



Perspective: The Crypto Question

Why in News?

- When [Bitcoin](#) started in 2008, the total market capitalisation of all cryptocurrencies was only \$20 billion in early 2017 which **went up to \$289 billion** in the next three years and thereafter exploded to reach a peak of \$2.9 trillion in November 2021.
- In the last three months, it has again **witnessed a sharp decline**.
- **Bitcoin:** It is a type of digital currency that **enables instant payments** to anyone. Bitcoin is **based on an open-source protocol** and is not issued by any central authority.
- **History:** The origin of Bitcoin is **unclear**, as is who founded it. A person, or a group of people, who went by the identity of **Satoshi Nakamoto** are said to have conceptualised an accounting system in the aftermath of the **2008 financial crisis**.
- **Use:** Originally, Bitcoin was intended to provide an **alternative to fiat money** and become a universally accepted medium of exchange directly between two involved parties.
 - Fiat money is a **government-issued currency** that is not backed by a commodity such as gold.
 - It gives central banks **greater control over the economy** because they can control how much money is printed.
 - Most modern paper currencies, such as the **US dollar and Indian Rupee are fiat currencies**.

What are the Key Points?

- **Current Scenario:** As of today the **total number of [cryptocurrencies](#) is 17,697** and the total number of [crypto exchanges](#) is **462**.
 - Currently, there is **no regulation or any ban on the use of cryptocurrencies** in India.
- **RBI's Stand:** The [Reserve Bank of India \(RBI\)](#) has earlier **banned banks from supporting crypto transactions**, however, the RBI order was reversed by the [Supreme Court order of March 2020](#).
 - The RBI has repeatedly underlined its strong view against cryptocurrencies, saying these **pose a serious threat to the macroeconomic and financial stability of the country**.
- **Government's Stand on Crypto:** The **Government of India is working** on legislation for the regulation of this sector.

What is Cryptocurrency?

- Cryptocurrency, sometimes called crypto-currency or crypto, is any form of currency that exists digitally or virtually and uses cryptography to secure transactions. Cryptocurrencies don't have a central issuing or regulating authority, instead using a decentralized system to record transactions and issue new units.

- It is supported by a decentralized **peer-to-peer network** called the **blockchain**.

What is Blockchain Technology?

- **Blockchain technology** ensures that **all transactions in cryptocurrencies are recorded** in a public financial transaction database.
 - Bitcoin, Ethereum, Ripple are a few notable **examples** of cryptocurrencies.
- Blockchain derives its name from the **digital databases or ledgers** where information is stored as **“blocks”** that are coupled together forming **“chains”**.
 - It offers a **singular combination of permanent and tamper-evident record-keeping**, real-time transaction transparency, and auditability.
 - An exact copy of the blockchain is **available to each of the multiple computers** or users who are joined together in a network.
 - Any new information added or altered via a new block is to be vetted and **approved by over half the total users**.
- **Significance of Blockchain:**
 - Blockchain technology can **facilitate innovations** across a range of processes and applications requiring management, storage, retrieval, and safety of vast and important information.
 - **These include** - management of information pertaining to financial transactions (as in the case of cryptocurrencies), electoral voting, medical records, academic lessons, property ownership records, and professional testimonials.
 - A decentralised framework like blockchain **makes the system and the information stored therein fraud-proof, transparent, and credible**.

What is the Current Status of Crypto in India?

- The **Union Budget 2022-2023** also proposed to **introduce a digital currency** in the coming financial year.
- At the moment, there is **no legislature that covers cryptocurrencies** in India, however, owning cryptocurrencies is still **not illegal**.
- As of now, a **30% tax on income from virtual assets** was announced.
 - China has declared **all cryptocurrency transactions illegal**, effectively imposing a complete ban, whereas **El Salvador has permitted Bitcoin as legal tender**.

Why is there a Need for the Regulation of Crypto?

- As crypto is not a legal tender, it is to be **treated as a separate class** so there's a need for the government to come up with a **separate regulation for crypto**.
 - According to the RBI, if people start treating crypto as a currency then there would be an **opportunity for peer-to-peer lending** that clearly requires regulation.
- 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**.

Why should Crypto be Classified as an Asset not a Currency?

- The main advantage of cryptocurrency is that the transactions are way **cheaper and faster to execute** because the transactions **don't have to be handled by a series of intermediaries** before they reach their destinations and it is **not possible to manifest that utility within India**.
- However, the rest of the world will use crypto for the main purpose for which it was built, and treating it as a digital asset the Indian government will **only be able to monetize the appreciation in value**.

What are the Concerns Associated with Cryptocurrencies?

- **Bombardment of Advertisement:** The crypto market is seen as a **way to earn quick profits**.

Due to this, there is a bombardment of advertising, **both online and offline**, to lure people into speculating in this market.

- However, there are concerns that these are **attempts to mislead the youth** through **“over-promising”** and **“non-transparent advertising”**.

- **Counterproductive Utility:** Unregulated crypto markets can become avenues for [money laundering](#) and [terror financing](#).
- **Macroeconomic and Financial Stability:** The extent of investment exposure of Indian retail investors in this unregulated asset class poses a risk to Macroeconomic and Financial Stability.
- **Stock Market Issues:** [Securities and Exchange Board of India \(SEBI\)](#) has flagged the issue that it has no control over the **“clearing and settlement” of cryptocurrencies**, and it cannot offer counterparty guarantees as is being done for stocks.
 - Further, **whether cryptocurrency is a currency, commodity, or security has not been defined.**
- **Blockchain Technology:** As crypto works on blockchain technology there are several concerns regarding this as well.
 - **Low Scalability:** Blockchains work fine for a **small number of users**. However, when the user number increases on the network, the transactions take **longer to process**.
 - As a result, the **transactions cost higher than usual**. It also restricts more users to the network.
 - **Security Challenges:** Blockchains are vulnerable to network attacks as they were **not originally designed for network protocols**. There are challenges of insertion of malware files and objectionable content as Blockchain services continue to grow.
 - This **raises issues** of privacy violation, potentially illegal files, copyright violations, malware, etc.

Way Forward

- **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.
 - At the time of the transaction, the KYC documents are always **preserved at two levels**- one is at the **exchange level and also at the bank level** because customers are using the bank accounts to initiate the transaction.
- **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.
- **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.
- **Legislative Framework:** India is yet to table the Cryptocurrency and [Regulation of Official Digital Currency Bill, 2021](#), which will lay down the regulatory framework for the launch of an **“official digital currency”**.
 - Thus, there is a **need to expedite passing of the bill** and design a [regulatory framework to deal with cryptocurrencies](#).

Conclusion

- Crypto is just an example among lots of technological changes that are happening in the **current financial world** and now there's a chance to accept new challenges as well as to allow a **new integrated regulation for the securities market as well as for the currency markets**.
- It is a **new revolution in digital technology** which India cannot afford to miss but at the same time, it also cannot afford to lower its guard **regarding internal security and other related issues** as well.

Previous Year's Question (PYQ)

Q. With reference to “Blockchain Technology”, consider the following statements: (2020)

1. It is a public ledger that everyone can inspect, but which no single user controls.
2. The structure and design of blockchain is such that all the data in it are about cryptocurrency only.
3. Applications that depend on basic features of blockchain can be developed without anybody's permission.

Which of the statements given above is/are correct?

- (a) 1 only
- (b) 1 and 2 only
- (c) 2 only
- (d) 1 and 3 only

Ans: (d)

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