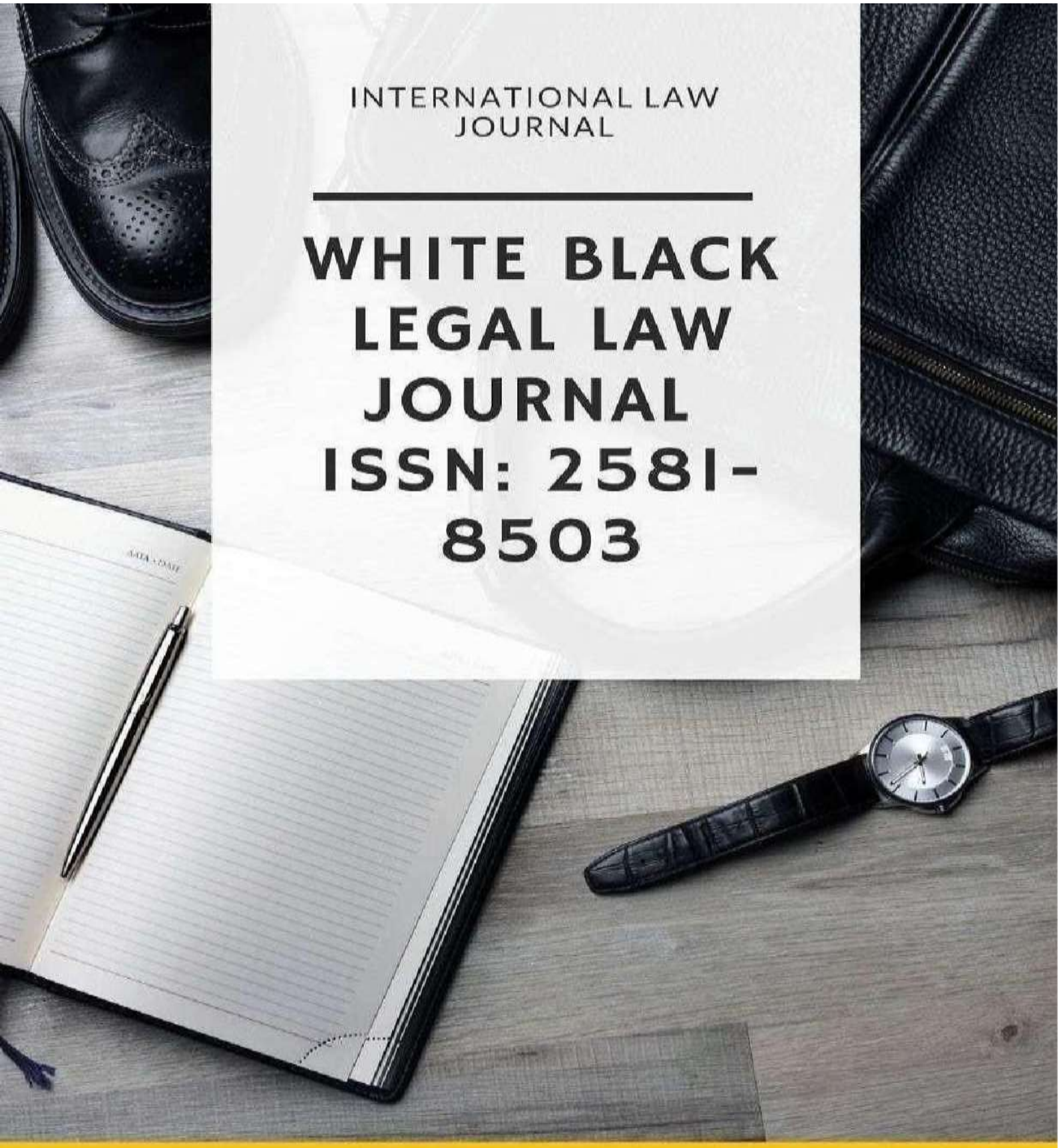

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REGULATORY FRAMEWORK FOR CRYPTOCURRENCY IN INDIA.

