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**End of the Road for Private Cryptocurrencies in India – the Proposed Ban**

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With more and more investors being attracted to invest in virtual currencies with their astonishing highs and painful lows, the cloud of confusion with regard to recognition and regulation of such currencies under Indian laws loomed. The nuances and legal status of virtual currencies under Indian laws including various directions issued by the Reserve Bank of India (“**RBI**”) on virtual currencies have been extensively discussed in our previous articles<sup>1,2</sup>.

After several advisories of the RBI, which cautioned investors against risks of virtual currencies but stopped short of declaring them as illegal, subsequent raids reportedly conducted by the Enforcement Directorate against operators of trading platforms of virtual currencies, the notices issued by the Income Tax department to crack down the unregulated rein of Bitcoins, it seems that it may be the end of the road for private cryptocurrencies in India. The Inter-Ministerial Committee (“**Committee**”) constituted with the mandate of studying various issues related to virtual currencies, examining the policy and legal framework and proposing specific action to be taken in this regard, has issued its report<sup>3</sup> (“**Report**”) and recommended the banning of private cryptocurrencies in India. Along with the Report, the Committee has also submitted a draft bill titled ‘Banning of Cryptocurrency & Regulation of Official Digital Currency Bill, 2019’ (“**Bill**”).

Some of the reasons for prohibition of cryptocurrency given by the Committee in its Report include:

- cryptocurrencies having been created by private enterprises do not reflect the sovereign guarantee of value and are distinguishable from fiat currency;



- there is no underlying intrinsic value in private cryptocurrencies and they lack all the attributes of a fiat currency. Furthermore, the market potential of cryptocurrency is subject to technological and behavioural changes rendering them subject to severe fluctuation in their prices;
- extreme fluctuations and volatility in price demonstrated by cryptocurrency in comparison to fiat currency and non-applicability of the law of one price in the cryptocurrency market, i.e. different exchanges transacting at different rates, deprive cryptocurrency of the essential characteristics of money;
- they are decentralised networks with no central authority;
- irreversibility of cryptocurrency transactions;
- protection of consumers from fraud (example: GainBitcoin scam);
- wide usage of virtual currencies may pose a problem for the central bank as regulation of the money supply may be affected due to the decentralised nature of cryptocurrency which in turn restricts the central banks ability to stabilise the economy;
- greater anonymity of virtual currencies can lead money laundering and terrorist financing activities<sup>4</sup>;
- review of global test practises also shows that private cryptocurrencies have not been recognised as legal tender in any jurisdiction.

#### Overview of the Bill

Considering the above factors, the Bill proposes for a blanket prohibition on any transaction related to cryptocurrency in India with stringent penal provisions.

“Cryptocurrency” has been defined exhaustively to mean “*any information or code or number or token not being part of **any Official Digital Currency**, generated through cryptographic means or otherwise, providing a digital representation of value which is exchanged with or without consideration, with the promise or representation of having inherent value in any business activity which may involve risk of loss or an expectation of profits or income, or functions as a store of value or a unit of account and includes its use in any financial transaction or investment, but not limited to, investment schemes*”.

The Bill proposes that no person shall be allowed to “*mine, generate, hold, sell, deal in, issue, transfer, dispose of or use Cryptocurrency*” in India and Cryptocurrency, whether directly or indirectly, will not be used as a legal tender or currency in India. Use of Cryptocurrency has also been prohibited for the following activities:

- as a payment system, whether authorised under the Payments and Settlement Systems Act, or otherwise;
- buying or selling or storing Cryptocurrency;
- provision of Cryptocurrency related services to consumers or investors which includes registering, trading, settling, clearing or other services;
- trading of Cryptocurrency with Indian currency or any foreign currency;

- issue of Cryptocurrency related financial products;
- as a basis of credit;
- issue cryptocurrency as a means of raising funds; and/or
- as a means for investment.

Transitional Period: The Bill has provided for a transitional period of ninety (90) days from the date of commencement of the Bill, to Cryptocurrency holders to make a declaration of their Cryptocurrency and dispose of the same within the transitional period.

Penal Provisions: The Bill has also proposed stringent penal action against offenders and any contravention of the provisions of the Bill may carry a term of imprisonment ranging from 1 to 10 years and/or fine which may range from the higher of three times the loss/harm caused by the person or gains made by the person. In case the loss cannot be reasonably determined, the fine will be as per the prescribed limit provided in the Bill depending upon the relevant provision contravened.

#### **Official Digital Currency**

Interestingly, the Committee in its draft Bill has provided an option to the Central Government to create its own virtual currency and recognise foreign digital currency with the inclusion of the terms “Digital Rupee” and “Official Digital Currency”.

“Digital Rupee” has been defined as “*currency issued digitally by the Reserve Bank and approved by the Central Government to be legal tender*”. “Official Digital Currency” has been defined as Digital Rupee or the foreign digital currency recognised by the RBI by way of notification as foreign currency.

Also, the Bill has clarified that the proposed legislation shall not apply to any person using technology or processes underlying any Cryptocurrency for the purpose of experiment or research, including imparting of instructions to pupils provided that no Cryptocurrency is used for making or receiving payment in such activity. Further, the proposed legislation shall not apply to the use of Distributed Ledger Technology (“**DLT**”, which is the underlying technology for the Bitcoin) for creating a network for delivery of any financial or other services or for creating value, without involving any use of cryptocurrency, in any form whatsoever, for making or receiving payment.

The Committee, in its Report, has also recommended to the Department of Economic Affairs to take necessary measures for facilitating the use of DLT and to various regulators such as the Securities Exchange Board of India, Insurance Regulatory and Development Authority etc. to consider and explore DLT in their fields.

#### **Conclusion**

Given the statements made by the earlier Union Finance Minister in the Budget Speech of 2018 to the effect that “*The Government does not consider crypto-currencies legal tender or coin and will take all measures to eliminate use of these cryptoassets in financing illegitimate activities or as part of the payment system. The Government will explore use of block chain technology proactively for ushering in digital economy.*”, there is a strong likelihood that the draft Bill would be accepted by the Central Government, bringing an end to increasingly popular yet significantly risky alternate investment route for Indian investors.

Endnotes:

[1] <http://www.mondaq.com/india/x/583670/fin+tech/Legal+Status+Of+Virtual+CurrenciesCryptocurrencies+In+India>

[2] <http://www.mondaq.com/india/x/608424/fin+tech/Future+Of+Virtual+Currencies+In+India>

[3] <https://dea.gov.in/sites/default/files/Approved%20and%20Signed%20Report%20and%20Bill%20of%20IMC%20on%20VCs%2028%20Feb%202019.pdf>

[4] Virtual Currencies: Guidance for a Risk-Based Approach report by the Financial Action Task Force.

Feedback

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