



UNDERSTANDING CRYPTO ASSETS AND REGULATORY APPROACH IN INDIA

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ABSTRACT

The underlying technology, blockchain, and even less about its core components, cryptography, have received less attention. On the other hand, officials around the world who are cracking down the spread of this mystery paint a stark picture. This research attempts to evaluate the frenzy of contradictory messages coming from a very fanatic community led by a billionaire, against almost total crackdown from regulators across the globe. While doing so, the research attempts to discuss the inherent benefits and disadvantages surrounding cryptocurrency, giving a comparative view of regulations around the globe and ultimately looking at the Indian scenario.

Keywords: Bitcoin, Blockchain, Cryptocurrency, Crypto assets, Initial Coin Offering (ICO).

INTRODUCTION

Contrary to what many might assume, the concept of “digital money” is not novel. In 1982, David Chaum who was concerned about the privacy of personal online payments authored a paper about a system of cryptographic protocols which developed the whole concept of “DigiCash”. DigiCash sought to protect the identity of users transacting money online by utilizing a system of public and private key cryptography.³ Further, Wake Forest J. aptly defines cryptocurrency as “the odd combination of a currency backed by no one and an investment involved in nothing.”⁴

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³ Chaum D., *Blind Signatures for Untraceable Payments*, SPRINGER BOSTON MA, 199-203 (1983). https://doi.org/10.1007/978-1-4757-0602-4_18.

⁴ Warren, Jonathan M, *A Too Convenient Transaction: Bitcoin and Its Further Regulation*, WAKE FOREST J. BUS. & INTELL. PROP. LAW, (2019).

As odd as it sounds, when a new paper authored by Satoshi Nakamoto on Bitcoin emerged, which catapulted cryptocurrencies into the limelight.⁵ Nakamoto was propelled after witnessing the fragility of fiat currency in the aftermath of the mortgage crisis.⁶ The inherent abuse of trust that the traditional currency systems bring across the globe highlighted the need for a novel worldwide money that could be “owned by anyone and spent anywhere.”⁷ It was envisioned as a ‘digital analogue to old fashioned gold’, fully ‘peer to peer, backed by no “trusted” third party’.

Bitcoin, one of the many ~2000 virtual currencies out there, operates on a peer-to-peer model using blockchain. Every Bitcoin is attached with one public identifier which is recorded on the blockchain and one private identifier enabling the holder of it to engage in transactions. Records of all transactions are maintained in the Ledger by way of Decentralized Ledger Technology (DLT) though they remain encrypted and hence the actual identities of transactors remain anonymous. This possesses challenges to old crimes like money laundering, terrorism etc. in newer formats. To curb these challenges, several countries around the globe have pre-emptively restricted the trade of crypto assets with most going the way of complete restriction on mining, trading, and all allied activities. With the exception of a handful, no country recognizes it as a legal tender and some of the leading economic blocs like the EU, BRICS, and NAFTA have severely restricted its usage.

At the time of authoring this paper, the value of 1 Bitcoin (BTC) was USD 58,079 and it is increasing day by day. Even the world’s largest automaker by value, Tesla, has started accepting payments in Bitcoins and the leading global

payments system, Visa, has started accepting payments using cryptocurrency.⁸ Meanwhile, Indian regulators are proposing a complete ban on cryptocurrency including mining. Draft Bill on “Banning of Cryptocurrency and Regulation of Official Digital Currency Bill, 2019” seeks to prohibit mining, holding, selling, trade, issuance, disposal or use of cryptocurrency in the country. The Bill makes mining, holding, selling, issuing, transferring or use of cryptocurrency punishable with a fine or imprisonment of up to 10 years, or both.

On the contrary, there stand countries like Japan and Switzerland where cryptocurrencies are registered and regulated as any other business. They are even accepted for tax payments.⁹ The research seeks to evaluate why there are two contradictory pictures drawn: a complete clamp down by countries like India, but fanaticism by leading corporates and consumers in addition to countries like Japan and Switzerland.

COMPARATIVE ANALYSIS: JAPAN, SWITZERLAND, INDIA

The entire debate so far pertains whether cryptocurrencies may be classified as currencies or assets or property or securities. This is a crucial identifier as it links to the next step forward in the sphere of crypto Regulations. With the help of the Draft Bill proposed by the Indian Government on the Banning and Regulation of Digital Currency and other definitions & classifications across the globe, with a focus on the Japanese and Swiss Regulations, one shall attempt to arrive at a consensus. Further, a common theme that runs across all the literature reviews the researchers analysed pertained to the criminal aspects of

5 Satoshi Nakamoto, *Bitcoin: A peer-to-peer electronic cash system*, BITCOIN, (2008) <https://bitcoin.org/bitcoin.pdf>. (Last visited Mar 31, 2022).