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Index

1. ABSTRACT

Cryptocurrencies have become an influential force that disrupts the traditional financial frameworks, forcing jurisdictions all over the world to reevaluate the sufficiency of their regulatory frameworks. The legal status regarding cryptocurrency in India is still preliminary and uncoordinated; despite being taxed and subjected to anti-money laundering requirements as a Virtual Digital Asset (VDA), there is still no specific legal framework within the sector. In this paper, the authors will follow the timeline of the evolution of the regulatory path of the Republic of India, starting with the 2018 ban on banking services to cryptocurrency organizations by the Reserve Bank of India and its overturn by the Supreme Court in Internet and Mobile Association of India v. RBI to this day, relies on indirect regulatory instruments. Based on a comparative study of other jurisdictions, among them the Payment Services Act of Japan, the licensing regime of Singapore, the MiCA framework of the European Union, the property-based approach of the United Kingdom, and the enforcement-led system of the United States, the paper assesses the degree to which the current position of India balances innovation with the protection of investors and systemic stability. The results reveal that there are long-term issues associated with volatility, jurisdictional uncertainty, technology complexity, and illicit financial risks. The article claims that India needs a logically consistent, technology-neutral and future-oriented framework of regulation that would provide India with responsible growth and international competitiveness.

2. Key Words

1. Cryptocurrencies
   Digital, decentralized currencies that operate on blockchain technology without central bank control.
2. Traditional financial frameworks
   Conventional banking and monetary systems regulated by the state.
3. Regulatory frameworks
   Legal and policy structures created to supervise financial or technological activities.
4. Virtual Digital Asset (VDA)
   A classification under Indian law that includes cryptocurrencies and subjects them to tax and anti-money laundering rules.
5. Anti-money laundering (AML)
   Laws and rules designed to prevent criminals from disguising illegally obtained money.

6. Reserve Bank of India (RBI)

   India's central bank, responsible for monetary policy and financial regulation.

7. Internet and Mobile Association of India v. RBI

   A 2020 Supreme Court ruling that struck down RBI's 2018 ban on banking services for crypto businesses.

8. Indirect regulatory instruments

   Regulation done through taxation, compliance requirements, and advisories rather than a dedicated crypto law.

9. Payment Services Act (Japan)

   Japan's law regulating crypto exchanges as "crypto asset" service providers.

10. MiCA (European Union)

    A comprehensive EU regulation governing crypto assets, service providers, and consumer protection.

11. Licensing regime (Singapore)

    A structured system requiring crypto businesses to obtain government approval and follow strict AML rules.

12. Property-based approach (United Kingdom)

    UK classification treating cryptocurrency as property, mainly for taxation and legal rights.

13. Enforcement-led system (United States)

    A model where regulators like the SEC act through investigations, lawsuits, and existing laws instead of a dedicated crypto statute.

14. Investor protection

    Safeguards to ensure investors are not misled, exploited, or exposed to undue risk.

15. Systemic stability

    Maintaining the stability of the financial system and preventing risks that could cause large-scale disruption.

16. Jurisdictional uncertainty

    Legal confusion about which country's laws apply to borderless digital assets.

17. Technological complexity

    Challenges arising from the advanced and rapidly evolving nature of blockchain and crypto technology.

18. Illicit financial risks

Threats involving illegal activity such as fraud, hacking, terror financing, and money laundering.

19. Technology-neutral framework

    Regulation focused on principles and risks, not tied to any specific technology.

20. Future-oriented regulation

    Laws designed to accommodate rapid innovation and evolving digital financial systems.

3. INTRODUCTION

3.1 What is cryptocurrency?

Cryptocurrency is a medium of exchange that utilizes blockchain technology and cryptography for recording transactions and for control of the issuance of new units. As one subgroup of alternative digital currencies, the first decentralized cryptocurrency was Bitcoin, created in 2009. Cryptocurrency emerged in India for the first time around 2009 in the form of Bitcoin. It was in the year 2010 that the first commercial transaction occurred, followed by the first Cryptocurrency exchange in the year 2013.

