Its ubiquitous usage is because of a law passed by the legislature, which establishes that taxes can only be paid in state-issued fiat currency.
- Although cryptocurrencies are intended to function as a means of payment, unlike fiat currencies, they lack a sovereign guarantee and their source of value is not quite clear.
- They are more like investment instruments like shares in the equity market and that's why they can be better-called **Crypto-Assets.**

What did the judgment hold?

- **Economic Dimension:** The judgment holds that while the RBI had the power to take note of and deal with virtual currencies, the prohibition was excessive since it cut off the lifeline of otherwise legitimate trade.

It also holds the RBI did not show any harm to its regulated entities as a result of their facilitating virtual currency trade or any defects in the functioning of virtual currency exchanges.
- **Administrative Aspect:** The Supreme Court held that an outright ban on virtual currencies would be a **disproportionate measure** by the government since many less intrusive measures are available.
 - It is worth remembering that virtual currency transactions do not operate in a complete regulatory vacuum.
 - Several existing laws such as the Consumer Protection Act, Information Technology Act, Foreign Exchange Management Act, PMLA, besides tax, deposit-related and criminal laws apply to the virtual currency domain just as they apply to any other economic activity.
 - In fact, action has already been taken in India under many of these laws against errant persons and entities operating in the virtual currency domain.
- **Constitutional Aspect:** The Supreme Court also held that the ban was unconstitutional. It is in violation of the **freedom to carry on trade guaranteed by Article 19(1)(g) of the Indian Constitution.**

Why had RBI banned cryptocurrencies in 2018?

- Cryptocurrencies are a poor unit of account, as demonstrated by their **frequent and high fluctuation in value.**
- They pose several risks, including **anti-money laundering and terrorism financing** concerns (AML/CFT) for the state and liquidity, credit, and operational risks for users.
- On the perspective of consumers, issues linked to cryptocurrencies are **heightened by the striking paucity of information on their design, use and operation and indications of market manipulation.**
- It is possible that the **business models of commercial banks may be seriously disrupted.**

Effects of lifting this ban on Cryptocurrency

- This lifting of the ban will help in **incorporation of blockchain technology**.
 - Blockchain technology is the underpinning technology behind many cryptocurrencies.
 - Blockchain, which was conceptualised for the verification of anonymous peer-to-peer transactions in bitcoin, has since been adapted for many other purposes.
 - It creates electronic ledgers, where every transaction is recorded and is open to verification by many persons while maintaining confidentiality.
 - It quickly detects fakes and disallows duplicate transactions.
 - Blockchain technology forms a crucial part of **Industrial revolution 4.0**.
 - It is also estimated that blockchain will generate \$3.1 trillion in new business value by 2030.
- **Cryptocurrencies act as alternative investments.**

These currencies may enable savvy traders to hedge global volatility, as it did during the financial turmoil of 2012-13.
- There is a **worldwide proposal for central-bank digital currencies**, which could allow for money to be transferred between users without the involvement of a third-party (commercial bank).

Allowing cryptocurrency will enable India to be part of this global deal.
- For India, aiming to be a **digital economy powerhouse**, embracing emerging technologies like cryptocurrency and blockchain is a must.

Way Forward

Rather than impose bans, it would be more pragmatic to institute awareness campaigns to alert investors to specific risks, and to monitor trades for fraud and scams. Fintech industry needs to jointly with the RBI and the government on a constructive policy framework for cryptocurrencies in India. In this context:

- There is a need for RBI to formulate a **detailed regulatory framework** to license virtual currency intermediaries like exchanges.
- These local cryptocurrency exchanges could be asked to adhere to the **KYC norms** followed by stock exchanges.
- There is a need for the **Fintech Industry** to show that virtual currency trade can be carried on in a safe and responsible manner with self-imposed safeguards, such as adequate customer due diligence.
- One immediate step that could be taken by the government is to designate virtual currency intermediaries as reporting entities under the **Prevention of Money Laundering Act (PMLA)**.
- These steps should ideally be done by a **new expert regulatory body** with capability in technology, economics and finance.

A vibrant cryptocurrency segment could add value to India's financial sector. Thus, in the face of growing technological innovation in the financial sector, it is critical to strengthen the supporting regulatory frameworks of India that operate regardless of the nature of an instrument.

Drishti Mains Question

A vibrant cryptocurrency segment could add value to India's financial sector. Discuss