6 Robin Blackburn, *The Subprime Crisis*, NEW LEFT REVIEW 60, 64 (2008) <https://newleftreview.org/issues/II50/articles/robin-blackburn-the-subprime-crisis>, (Last visited Mar 31, 2022).

7 Crosby, M., Pattanayak, P., Verma, S. and Kalyanaraman, V. *Blockchain technology: Beyond Bitcoin*, APPLIED INNOVATION 2, 71, (2016) <https://j2-capital.com/wp-content/uploads/2017/11/AIR-2016-Blockchain.pdf> (Last visited Mar 31, 2022).

8 TESLA, <https://www.tesla.com/support/bitcoin> (Last visited Mar 31, 2022).

9 Bitcoin Suisse, *Canton Zug to accept cryptocurrencies for tax payment beginning in 2021* (2021) <https://www.bitcoinsuisse.com/news/canton-zug-accept-cryptocurrencies-for-tax-payment-in-2021> (Last visited Mar 31, 2022).

cryptocurrencies which can be classified threefold: Consumer Protection; Money Laundering; and miscellaneous crimes including but not restricted to child trafficking, human trafficking, cyber terrorism, etc.

The aim of this analysis is two-pronged: an attempt to arrive at a consensus regarding the classification of cryptographic currencies/properties/assets/securities; and a comparative look at the ways adopted by countries across the globe to curb criminal behaviour in the crypto sphere resulting in a proposed model of regulatory mechanism for the Indian regulators.

Crypto Regulation in Japan

Japanese legislators are quite far ahead when it comes to regulating the crypto sphere.¹⁰ This might be because of their rather technologically forward outlook or maybe because of the ignominious history of the former world's largest crypto exchange, the Japanese Company, Mt. Gox.¹¹ Irrespective, Japan has been the first country to have enacted laws defining crypto assets, mandates exchange providers to register, and have taken steps to counter money laundering issues.

Definition

The primary legislation concerning the crypto sphere is the **Payment Services Act (PSA)**. Recently, several revisions were made to the PSA which came into force on 1st May 2020, and now terms “**cryptocurrencies**” as “**crypto assets**” defining them as follows:

Crypto Asset (Article 2, PSA):

“Proprietary value that may be used to pay an unspecified person the price of any goods purchased or borrowed or any services provided and which may be sold to or purchased from an unspecified person (limited to that recorded on electronic devices or other objects by electronic means and excluding Japanese and other foreign currencies and

Currency Denominated Assets; the same applies in the following item) and that may be transferred using an electronic data processing system; or”

“Proprietary value that may be exchanged reciprocally for the proprietary value specified in the preceding item with an unspecified person and that may be transferred using an electronic data processing system.” (Article 2, PSA, 2020)

It is interesting to note that Japan has clearly demarcated between Crypto Assets which includes the likes of Bitcoin, Ethereum, etc., and Crypto Denominated Assets which would include all such assets denominated in domestic or internationally recognized currency and including the likes of gift cards or even a probable digital currency if issued by its central bank. The shift of terminology from crypto “currency” to crypto “asset” though brings no substantive change in legal interpretation but signals to the globe that the former classification does not reflect the true nature of the underlying technology.

The definition (“...transferred using an electronic data processing system”) brings forth the intangible nature of the asset. It also highlights (“...an unspecified person”) a key characteristic of crypto assets, the use of cryptographic technology, which makes the identity of the individuals opaque. Though not classified as currency, the definition attributes several of its characteristics: store of value and medium of exchange. Overall, this definition seems very balanced as it covers all the necessities of the underlying technology:

a. Anonymity: it provisions for anonymity created due to the fundamental cryptographic nature of the technology embracing it rather than criticizing or being blind to it.

b. Currency v. Assets: it recognizes certain key aspects of fiat currency exhibited by crypto related technologies but classifies them as assets instead. By doing so, it restricts the influence that the

10 O Jackson, *Japan's separate rules for crypto could be the answer*, INTERNATIONAL FINANCIAL LAW REVIEW (2018).

11 M Ishikaw, *Designing Virtual Currency Regulation in Japan: Lessons from the Mt Gox Case*, JOURNAL OF FINANCIAL REGULATION, 3(1), (125-131), (2017) <https://doi.org/10.1093/jfr/fjw015>. (Last visited Mar 31, 2022).

volatile nature of the technology might have had on the country's core financial and forex system.

c. Digital Representation of Value: the definition must be lauded for demarcating the digital representation of value created using cryptographic technology and other forms of digital representation of value like digital reward points, e-gift cards, etc.