3.2 Why is it important to regulate it?

Cryptocurrency serves to transform our conceptions surrounding money, investment, and technology; however, without supervision, it can quickly become a hotspot for scams, volatility, and abuse. Supervision protects individuals and companies so they can safely interact with digital assets because there are systems to safeguard their interests. Regulation cultivates trust, responsibility, and `transparency—hallmarks of a developed financial system—while still permitting creativity to prosper. It's not about control for control's sake; it's about risk management in an environment where advancements help the majority and not just an exclusive group.

3.3 Brief background of the legal status in India

In India, cryptocurrency comes under the category of Virtual Digital Asset, which permits individuals to buy, sell, and hold cryptocurrency. It operates as not legal tender, meaning it cannot be used to transact like the rupee. The cryptocurrency tax policy is clear as well: gains are taxed at thirty percent, 1% TDS is charged on some transactions, and crypto exchanges have to comply with strict KYC and anti money laundering regulations. This approach fosters

innovation while still keeping some control and responsibility within the system, balancing innovation and regulation.

3.4 Research problem

As the recognition of cryptocurrencies as an accepted payment mechanism and a globally recognized store of wealth continues to expand, India's regulatory response places cryptocurrencies in the classification of Virtual Digital Assets, while not categorizing them as lawful tender. This raises some pertinent questions as to whether this regulatory approach is a type of innovation, consumer protection, or approach to market stabilization. In comparison, other jurisdictions, like Japan, Switzerland, and now in the European Union, are cautiously implementing positive regulatory regimes that can bring structure to organizations in the crypto ecosystem and provide a balance for regulatory benefits with the development of a particular technology.

3.5 Objectives of the study

This study will provide comparisons of India's regulatory model with these other jurisdictions and provide a measure of whether the VDA classification is a suitable regulatory response to the legal, economic, and consumer aspects of the crypto evolution. This study aims to explore how India’s current approach to regulating cryptocurrency—treating it as a digital asset but not as official money—impacts investors, market growth, and legal clarity. It will look at how this compares to countries like Japan, Switzerland, and those in the European Union, where rules are more clearly defined and often more supportive of innovation. The goal is to understand whether India’s cautious stance is helping or holding back progress, and to identify lessons from other countries that could guide India toward a more balanced and forward looking policy.

3.6 Scope

This study examines how cryptocurrency is legally regulated in India, the technical classification of cryptocurrency as an asset instead of its designation as official currency, and the consequences of this classification of cryptocurrency on the confidence of investors, their willingness to participate in the market, and ultimately on the success and growth of crypto related businesses. The study includes an analysis of specific regulated models in Japan, Switzerland, and countries in the European Union to compare the models in India, and includes ideas on legal recognition of cryptocurrency, consumer protection, and supporting innovation.

By looking at these views from both domestic and international perspectives, the hope is to better understand how India sits on these dimensions and what it can learn about how to develop a more effective.

