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THE LEGALITY OF CRYPTOCURRENCY IN INDIA

Authored By-Alden Vas, Anaita Vas & Aayan Mohapatra

Raising The Proper Questions

Bitcoin's rise to prominence in 2008 marked the beginning of the cryptocurrency world. The crypto scenery has rampantly spread since, accordingly presently more than 20,000 cryptocurrencies are being merchandising all over the globe¹. In reality, India currently has the largest concentration of cryptocurrency investors globally². The Indian government has established a cryptocurrency fee, but has made clear that this does not constitute legalisation³. In order to encourage more substantial investments, market participants are pressing for greater clarity from governments on the subject of cryptocurrency trading and investing. Nevertheless, the fundamental difficulty associated with such a requirement is difficult from both a mechanical and a regulatory standpoint.

Is It Possible To Legally Propose Legalizing/Recognizing All Digital Currencies?

Numerous digital currencies are currently in use, each of which is theoretically predicated on the decentralised blockchain system. Any individual has the ability to create, generate, and/or disseminate a cryptocurrency. The problem emerges, for the purpose of discussion, whether or not all cryptocurrencies/coins, digital money, and/or Non-Fungible Tokens ("NFTs") will be

¹Hayed, A. (2022, July 8). 10 Important Cryptocurrencies Other Than Bitcoin. Investopedia; www.investopedia.com. <https://www.investopedia.com/tech/most-important-cryptocurrencies-other-than-bitcoin/#:~:text=One%20reason%20for%20this%20is,communities%20of%20backers%20and%20investor>

²Livemint. (2021, October 13). India has highest number of crypto owners in the world at 10.07 crore: report | Mint. Mint; www.livemint.com. <https://www.livemint.com/market/cryptocurrency/india-has-highest-number-of-crypto-owners-in-the-world-at-10-07-crore-report-11634110396397.html>

³ET Online. (2022, February 12). FM Sitharaman says taxing cryptos doesn't mean it has been legalised: report | ET. ET; <https://economictimes.indiatimes.com/news/economy/policy/fm-sitharaman-says-taxing-cryptos-doesnt-mean-it-has-been-legalised/articleshow/89496281.cms>

recognized/legalized/regulated if they were to be constituted a legal currency. If this were to happen, it would immediately flood the with around 20,000 more legitimate bids. More cryptocurrencies (especially Bitcoin) are built on uncensorable blockchain systems, therefore even if just a handful of the most popular ones are acknowledged, anybody would still be capable of creating lawful currencies. To rephrase, everyone in the entire globe may generate bitcoins right now, and if they were legally acknowledged, anyone around the globe could theoretically generate legitimate currencies from anywhere in the planet. Considering this alternative is completely out of the question.

Is There Any Way To Legally Acknowledge Any Of The Most Popular Cryptocurrencies?

Undoubtedly, a call to universally recognise, legalise, and regulate cryptocurrencies will not suffice. In 2021, El Salvador became the first country to recognise Bitcoin as a legal tender. El Salvador was the first nation to officially accept Bitcoin as legitimate money in 2021. It might be asserted that governments have enough room for constitutional manoeuvre to legalize Bitcoin, Ethereum, Dogecoin, and other significant cryptocurrencies in this framework. In addition, certain currencies may be eligible for official status based on objective criteria such as unpredictability, quantity of trading, enterprise value, invention authentication, and so on.

Legislators can do what is needed to make this recommendation a reality because it was tried and true in 2021's Intermediary Guidelines, in which the three leading social media platforms (YouTube, Twitter, and Facebook) were designated as "prominent social media middlemen" and made subject to a new set of rules. The key source of disagreement here is not the features of identification, but the core technology enabling the cryptocurrency economy, therefore acknowledging a few significant currencies might not be a great answer either.

Given the foregoing, the pertinent concerns are not whether or not cryptocurrency trade would be "permitted", alternatively, whether it will be recognized by the government. Instead, patterns in taxes, advertising approval, certification of consolidated crypto-exchanges, and the severity of reprisals (if any) on the crypto-ecosystem conceal the true issues and practical needs. In this perspective, this article clarifies some of the ethical and pragmatic grey areas that arise when trying to make sense of the vast and varied crypto environment.

⁴Virtual Currencies | Internal Revenue Service. (n.d.). Virtual Currencies | Internal Revenue Service; www.irs.gov. Retrieved August 23, 2022, from <https://www.irs.gov/businesses/small-businesses-self-employed/virtual-currencies>

⁵Gautam, V. (2022, February 12). Countries Where Cryptocurrency Is Taxed. India Times; www.indiatimes.com. <https://www.indiatimes.com/worth/investment/countries-where-crypto-is-taxed-561760.html>

An International Look At Cryptocurrency Taxes

All legislative, governmental, and administrative activity concerning cryptocurrency is dynamic, adaptable, and sometimes reactionary. The United States has taxed cryptocurrency transactions and ownership despite officially acknowledging any currency as lawful cash⁴. In contrast, the United Kingdom treats cryptocurrency as equity capital and taxes their trade, payment for merchandise and services, and donation in accordance with the country's pre-existing tax brackets.