Consumer Protection

PSA legalizes crypto businesses and thereby brings them under the purview of strict regulatory control. It starts by terming these exchanges as "Crypto Asset Exchange Services" and provides the following definition of such businesses:

- a. *"Sale or purchase of Crypto Assets, or the exchange of a Crypto Asset for another Crypto Asset;*
- b. *Intermediating, brokering or acting as an agent in respect of the activities listed in item (a);*
- c. *Management of customers Crypto Assets for the benefit of another person."*¹²

This definition also brings Crypto Asset Custody providers within the purview of Exchanges. They are required to provide extensive details and a clear structure of their organization in addition to having a minimum capital of 10 million JPY.

Next comes the issue of Initial Coin Offering (ICO) by way of which crypto assets are introduced in the markets. They are either issued by the Exchange itself or by the Exchange on behalf of the Issuer. ICO Rules (Rules for Selling New Crypto Assets) govern such arena and provide for the following regulations:

- i. *"Maintenance of a structure for review of a targeted business which raises funds via ICO;*

- ii. *Information disclosure of the token, the token issuer's purpose for funds, or the like;*
- iii. *Segregated management of funds (both fiat and Crypto Assets) raised by ICO;*
- iv. *Proper account processing and financial disclosure of funds raised by ICO;*
- v. *Safety assurance of the newly issued token, its blockchain, smart contract, wallet tool, and the like; and*
- vi. *Proper valuation of newly issued tokens."*¹³

These Regulations tackle the issues of fraudulent crypto assets floated in the market to unsuspecting investors and price jacking by issuers (Point vi).

Further, Financial Instruments and Exchanges Act (FIEA) prohibits unfair acts in the crypto sphere including market manipulation. Perhaps someone like Elon Musk would have been penalized under FIEA for using his influence over the populace and inflating Bitcoin prices while his company (Tesla) made a USD 1.5 billion investment in Bitcoin.¹⁴

Money Laundering

Act on Prevention of Transfer of Criminal Proceeds (APTCP) makes the Exchange providers liable to verify and disclose transaction records and maintain them for 7 years. Therefore, the National Diet (Japan's Bicameral Legislature) has a two-pronged target system to legalize, and regulate activities in the crypto sphere:

A. Legalization: Legalizing by adequately covering all aspects of crypto assets in its definition so that what is to be regulated is clear.

B. Regulation: Comprehensive yet precise regulations covering crucial aspects like ICOs, and Exchanges ensuring that their positive effect spills over to end-user behaviour and protection.

¹² Payment Services Act, 2019, No. 2 of 2019 (Sing.).

¹³ *Id.*

¹⁴ Al Root, *Bitcoin Hits \$60,000. Tesla's Crypto Bet Continues to Pay Off* (2021) BARRONS <https://www.barrons.com/articles/bitcoin-hits-60-000-teslas-crypto-bet-continues-to-pay-off-51615653236>. (Last visited Mar 31, 2022).

Crypto Regulation in Switzerland

Along with Swiss chocolates and watches, their banking sector is as emblematic. Known for its high regard for the privacy of investors, it comes as no surprise that Switzerland is keen on adopting cryptocurrencies with an aim to lead the market.¹⁵ As recently as in September 2020, the Swiss canton of Zug, regarded as the “Swiss Crypto Valley”, announced that it shall be accepting Bitcoin or Ethereum for tax payments in 2021.¹⁶

Definition

Switzerland, akin to Japan, classifies cryptocurrencies as “assets” and not legal tender. However, this is where the similarity ends because, unlike Japan, Switzerland still uses the term “cryptocurrency” and not “crypto asset”. Additionally, a further departure from Japanese practice is the absence of a statutory definition of cryptocurrency.

The Swiss “Federal Council report on virtual currencies in response to the Schwaab and Weibel postulates” published in June of 2014 defines Virtual Currencies as follows:

“A virtual currency is a digital representation of a value which can be traded on the Internet and although it takes on the role of money – it can be used as a means of payment for real goods and services – it is not accepted as legal tender anywhere. These currencies have their own denominations. They differ from e-money in that they are not based on a currency with legal tender status. Virtual currencies exist only as a digital code and therefore do not have a physical counterpart for example in the form of coins or notes. Given their tradability, virtual currencies should be classified as an asset.”¹⁷

However, a more analytical definition of cryptocurrencies by the Swiss authorities can be gauged by the categories into which The Swiss Financial Market Supervisory Authority (FINMA) classifies ICOs.