4. Understanding Cryptocurrency: Legally & Technically

4.1 Nature of cryptocurrency: currency, asset, or commodity?

Cryptocurrency protocols are, by design, not conducive to being classified traditionally as one kind of single category; indeed, they are simultaneously a currency, asset, and commodity. As a currency, such a cryptocurrency is a decentralized medium of exchange and a peer to peer transaction system, and it works as such without governmental fiat or other intermediaries, possibly back to Bitcoin's design. As an asset, a user can hold the cryptocurrency as a store of value and use it as investment options, as many users appear to hold the cryptocurrency as speculation or for a corpus to diversify into, much like stocks or outside investments into real estate. As a commodity, many cryptocurrencies possess many of the qualities of scarce supply (as an example, Bitcoin has a capped supply), fungibility, and price discovery through supply and demand based exchanges in the form of multiple Types of exchanges. Crypto is bought and sold based on prevailing market forces, trading on spot and derivatives type exchanges worldwide; thus, some economists and scholars consider it a commodity similar to gold or oil. Different emphasis is applied by different jurisdictions; the U.S. Commodity Futures Trading Commission characterizes Bitcoin and Ethereum as commodity types; the EU Heighten Regulatory regime MICA distinguishes between payment tokens, utility tokens, and asset referenced tokens; some jurisdictions consider certain tokens as being characteristically securities. In a general sense, cryptocurrency protocols are hybrid type currencies cryptocurrency's characteristic nature is determined less by the actual characteristics of the underlying protocols or codes and more on what functional view is adopted, pluralistically in customary use and its standing in Law and/or regulation Hybrid options believed to possessing non contestable alternative natures in equivalency to money, property goods, and properties of transferable goods; which may enable the use of hybrid value type characteristics.

4.2 Blockchain technology and how it works

Blockchain is a kind of technology that works based on decentralization, not trusting any one entity is one of the types of digital technology that allows anyone to set up their data transparently and securely. It stores data in blocks. Each data block contains some transactions,

a timestamp, and a unique code called a hash that makes it an unchanging entry. Every block is linked to the previous one via its hash, hence creating a continuous chain of records. When a new transaction takes place, it is submitted to the network of computers called nodes, either through an application or by accessing a publicly available peer to peer network, and consensus mechanisms, such as proof of work or proof of stake, are resorted to in order to validate ownership of said data. Once the transaction has been accepted by most of the nodes or miners, it is attached to the blockchain forever. This also implies that in order to alter a record, one must validate every single block thereafter, an act that is computationally infeasible. That is to say: a block cannot be altered if a majority of nodes have accepted it, and this is with the possible involvement of thousands of nodes distributed worldwide, and no single party has any authority on such transactions. Decentralization affords the blocking of distributed.

4.3 Global legal definitions and classifications

Countries around the world classify and define cryptocurrencies in different ways according to how they are utilized or what risks the regulators want to manage. In the United States, some regulators treat Bitcoin and some other cryptocurrencies as commodities, while others treat some tokens as securities because they look like investment contracts. In the new European Union regulations on crypto assets, they classify crypto assets into payment tokens, utility tokens, and asset referenced tokens, each with its own regulations. In Japan, they refer to them as crypto assets and regulate exchanges as part of the country's Payment Services Act, while countries like Singapore view them as digital payment tokens, which require licensing for service providers offering a digital payment token service. Not surprisingly, these differences show that there is not one single definition that is unified around the world, and ultimately, legal identity associated with having a cryptocurrency will vary by a country's laws, how the token actually functions, and whether the primary purpose of the token is as a money, investment, or some kind of tradable good.

5. Legal status of cryptocurrency in India

5.1 Historical Background

The journey of cryptocurrency in India has had many ups and downs. It started in the early 2010s, when Bitcoin was still a word circulated in private online forums by a small number of technology enthusiasts. At that time, there were no regulations, and trading felt too good to be true. All of the hype did not stop the trials of scams, frauds, and money laundering from taking

place. In 2018, the Reserve Bank of India issued a ruling that prohibited banks from interacting with crypto businesses, and this ruling caused crypto trading activity to drop to practically nothing and caused many exchanges to close. This was the painfully unsatisfying state of crypto until the banking ban was lifted by the Supreme Court in 2020 and renewing hopes and excitement in the market. Since then, the government has yet to issue an outright ban on cryptocurrencies, but they have tried to level the playing field by imposing certain tax rules and anti money laundering guidelines, which have regulated a lot of the developing activity surrounding the marketplace and have made it more costly to deal with crypto. These heavy taxes, specifically a flat thirty percent tax on gains and one percent on crypto transactions, justified the majority of trading moving offshore. Thankfully, the conversation is not banning provisions but rather regulations, while the Indian government tries to balance the need for innovation in a digital based finance environment with the current stability of the economy, leaving the case of crypto open but under observation.