All legislative, governmental, and administrative activity concerning cryptocurrency is dynamic, adaptable, and sometimes reactionary. The United States has taxed cryptocurrency transactions and ownership despite officially acknowledging any currency as lawful cash⁴. In contrast, the United Kingdom treats cryptocurrency as equity capital and taxes their trade, payment for merchandise and services, and donation in accordance with the country's pre-existing tax brackets. Both Canada and Germany have shown a greater welcoming of cryptocurrency use⁵. To Canada, it is a technology platform subject to taxation only upon sales, whereas to Germany it is personal currency subject to taxation upon exchange or sale within one year. The majority of nations have decided it is appropriate to regulate cryptocurrency consumers, provide a regulated certification, and implement self-disclosure methods instead of recognising certain currencies as statutory cash.

From the planned tax framework and its implementation, it is clear that the Indian government views cryptocurrencies with some trepidation. Profits generated through the sale or exchange of digital currencies or other similar virtual resources will be subject to a 30% rate of taxation under revisions to the Income Tax Act 1961 ("IT Act") envisaged in the Finance Bill, 2022 ("2022 Bill"). The concept of "online virtual currency" was adopted in the 2022 Budget through the 2022 Bill, initiating the review regime for all NFTs and cryptocurrencies.

The Reserve Bank Of India's Virtual Rupee And Cryptocurrency

The government reserves the right to include or exclude certain cryptocurrency and/or NFT in its modern interpretation. In order to prevent the Reserve Bank of India's (RBI) anticipated virtual currency, the Digital Rupee or Central Bank Digital Currency ("CBDC"), from being taxable or regulated under the 2022 Bill, a preservation clause has been included.

Distinctions Involving Permissioned And Permissionless Blockchains Are At The Heart Of The Conceptual Divide Separating Cryptocurrencies And Central Bank Digital Currency

The planned CBDC differs significantly from independent cryptocurrencies, even if they do have official support. In contrast to the uncensorable blockchain systems utilised by most major cryptocurrencies like Dogecoin and Shiba, the CBDC would be built on a permissioned blockchain.

Because it is a decentralized system, anybody with access to the internet may join and make contributions ('mine' currencies by evolution of internet) to a blockchain platform. Therefore, anyone with access to suitable mining hardware may create Bitcoins. In contrast, only the Central Government as well as other entities authorised by the Government will have the competence to produce, tune the quantity, and/or manage the availability of CBDC due to the nature of permissioned blockchain systems and CBDC in particular. In order to limit individuals from constructing or modifying networks to the blockchain, blockchain systems incorporate an access-control layer within the blockchain network. The Government of India is employing this technology to safeguard their virtual money, the Rupee, and has found it to be particularly useful for financial institutions, ministries, and other institutions utilizing blockchain solutions.

Central Bank Digital Currency Shall Be A Stablecoin

A further key distinction involving CBDC and commercial cryptocurrencies is that, in contrast to their nominal valued counterparts, CBDC will be supported by the government. It looks that the CBDC Virtual Currency will operate as a Stablecoin whose worth is tethered to the worth of the Rupee, i.e., the equivalent of 1 INR/Rupee. Stablecoins are digital currencies whose worth is anchored to another asset (typically a national fiat money) but yet retaining the portability and convenience of cryptocurrency⁶. Binance USD ("BUSD"), for example, is a virtual cryptocurrency with a worth of one USD equal to 1 US dollar. The long-term goal is for CBDC to flow into the same pool as other valuation commodities, such as cash. It is a viable solution for the Government as cash-related management and circulation problems are expensive to tackle. According to Finance Minister Mrs. Nirmala Sitharaman, "Implementation of CBDC would provide a major boost to digital economy... [and] would also contribute to an increasingly efficient and less expensive currency management platform," the government is looking forward to CBDC as a simple, quick, and affordable alternative⁷.

⁶@CNBCTV18Live. (2021, December 30). *What Are Stablecoins, How They Work, How To Buy Them, And Other Questions Answered*. Cnbctv18.Com; www.cnbctv18.com. <https://www.cnbctv18.com/cryptocurrency/what-are-stablecoins-how-they-work-how-to-buy-them-and-other-questions-answered-11970862.htm>

The Technical Challenges Of Outlawing Virtual Currency

One of the goals of the current draught of the Cryptocurrency and Regulation of Official Digital Currency Bill, 2021 ("draught Bill") is to outlaw the use of unregistered cryptocurrencies within India. On the other hand, it is important to realise that the basic tenet of the bitcoin network is its autonomous nature.