“Payment tokens are synonymous with cryptocurrencies and have no further functions or links to other development projects. Tokens may in some cases only develop the necessary functionality and become accepted as a means of payment over a period of time.

Utility tokens are tokens which are intended to provide digital access to an application or service.

Asset tokens represent assets such as participations in real physical underlying, companies, or earnings streams, or an entitlement to dividends or interest payments. In terms of their economic function, the tokens are analogous to equities, bonds or derivatives.”¹⁸

Payment tokens are considered “pure cryptocurrencies” and are “purely factual intangible assets”. Unlike its Japanese counterpart, the Swiss authorities do not go into the fundamentals of the technology. Rather, it takes applications on a case-by-case basis segregating them on the utility of the asset offered.

Consumer Protection

As discussed earlier, the chief complaints pertinent to the crypto sphere are inept Exchanges and ICOs. Switzerland, depending on the purpose of the tokens/coins to be issued, traded, and managed categorizes the nature of regulations to be imposed. As per the ICO Guidelines published by FINMA in 2018, regulations have three

15 Shanaev, S., Sharma, S., Ghimire, B. and Shuraeva, A. *Taming the blockchain beast? Regulatory implications for the cryptocurrency Market*, RESEARCH IN INTERNATIONAL BUSINESS AND FINANCE, 51 (2020). <https://doi.org/10.1016/j.ribaf.2019.101080>. (Last visited Mar 31, 2022).

16 *Supra* note 9.

17 Federal Council Report, 2014.

18 FINMA (2018), <https://www.finma.ch/en/news/2018/02/20180216-mm-ico-wegleitung/> (last visited Mar. 31, 2021).

distinctions, and each case is decided on individual merits:¹⁹

“Payment ICOs: For ICOs where the token is intended to function as a means of payment and can already be transferred, FINMA will require compliance with anti-money laundering regulations. FINMA will not, however, treat such tokens as securities.

Utility ICOs: These tokens do not qualify as securities only if their sole purpose is to confer digital access rights to an application or service and if the utility token can already be used in this way at the point of issue. If a utility token functions solely or partially as an investment in economic terms, FINMA will treat such tokens as securities (i.e. in the same way as asset tokens).

Asset ICOs: FINMA regards asset tokens as securities, which means that there are securities law requirements for trading in such tokens, as well as civil law requirements under the Swiss Code of Obligations (e.g. prospectus requirements).²⁰

Therefore, existing regulations are applied after categorizing cryptocurrencies. Bitcoin and Ether fall under Payment Tokens and are not classified as securities, though FINMA keeps an open mind and adds in its Guidelines that, *“If payment tokens were to be classified as securities through new case law or legislation, FINMA would accordingly revise its practice.”*²¹

However, under the DLT (Digital Ledger Technology) Draft Law a new category of license, “DLT Trading Venue”, is provisioned to allow “potential trading, clearing, settlement, custody of DLT Securities” by regulated and unregulated market applicants.

Money Laundering

Swiss Anti-Money Laundering Act keeps in check the issue of money laundering and is applicable to issuers of cryptocurrencies on the basis of their classification as “banking sector” and “non-banking sector” per the Act. The former is subject to heavy set of regulations and supervision while the latter are more self-regulated.

Switzerland’s approach to cryptocurrency is very accepting and emphasizing in the sense that the country wants its name to be as emblematic in the crypto industry as it is in Banking and to achieve this goal, it seeks to handle cases individually, shifting focus on every applicant. The Swiss believe that their existing structure, after minute modifications, is proficient enough to handle the cryptographic sphere when combined with an individualistic approach. They have brought in reforms by way of the DLT Act, but it is still very nascent to evaluate the Swiss approach on its basis.

Crypto Regulation in India

India’s dilemma over the right action for the crypto sphere has been very legitimate. An estimated 8 million Indians hold over USD 1.4 billion in crypto investments. That is a scanty 0.6% of our population.

On the other hand, the rate of adoption of cryptocurrencies in the country has been quite fast even as even a technologically forward and regulatory stable country like Japan has only 4% penetration. Further, the desire to understand the DLT and create a financial system decentralized from the one dictated by the US Dollar is every country’s ambition.²² More than 60 countries across the globe have initiated research on digital currency.