RBI Circular of 2018

In April 2018, the Reserve Bank of India issued a ruling that required all regulated entities, which include banks or payment businesses, to stop providing services to consumers and businesses involved in cryptocurrency. The ruling essentially severed the banking system and prohibited crypto exchanges from carrying out deposits or withdrawals in Indian Rupees. The RBI stated that it was necessary to remove the links to cryptocurrencies to protect the financial system, citing areas of risk including fraud, money laundering, and market volatility.

Crypto Exchanges' Problems

The exchanges in India experienced serious operating problems as a result of the RBI's ruling. By eliminating any linkage to banking channels for both deposits and withdrawals, each exchange was forced to make decisions on whether or not to cease operations altogether or to merely serve crypto to crypto models. Even after the Supreme Court ruling struck down the RBI ban in early 2020, the exchanges in India continued to experience problems. Induced uncertainties of regulation, on the part of the government, newly imposed tax policies, strict anti money laundering policies, and a flat taxation of 30 percent of gains have all contributed to lower trading volumes in exchanges. Furthermore, the costs surrounding regulations, along with retention and replacement of talent, and the competition presented by globally recognized exchanges, will force more Indian traders to migrate to global exchanges that represent fewer

costs and restrictions.

5.2 Landmark Case Law: Internet and Mobile Association of India v. RBI (2020)

Brief Facts

On April 6, 2018, the Reserve Bank of India (RBI) issued a circular directing all entities regulated by it, such as banks, payment system providers, and non banking financial companies, to stop providing services to individuals or businesses involved in cryptocurrency trading. Although the circular did not ban cryptocurrencies directly, it cut off their link to the formal financial system, making it impossible for exchanges to operate normally. The Internet and Mobile Association of India (IMAI), representing several crypto exchanges, filed a writ petition in the Supreme Court, challenging the circular as unconstitutional.

Legal Issues

Whether the RBI had the power to restrict banking services to cryptocurrency related businesses.

Whether the circular violated Article 19(1)(g) of the Constitution, which guarantees the right to carry on trade or business, subject to reasonable restrictions.

Whether the restriction was proportionate to the risks posed by cryptocurrencies.

Arguments by IMAI

Cryptocurrencies were not banned under any Indian law.

The RBI's circular was arbitrary and disproportionate because there was no evidence of actual harm to the financial system caused by crypto exchanges.

The restriction effectively shut down a lawful business, infringing on the fundamental right to trade.

Arguments by RBI

RBI has a statutory duty to protect the stability and integrity of India's financial system.

Cryptocurrencies pose serious risks, including money laundering, terror financing, consumer protection issues, and volatility.

A preventive approach was justified, given global regulatory concerns.

Supreme Court's Reasoning

The Court acknowledged that RBI has wide powers to regulate currency, payment systems, and the financial sector. However, it applied the doctrine of proportionality and found that the circular imposed a severe restriction on the right to trade without sufficient evidence of harm. Since cryptocurrencies were not illegal in India, completely cutting off banking services was excessive.

Legal Implications

The judgment established that regulatory measures affecting fundamental rights must be backed by evidence and be proportionate to the threat. It restored banking access to crypto exchanges, reviving the industry.

Aftermath

The decision boosted the crypto industry, but without a clear legislative framework, uncertainty persisted as the government explored dedicated cryptocurrency laws.

5.3 Current Legal Status

Current Legal Status of Cryptocurrency in India

Taxation and VDA Definition under the Finance Act, 2022

The Finance Act, 2022, formally introduced the term Virtual Digital Asset (VDA) into the Income Tax Act. VDAs include cryptocurrencies, non fungible tokens, and similar digital assets. The Act imposes a flat 30 percent tax on all gains from the transfer of VDAs, regardless of the holding period, and does not allow deductions for expenses other than the cost of acquisition. Losses from VDAs cannot be set off against other income or carried forward. In addition, a one percent tax deducted at source (TDS) is applied on transactions above a specified threshold.

