



Regulation of Crypto Assets

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This editorial is based on the article **We need smart regulation to unlock the true potential of crypto assets** which was published in The Livemint on 26/10/2021. It talks about the issues of cryptocurrency assets and issues of regulation of the crypto.

Often touted benefit of crypto assets is that the crypto makes finance more inclusive and decentralized. But India already has the world's largest **financial inclusion** programme in **Jan Dhan**. In the past seven years, 430 million bank accounts have been created for the under-banked. A majority, 55%, of them are women. Crypto can't match the scale of Jan Dhan Yojana in India.

Moreover, Regulation of crypto assets such as bitcoin and ethereum is a hot topic globally. Countries are in various stages of banning, un-banning, re-banning and regulating crypto assets. We may take some cues from other countries, but what we need is smart regulation that's made in India.

Reasons For Adoption of Crypto in India

- Financial inclusion is not the main reason to embrace crypto assets in India. But there are three compelling **India-specific reasons to embrace crypto assets**.
- **Establish India as an Integral Part of the New Financial Ecosystem:** Large global financial institutions and investors are adding crypto assets to their portfolios.
 - Finance firms, banks, fintech and crypto startups can tap into the huge growth of the industry. **Software technology parks (STPs)** and **special economic zones (SEZs)** enabled the IT services boom.
 - Creative '**crypto export zone**' schemes can incubate clusters of excellence and create world-class financial services firms and unicorns.
- **Capitalize on New Technology and Services Opportunities:** Blockchain application development, its scalability, security and analytics are their next growth opportunities. To cater to this demand, there is a need for a large talent pool with expertise in the crypto tech stacks.

- **Scope of Financial Innovation:** There is a burst of technology innovation and business models around blockchains. There are several interesting applications, but new killer apps will emerge. The impact of new technologies is overestimated in the short term, but underestimated in the long term.

Key Regulatory Concerns

- **Investor protections:** Investor protection has been a top priority for Indian regulators. Crypto assets are seen as high-risk, speculative assets. Investor education, guidelines against mis-selling and other safeguards are needed.
 - Crypto assets are now better understood as digital assets, instead of as digital currencies.
 - Regulating them like commodities and clarifying their tax treatment is a win-win. The government's tax revenues can go up.
 - It can also increase the number of tax filers (only 64 million in FY20) and the number of taxpayers (14 million).
- **Sidestepping current regulations:** Some crypto assets may allow individuals to bypass securities issuance laws. That's a potential risk to economic stability.
 - If crypto holders have to declare their holdings above a particular level in their tax forms, such concerns can be mitigated.
- **Illicit transfers:** Anonymous transfers of crypto assets may weaken **anti-money laundering laws** or combating the financing of terrorism rules. That's a potential national security issue.

Issues Associated with Banning Decentralised Cryptocurrencies

- **Blanket Ban:** The intended ban is the essence of the Cryptocurrency and Regulation of Official Digital Currency Bill, 2021. It seeks to prohibit all private cryptocurrencies in India.
 - However, categorising the cryptocurrencies as public (government-backed) or private (owned by an individual) is inaccurate as the cryptocurrencies are decentralised but not private.
 - Decentralised cryptocurrencies such as bitcoin aren't or rather, can't be controlled by any entity, private or public.
- **Brain-Drain:** Ban of cryptocurrencies is most likely to result in an exodus of both talent and business from India, similar to what happened after the RBI's 2018 ban.
 - Back then, blockchain experts moved to countries where crypto was regulated, such as Switzerland, Singapore, Estonia and the US.
 - With a blanket ban, blockchain innovation, which has uses in governance, data economy and energy, will come to a halt in India.

- **Deprivation of Transformative Technology:** A ban will deprive India, its entrepreneurs and citizens of a transformative technology that is being rapidly adopted across the world, including by some of the largest enterprises such as Tesla and MasterCard.
- **An Unproductive Effort:** Banning as opposed to regulating will only create a parallel economy, encouraging illegitimate use, defeating the very purpose of the ban.
A ban is infeasible as any person can purchase cryptocurrency over the internet.
- **Contradictory Policies:** Banning cryptocurrency is inconsistent with the Draft National Strategy on Blockchain, 2021 of the Ministry of Electronics and IT (MeitY), which hailed blockchain technology as transparent, secure and efficient technology that puts a layer of trust over the internet.

Way Forward

- **Regulation is the Solution:** Regulation is needed to prevent serious problems, to ensure that cryptocurrencies are not misused, and to protect unsuspecting investors from excessive market volatility and possible scams.
The regulation needs to be clear, transparent, coherent and animated by a vision of what it seeks to achieve.
- **Clarity on Crypto-currency definition:** A legal and regulatory framework must first define crypto-currencies as securities or other financial instruments under the relevant national laws and identify the regulatory authority in charge.
- **Strong KYC Norms:** Instead of a complete prohibition on cryptocurrencies, the government shall rather regulate the trading of cryptocurrencies by including stringent KYC norms, reporting and taxability.
- **Ensuring Transparency:** Record keeping, inspections, independent audits, investor grievance redressal and dispute resolution may also be considered to address concerns around transparency, information availability and consumer protection.
- **Igniting the Entrepreneurial Wave:** Cryptocurrencies and Blockchain technology can reignite the entrepreneurial wave in India's startup ecosystem and create job opportunities across different levels, from blockchain developers to designers, project managers, business analysts, promoters and marketers.

Conclusion

In summary, a smart regulatory approach should consider both the potential upside and downside. It fosters financial innovation, safeguards investors and unshackles the Indian crypto ecosystem.

Drishti Mains Question

India needs proper regulation to unlock the true potential of crypto assets. Discuss.