The present-day numbers contrasted with the future growth opportunities have largely

19 *Id.*

20 *Id.*

21 *Id.*

22 Enrique Dans, *China’s Digital Currency is About to Disrupt Money*, FORBES, (2021) <https://www.forbes.com/sites/enriquedans/2021/04/07/chinas-digital-currency-is-about-to-disrupt-money/?sh=247dfa901665>. (Last visited Mar 31, 2022).

driven the Indian approach: a complete ban on all cryptocurrencies BUT with a plan to launch an official digital currency.²³

The Draft bill on “Banning of Cryptocurrency and Regulation of Official Digital Currency Act, 2019” (hereinafter “The Bill”) seeks to do exactly what it spells like. Though the Bill never became an Act, this shall be our point of reference inside the Indian regulators’ minds as their stance has remained the same since 2019. This Bill has two components: banning and criminalization of trade/mining of cryptocurrencies; and introduction of the digital rupee.

Definition

The Bill defines cryptocurrency under Section 2 (1) (a) as follows:

“Cryptocurrency: The draft Bill defines cryptocurrency as any information, code, number or token, generated through cryptographic means or otherwise, which has a digital representation of value and has utility in a business activity, or acts as a store of value or a unit of account.”²⁴

It includes within its scope not just cryptocurrency or crypto assets but all forms of digital representations of value including a singular line of information that might be valuable digitally. This is draconian legislation arbitrarily classifying all digital forms of value under cryptocurrency. If the Bill were ever passed, it seems rather difficult that it would never end up before the Constitutional Bench of the Hon’ble Supreme Court. Perhaps this is the reason why it has not so far.

Further, the Bill not just seeks a ban on the trade of cryptocurrency but also a complete stop to its mining. What is interesting is how the Government would identify miners as besides the increased carbon footprint bitcoin mining leaves, there are no other identifiers. Even the ban on trading would result in behind-the-scenes trading by using Tor networks and the Government would be none the wiser.²⁵ Even if we consider the Government deploys quick and advanced detection systems to counter illegal trading, we have to acknowledge that Bitcoins can simply be stored in a bit-sized pen drive which can then be traded across borders and the Government would be none the wiser. Therefore, even though crypto assets are intangible, they can very well be smuggled by all tangible means.

Rationale

The rationale for the total ban behind India’s democratic government’s stance is not made available to the public. What is in the public domain is their analogy that cryptocurrency is a ‘Ponzi scheme’²⁶ and the Government’s belief that they are neither currency nor commodity nor securities, hence, are impossible to be regulated by SEBI and RBI but capable of disrupting the Indian economy.²⁷ Therefore, our analysis behind the Indian Government’s rationale would be two-pronged: to determine whether there is any substance to the Government’s claim of cryptocurrencies resemble Ponzi schemes; and whether it is really impossible to not regulate cryptocurrencies by the RBI and/or SEBI.

23 Aftab Ahmed, Nupur Anand, *India to propose cryptocurrency ban, penalising miners, traders*, REUTERS (2021) <https://www.reuters.com/article/uk-india-cryptocurrency-ban-idUSKBN2B60QP>. (Last visited Mar 31, 2022).

24 Draft Banning of Cryptocurrency & Regulation of Official Digital Currency Bill, 2019.

25 Dingleline, R., Mathewson, N. and Syverson, P. *Tor: The second-generation onion route*, Naval Research Lab Washington DC, (2004) <https://apps.dtic.mil/sti/citations/ADA465464.24> (Last visited Mar 31, 2022).

26 PTI, *Crypto currency is ‘ponzi scheme’, should be banned in India: Govt official*, BUSINESS STANDARD (2021). https://www.business-standard.com/article/pti-stories/crypto-currency-is-ponzi-scheme-should-be-banned-in-india-govt-official-119042600794_1.html. (Last visited Mar 31, 2022).

27 Anurag Thakur, *Cryptocurrencies are neither currency nor commodity; will bring bill soon*, BUSINESS TODAY (2021) (Mar. 31, 2021 11:56 PM), <https://www.businesstoday.in/current/corporate/cryptocurrencies-are-neither-currency-nor-commodity-will-bring-bill-soon-anurag-thakur/story/430725.html>. (Last visited Mar 31, 2022).

Ponzi Scheme

The government's analogy can prima facie be justified on the basis that as the number of investors increases, the value of Bitcoin increases since supply is predetermined (21 million) akin to a Ponzi scheme in which due to the addition of new investors, cash outflow remains consistent ensuring earlier investors are paid. However, the similarity is only surface level, and a comparative investigation is needed to check the Government's understanding of Ponzi schemes and cryptocurrencies.