Government's Evolving Stance

The Indian government has shifted from considering an outright ban on private cryptocurrencies to adopting a cautious regulatory approach. While the Reserve Bank of India continues to warn about risks such as volatility and financial instability, the government has emphasised the need for global cooperation in regulating digital assets. It has also brought VDA transactions under the Prevention of Money Laundering Act to enhance compliance and transparency.

Absence of Comprehensive Regulation

Despite taxation measures and anti money laundering rules, India does not yet have a dedicated cryptocurrency law. This leaves the sector operating under fragmented rules, creating uncertainty for investors, businesses, and regulators.

6. International Regulatory Approaches (Comparative Overview)

6.1 USA (SEC/IRS)

In the United States, there are various agencies charged with regulating cryptocurrencies. The major federal players are the SEC and the IRS. The SEC views cryptocurrencies and tokens as equivalent to securities if they can satisfy the Howey Test: If an investor has an investment intent that they will profit from the efforts of others. Because the Howey Test is factually based, the SEC has launched many tokens and exchanges that it feels are selling unregistered securities. The IRS, on the other hand, has determined that cryptocurrencies are property. This means that every crypto transaction (each sale or trade) (and even purchasing goods and services using cryptocurrencies) will generate a taxable event that will create capital gains taxes. All gains and losses must be reported. Failure to include gains or losses can have penalties assessed against a taxpayer by the IRS. The U.S. is implementing a response to cryptocurrencies based on enforcement and utilizing the current rules (i.e., securities laws and tax laws) as opposed to a collection of statutes. This involves ongoing confusion around jurisdiction, compliance, potentially, and potentially needing clear and consistent laws provided.

6.2 UK

In the UK, cryptocurrency and crypto activities are not legally recognized as legal tender, but laws for legal systems and taxation classify it as a type of property. The FCA regulates some crypto asset activity, focusing on AML and Counter Terrorist Financing obligations. All crypto asset businesses have to register with the FCA and complete KYC due diligence. The FCA has prohibited the sale of crypto derivatives and exchange traded notes to retail consumers because of the risks associated with these products. In respect of taxation, HMRC considers holding cryptocurrency as simply an asset, and disposals made by an individual, so that means gain from a sale or exchange, will incur capital gains tax upon the individual. If disposed of in the lifecycle of the business, it will incur corporate tax on profits. If payment is made to a person in cryptocurrency, HMRC will treat it as taxable income at the time of receipt. The regulatory

approach in the UK is rules based and aims to protect consumers, ensure market integrity, and reduce financial crime, whilst allowing space for different innovations, such as the regulatory sandbox initiated by the FCA. In the UK is still no comprehensive, specific single/stand alone law covering the whole of the spectrum of crypto or crypto activities, and policies change and evolve with global developments.

6.3 EU (MICA Regulation)

The European Union has launched its Markets in Crypto Assets (MiCA) Regulation, creating Europe's first fully comprehensive legal framework governing cryptocurrencies at the EU level and its Member States. MiCA is designed to harmonize the rules relating to the issuance, trading, and service provision of crypto assets and reduce regulatory divergence across EU Member States. MiCA divides crypto assets into three interrelated categories: asset referenced tokens, e money tokens, and utility tokens, outlining applicable requirements. MiCA includes licensing for crypto asset service providers ("CASPs"), consumer protection, operational transparency, and compliance with anti money laundering regulations. MiCA includes requirements for white papers for new token issuances, detailing the project, risks, and rights of holders. To the extent possible, MiCA seeks to harmonise rules in order to foster innovation, while balancing financial stability and investor protection. The MiCA regulation is a more proactive and structured approach when compared to jurisdictions based on existing laws. Although decentralised finance (DeFi) and non fungible tokens (NFTs) are not specifically covered in the MiCA, the Framework allows for updates as the market matures, making it one of the most forward looking regulatory frameworks in the world.