Since there is no one controlling body over the business, it is impossible to prohibit or govern it at its foundation. Whatever seems to have been intended from the draught Bill is the ability to control or outlaw usage, possession, dealings, and so on. The government is in favour of outlawing cryptocurrencies for four primary reasons: the high degree of price fluctuations, the danger to purchasers from hacking attempts and Ponzi ploys, the effect on energy usage (a single Bitcoin deal uses enough electricity to supply approximately 380 Indian homes for one day), and its prospective use in criminality, such as financial fraud, profiteering, etc⁸.

Decentralized Atmosphere

The Indian government is aware of the technical challenges of outlawing cryptocurrencies and is still considering taking that path. This will need a resolute team, policy analysis, enforcement procedures, legal upgrades, and so on. We have mechanical roadblocks due to the decentralised environment described herein. To simplify, one could engage in cryptocurrency transactions via any of the following three channels:

- *Centralized Exchanges*: To engage in cryptocurrency transactions on a Central Exchange, individuals must provide personally identifiable information, connect a bank account, and properly comply with Know Your Customer (KYC) rules. As far as cryptocurrency exchanges go, this is one of the more respectable options. Using a Central Exchange, customers may instantly convert their bank-linked fiat cash into bitcoin. Using a Central Exchange, customers may instantly convert their bank-linked fiat cash into bitcoin. To put it succinctly, the government is always cognizant of one's bitcoin assets and activities using this manner. Nowadays, various domestic Central Exchanges such as CoinDCX, WazirX, and others have sprung up. Due to the obvious openness and adherence provided by Central Exchanges, it will also be feasible to impose tax on trades.

⁷ Thomas, K. S. (2022, February). *The promise of digital rupee and the subsequent collateral damage - The Week*. The Week; www.theweek.in. <https://www.theweek.in/theweek/business/2022/02/19/the-promise-of-digital-rupee-and-the-subsequent-collateral-damage.html>

- *Decentralized Exchanges:* However, several Decentralized Exchanges (such as Uniswap, Metamask, pancakeswap, etc.) do not need users to comply with KYC regulations or even reveal their identify or private details in order to open an account. No financial institution is required to begin dealing on Decentralized Exchanges. When a user signs up for an account, the system will randomly generate an online wallet (distinct to each user) consisting of a string of numbers and letters that will be utilized for sending and receiving digital currencies. In Decentralized Exchanges, customers' anonymity is ensured, and oftentimes, not even the system itself is aware of who is doing what trades. Cryptocurrency traders on Decentralized Exchanges often buy and sell cryptocurrencies employing stablecoins obtained either via peer-to-peer (P2P) transactions, centralised exchanges, or the Decentralized Exchanges themselves.
- *Peer – To – Peer Exchanges:* A quick internet search will show that there are numerous cryptocurrency networks organised on Telegram and other chat webpages for direct p2p payments in cryptocurrencies using Decentralized Exchanges electronic addresses/wallet. Cryptocurrency holders have the option of making a direct transfer for fiat money, alternative digital currencies, or other valued assets. Cryptocurrency dealers can use P2P trading as a recruiting tool to exchange their assets on Decentralized Exchanges.

Conclusion

In the event of a prohibition on commercial cryptocurrencies, its enforcement would be complicated by the fact that e - wallets generated on Decentralized Exchanges and containing cryptocurrencies cannot be readily tracked. Even while it's possible to block access to DEX platforms within the nation, doing business in personal cryptocurrency wallets is also unlawful. Customers' cell phones and other gadgets might be impounded as way of an inquiry, but whether requiring someone accused to give credentials or online wallets addresses might constitute self-incrimination remains a contentious ethical topic. It is conceivable that it'll create a whole new body of law from scratch. As a result, law enforcement agencies would need to broaden their understanding of the topic, recruit additional moral specialists, and build investigative and crime-detection tools. In the most basic sense, the worth of money, goods, and belongings is based on a well-ordered fiction that characterizes our complex lives. From the business partnership to civil rights, all are elements of our ordered architectural imaginal world, as Yuval Noah Harari points out in *Sapiens: A Brief History of Humankind*. Why then should the speculative value of cryptocurrencies be stigmatised when it fluctuates just like any other asset? Additionally, just as with any other made-up actuality, cryptocurrencies must be handled with a healthy dose of caution.

The country's concerns about cryptocurrency are warranted. Who exactly controls the environment and which coins? What is the exact location of such servers? Is it true that terrorists and other criminals are using cryptocurrency to launder money from India? Even though there are regular, massive transactions, the government has not used this as a factor in deciding whether to outlaw the practise. Understanding that privacy is the foundation of the crypto economy, it is lucky or sad that openness is now the most important factor to safeguard. As of the time this article was written, cryptocurrencies are not outlawed in India. However, it would be fascinating to observe what the government decides to do in the future with regard to private cryptocurrencies.

⁸ Vaishnav, A. (2019, September). *Ban on cryptocurrencies: Understanding the proposed legislation*. Ban on Cryptocurrencies: Understanding the Proposed Legislation; prsindia.org. <https://prsindia.org/theprsblog/ban-cryptocurrencies-understanding-proposed-legislation>