The Securities regulatory arm SEBI shrieked when asked by the Hon'ble Supreme Court to show its initiatives for protecting investors from such schemes. SEBI denied having any regulatory control over it passing the buck to the Centre and State.²⁸ Even the chief financial institution in the country, RBI, nowhere defines Ponzi schemes though it does have a website (sachet.rbi.org.in) access is not secure.

Therefore, to understand the characteristics of Ponzi schemes, we look West at the US SEC's defining characteristics of it:

a. *"High returns with little or no risk. Every investment carries some degree of risk, and investments yielding higher returns typically involve more risk. Be highly suspicious of any guaranteed investment opportunity."*²⁹

Bitcoin never advertises guaranteed returns or even a safe investment opportunity. Rather, the asset has traditionally been known for its volatility rendering the first characteristic a moot point.

b. *"Overly consistent returns. Investments tend to go up and down over time. Be sceptical about an investment that regularly*

*generates positive returns regardless of overall market conditions."*³⁰

The same goes for consistent returns which have been absent from this ever-fluctuating crypto asset market.

c. *Unregistered investments. Ponzi schemes typically involve investments that are not registered with the SEC or with state regulators. Registration is important because it provides investors with access to information about the company's management, products, services, and finances.*

These issues are mimicked by crypto exchanges only in States wherein regulations are either absent or insufficient. As we have seen that when countries like Japan or Switzerland take initiative, they can combat these issues very successfully.

The underlying technology, cryptography, may perhaps be confounding for end users but certainly, this does not turn crypto assets into Ponzi schemes.

Besides the surface-level similarity we saw, crypto assets do not exhibit characteristics of a Ponzi scheme. However, the concern of Ponzi schemes being run in the name of crypto assets is a real threat³¹ but one that falls squarely on lack of awareness and not the inherent nature of the technology. It is the failure to regulate crypto exchanges and license firms dealing in any advertised form of crypto business because of which Ponzi schemes are being run as crypto assets.

Regulatory Framework

The then Union Minister of Finance, Mr. Anurag Thakur, in response to a question in the

28 Krishnadas Rajagopal, *Ponzi Schemes not in our Regulatory Ambit: SEBI to Court*, BUSINESS LINE (2021). <https://www.thehindubusinessline.com/markets/ponzi-schemes-not-in-our-regulatory-ambit-sebi-to-apex-court/article8960440.ece>. (Last visited Mar 31, 2022).

29 *Supra* note 26.

30 *Id.*

31 Mike Orcutt, *Millions of people fell for crypto-Ponzi schemes in 2019*. MIT TECHNOLOGY REVIEW. (2020) <https://www.technologyreview.com/2020/01/30/275964/cryptocurrency-ponzi-scams-chainalysis/> (Last visited Mar 31, 2022).

Lok Sabha pertinent to cryptocurrency regulation, remarked, “Regulatory bodies like RBI and Sebi, etc also don’t have a legal framework to directly regulate cryptocurrencies as they are neither currencies nor assets, securities, or commodities issued by an identifiable user. The existing laws are inadequate to deal with the subject.” Such remarks are in contrast to the Government’s previous actions. In 2018, the RBI via a Circular directed all the entities under its purview to stop dealing in virtual currencies in any way or form.³² The Hon’ble Court held that RBI does have the inherent authority to regulate cryptocurrencies as it considered it to be currency coming under the category of “other instruments” as per Section 2 (h) of the FEMA Act, 1999. Since RBI was unable to show any damage suffered by the entities it regulated due to virtual currencies, the Hon’ble Court struck down the Circular on grounds of it being violative of Article 19 (1) (g).

It is evident that the Government’s reasoning for the inadequate regulatory framework and expectation of damage to State financial entities does not stand on solid grounds. Rather, the conclusion that the Government is trying to digress from any material discussion on the actual regulation of crypto assets does not seem implausible. After careful analysis of the Indian Government’s rationale behind their inclination for a total ban of all crypto-related commercial activities, we can safely conclude that none of them are substantive enough to justify it. Hence, the question is why the Indian Government afraid of existing crypto assets.

