Regulating cryptocurrencies

(Mains GS 2 & 3 : Government policies and interventions for development in various sectors and issues arising out of their design and implementation & Science and Technology- developments and their applications and effects in everyday life.)

Context:

Eight years after the RBI issued its first advisory cautioning holders of virtual currencies about the potential financial and security risks, and two years after drafting a Bill to ban cryptocurrencies, the Government is set to introduce the Cryptocurrency and Regulation of Official Digital Currency Bill, 2021 in Parliament this winter session which officially proscribe such currencies.

Nature of cryptocurrencies:

- Crypto-assets or cryptocurrencies are being embraced by many but they are under fire mostly by the officialdom in many parts of the world.
- It is primarily because the transaction process using cryptocurrencies is so secure that only a money transfer can be seen and nothing can be known about the sender and the recipient.
- These decentralised assets, with no central bank controlling them, may therefore be used for 'hawala', which is a trust-based system of transferring money quickly in a parallel arrangement avoiding the traditional banking system and escaping the due tax.
- Anonymity and privacy are the underlying characteristics as well as the potential danger of cryptocurrencies.

- The risks investors and consumers face in dealing with these so-called currencies, given that they are neither ‘a store of value nor are they a medium of exchange’, and the ostensible threat they pose to financial stability, are also key factors.

Jump in investment:

- Despite Centre and the RBI’s deep disquiet, cryptocurrencies have seen an exponential jump in investment in virtual currencies, especially after the Supreme Court last year struck down an RBI notification barring financial entities from facilitating customer transactions related to virtual currencies.
- Industry estimates peg cryptocurrency holdings in India at about ₹40,000 crore, held by about 15 million investors, and advertising trends show an upsurge in ads promoting brands associated with investment in virtual currencies.
- The original crypto inventors wanted it to emerge as a form of money that could compete with fiat money but that hasn’t happened. Meanwhile, cryptos have emerged as an avenue for investment and any form of investment needs to be regulated.

Regulate cryptocurrencies:

- The risks associated with cryptocurrencies includes their potential use for money-laundering and financing of illegal activities
- The pandemic has accentuated the global embrace of all things digital and investment in the technologies enabling cryptocurrencies including blockchain, appear to be no different.
- Canada, Japan and Thailand permit the use of virtual currencies as a payment method, with some jurisdictions regulating them as a digital asset, and others as a commodity.
- Canada and the U.S. closely monitor virtual currency activity to ensure they do not run afoul of laws on financial crimes, with the former also earning tax revenue on transactions.
- Thus India should try to regulate cryptocurrencies to some extent and also tax Bitcoin gains in their own ways.

No regulation is perfect:

- A regulated market will certainly keep illegal activities under control to some extent as most of the common investors will comply with the rules and substantial money will be gained from taxes.
- But it is not at all possible to completely stop hawala, drug or terror funding by crypto with such regulations as crypto investors need not necessarily invest through crypto platforms, that they can move to peer-to-peer exchanges (P2P) exchanges located outside India.

- Recently, Prime Minister Narendra Modi said cryptocurrencies must not fall into the “wrong hands and spoil our youth” and urged all democratic nations to come together and ensure that things like these do not happen.

  Of course, unless all nations work together, the genie cannot be completely controlled and in real word no regulation is perfect but not having regulation because it’s not perfect is hardly an excuse.

Conclusion:

The Indian government should follow the most practical approach that would involve not limiting investors from investing in cryptos and at the same time creating “a framework in which to regulate them and any financial products related to them".