Perhaps it is due to the perceived difficulty in framing laws and their actual robust implementation that makes the Government shy away from doing all this work for something in which only 0.6% of the population is invested. Or maybe,

the Government sees existing cryptocurrencies as competition to its plans of launching its own Central Bank Digital Currency (CBDC).³³ The latter would not be unheard-of as China has also adopted a similar approach.³⁴

PROPOSED REGULATORY APPROACH

India has one of the highest cash to GDP ratio.³⁵ The introduction of a regulated crypto assets market and CBDC could just be the push needed to change this. India should adopt a hybrid approach when it comes to a regulatory framework surrounding crypto assets. It must take inspiration from its Japanese and Swiss counterparts to help frame its regulations.

Definition

An accurate is imperative as it sets the scope and extent of regulations. As discussed earlier, the proposed definition of cryptocurrency in the Draft Bill is far too broad for it to ever stand the test of constitutionality.

We must take inspiration from Article 2 of the Japanese legislation, the Payment Services Act which provides for a comprehensive, exhaustive yet succinct definition.

A proposed definition is as follows:

Crypto Assets:

“Digital representation of value, stored digitally or otherwise, generated by means of cryptography, used for payment of goods/ services to an unspecified person including body corporate and/or as a means of investment or trade and which may be transferred using an electronic data processing system.”

This definition has the following key elements:

- a. a. Crypto Asset

32 RBI, Prohibition on dealing in Virtual Currencies (VCs), Reserve Bank of India (2018).

33 Rajesh Bansal, *Govt can ban Bitcoin but for ‘digital rupee’ to succeed, India has to do a lot*, THE PRINT (2021). <https://theprint.in/opinion/govt-can-ban-bitcoin-but-for-digital-rupee-to-succeed-india-has-to-do-a-lot/608542/>. (Last visited Mar 31, 2022).

34 Supra note 25.

35 Abhishek Waghmare, *Cash-to-GDP ratio could hit 14-15%, the highest since independence*, (Oct. 6, 2020 10:25 PM), BUSINESS STANDARD (2020) https://www.business-standard.com/article/economy-policy/cash-to-gdp-ratio-could-hit-14-15-the-highest-since-independence-120100600876_1.html. (Last visited Mar 31, 2022).

- b. b. Digital representation of value
- c. d. Generated by means of Cryptography
- d. e. Payment/Investment/Trade
- e. f. Unspecified Person/Body Corporate

Regulatory Mechanism

After providing an exhaustive yet succinct definition, we must have a robust regulatory mechanism governing crypto businesses including exchanges. This will allow us to curb criminal activities and anti-consumer behaviours.

For a robust regulatory mechanism, we must look at our Swiss counterpart, specifically the ICO Guidelines published by FINMA as earlier discussed. This shall allow us to categorize the set of regulations to be imposed depending upon the purpose of the crypto asset offered.

Since the approach is individualistic, it will bring proper scrutiny ensuring only market-friendly businesses are allowed to float. The approach is time-consuming, and the Indian regulators are not known to be swift, to begin with, however, it is the safe way to ensure a transparent working structure keeping in mind consumer protection. In turn, this would put a burden on Government staff to get acquainted with the nitty gritty of crypto assets but that shall be a small cost to bear.

Further, we must also look at the Japanese FIEA Regulations and their provisions pertinent to curbing market manipulation of any kind. This will not only serve to protect investors from traditional forms of market manipulative practices but also manipulation by way of new age media like the curious case of Elon Musk's tweets and resulting variations in Bitcoin's valuation.³⁶

This is crucial because the value of crypto assets is largely driven by public perception which in turn is very fragile. Lastly, the concerns about money laundering stemming from the anonymous nature of the technology can be kept in check by making the Exchanges and allied crypto businesses liable to verify and disclose all transactions. These businesses could in turn impose certain mandatory conditions upon users in the form of KYC documents and/or bank account linkage.

CONCLUSION AND SUGGESTIONS

Looking into the definitions provided by Japan, crypto assets seem to be a better classification. We have come a long way from DigiCash, the bankrupt digital currency of 1982. The crypto assets market has crossed over \$2.0 trillion in value out of which Bitcoin itself accounts for more than 50% of it.³⁷ However, the Indian reason for shying away from regulating crypto assets seems rather like an after-thought.

When Satoshi Nakamoto authored the white paper leading the crypto revolution in 2008, he was disillusioned by the repeated breach of trust of the belief that institutions would never debase the currency. He envisioned an alternative to the traditional currency, one which was peer-to-peer, could be owned by anyone and spent anywhere, detached from any central regulatory authority.

After more than 12 years since its launch, and with more than 100 million users of all forms of crypto assets,³⁸ Satoshi's apprehensions about traditional global financial institutions are well echoed. As Bitcoin and other forms of crypto assets are increasingly finding themselves in conversations at legislative houses several are

36 Ron Shevlin, *How Elon Musk Moves The Price Of Bitcoin With His Twitter Activity*, FORBES (2021). <https://www.forbes.com/sites/ronshevlin/2021/02/21/how-elon-musk-moves-the-price-of-bitcoin-with-his-twitter-activity/?sh=4b12762e5d27>. (Last visited Mar 31, 2022).

37 Kumar Gandharv, *Industry Reactions to Cryptocurrency Market Hitting \$2 Trillion Mark*, AIM (2021). <https://analyticsindiamag.com/industry-reactions-to-cryptocurrency-market-hitting-2-trillion-mark/>. (Last visited Mar 31, 2022).

38 Harry Robertson, *The estimated number of global crypto users has passed 100 million - and boomers are now getting drawn to bitcoin too, reports find*, BUSINESS INSIDER (2021), <https://www.businessinsider.in/stock-market/news/the-estimated-number-of-global-crypto-users-has-passed-100-million-and-boomers-are-now-getting-drawn-to-bitcoin-too-reports-find/articleshow/81210262.cms#:~:text=More%20than%20100%20million%20people,according%20to%20two%20separate%20reports>. (Last visited Mar 31, 2022).

confounded by the likelihood of the existence of an asset that was meant to be unregulated.

However, with a deeper understanding of the inherent cryptographic technology and the Distributed Ledger System it works on, as discussed in our introduction, we find that legislation can never regulate the fundamental working of crypto assets. Rather, regulations are for ensuring transparency, maintaining accountability, and creating awareness amongst consumers. They are not meant for the underlying technology but for the people who transact in them.

Canvassing existing literature on this subject four key elements can be highlighted: a global consensus on the need for regulations; a majoritarian view on avoiding a complete ban; embracing the underlying Distributed Ledger Technology by nations and official digital currency; and a lack of consensus on the definition of cryptocurrency or crypto asset. However, after looking at the leading countries in the crypto regulatory sphere (Japan and Switzerland) we find a growing shift towards the term crypto asset rather than cryptocurrency or virtual currency. The reasoning is based upon the fundamental nature of the technology itself i.e., cryptography.

The term Virtual Currency (VC) can be attributed to even the official digital currency by the States or perhaps any form of digital representation of value. The term 'cryptocurrency' can also be misconstrued by implying that Bitcoin, Ethereum, etc. are State sponsored since the term 'currency' has traditionally been used for legal tenders. Thus, the term 'crypto asset' is more appropriate as it covers the inherent nature of the technology unlike VC and is in no way indicative of being State sponsored unlike cryptocurrency. The comparative analysis also brought forth a regulatory mechanism depending upon the utility of the crypto asset to be offered. These regulations centred around regulating the exchanges, ensuring their structure is transparent, their modus operandi is established, and through them, their customers can be held accountable.

Further, the endeavour is to understand the Indian Government's inclination towards a complete ban on any commercial crypto-related activity bringing forth the inadequacy in its reasoning.

The research compared crypto assets with Ponzi schemes and found out that their similarity is only superficial. Unlike Ponzi schemes, crypto assets never guarantee any stable returns, nor promise any risk-free investment opportunity debunking the Government's assertion that cryptocurrency was Ponzi scheme.

The research also looked into the Government's remarks that our existing institutions like the RBI and SEBI lack the inherent jurisdiction to control cryptocurrencies. The Hon'ble Supreme Court in the case of Internet and Mobile Association of India v. Reserve Bank of India, as earlier discussed, long debunked this Governmental claim. Ultimately, this research recommends that a regulatory approach and an exhaustive, yet succinct definition should be adopted by the Indian Government to embrace the technology rather than shun it. The definition provided by this research covers the key aspects pertaining to the inherent nature of crypto assets, their intangible yet tangible nature, and their anonymity, while putting forth a strict separation from other forms of digital representation of value.

The research also recommends a regulatory mechanism much like the one followed in Switzerland in which crypto businesses are licensed on a case-by-case basis. Though this approach is time-consuming and requires technical know-how on part of regulators, it seems the sole way to have a grip over the crypto commercial sphere. More than 8 million Indians have invested over an estimated USD 1.2 billion in a market that is completely unregulated, largely unknown, and greatly puzzling over a very short period of time. It is despite these barriers, that citizens have placed their trust in this asset. The Government needs to step up and protect the citizens' fundamental rights under Article 19 (1) (g) rather than placing a pre-emptive ban based on the apprehension of damage in the absence of any real example.