6.4 Japan, Singapore (progressive models)

Japan defines cryptocurrencies as "crypto assets" within its Payment Services Act. Crypto exchanges must register with the Financial Services Agency (FSA). Crypto exchanges must comply with onerous requirements related to protecting, safeguarding, and securing customer assets, security systems, and Know Your Customer (KYC) rules. Subsequent to the Mt. Gox hacking incident, Japan has enhanced regulations as it relates to custody services, requiring customer funds to be held separately from company assets. Crypto trading remains legal, and a clearer guide has provided the opportunity for Japan to have a relatively transparent and stable marketplace.

A similar innovative approach is taken in Singapore with a parallel definition of cryptocurrencies as "digital payment tokens" under its Payment Services Act. Singapore licenses service providers through the Monetary Authority of Singapore (MAS); the MAS also prescribes the anti money laundering and counter terrorist financing (AML/CFT) requirements on service providers. Singapore regulates innovation with regulatory sandboxes, which deal with emerging blockchain and crypto solutions under looser requirements and oversight, allowing entities to explore innovative solutions. Tax treatment here is advantageous as there are no capital gains taxes, while income from crypto related activities is treated as business income.

Japan and Singapore provide examples of how regulation can be provided to cryptocurrency whilst protecting consumers and financial stability, and promoting the growth and adoption of technology.

6.5 Comparative analysis with India's stance

Japan considers cryptocurrencies to be "crypto assets" subject to regulatory oversight under the Payment Services Act. The regulations have stringent licensing, custody, and security controls that undoubtedly provide the market clarity to achieve stable growth. Singapore also considers cryptocurrencies to be "digital payment tokens," providing a regulatory umbrella under its Payment Services Act while ensuring strong compliance but also incentivising innovation through measures like regulatory sandboxes and tax incentives. The MiCA regulation, which the EU passed in late 2022, provides a comprehensive regulatory framework that is uniform across all member states, classifies assets, and regulates service providers, while also providing comprehensive consumer protection. The UK accepts cryptocurrencies to be property, ensures anti money laundering protections apply, and taxes them like any other asset, without a single dedicated law. In the USA, regulation strikes an inconsistent patchwork of approaches, with the SEC considering some tokens to be securities, the IRS taxing them as property, enforcement dependent on existing laws that often do not fit crypto, and differing approaches in different states. Unlike many other jurisdictions discussed here, India has no dedicated statute for cryptocurrencies, but it relies on taxation, regulations laying out anti money laundering obligations, and central bank advisories cautioning against investment in cryptocurrencies, this approach favors financial stability, but inhibits innovation and pushes much of the active industry activity offshore, unlike the clearer and more progressive tax and

regulatory frameworks from these other jurisdictions.

7. Proposed Legislation and Policy Debates

India's proposed draft law of "Banning of Cryptocurrency and Regulation of Official Digital Currency Bill, 2019" would have been unprecedented in that it would have entirely banned all private cryptocurrencies in India (e.g., Bitcoin, Ethereum, etc.). The Bill sought to ban, basically, all activities with respect to cryptocurrency, to currency (including Bitcoin) activities that involve mining, buying, selling, trading, and even holding; and anyone who violated the provisions of this Bill exposed to the potential of hefty fines and/or imprisonment. The bill's stated purpose was to protect India's financial system, combat money laundering and terror financing, and protect consumers from the inherent volatility of markets and potential fraud. The bill also aimed to grant the Reserve Bank of India exclusive authority to issue a digital rupee as the only legal digital currency of India. While the government saw the ban as a way to maintain control over a monetary system, critics noted that a ban would stifle innovation by preventing the blockchain and fintech sectors one of the fastest growing in India from developing, potentially harming economic growth. Critics argued that rather than banning India should engage in regulation of the sector to allow for rapid technological growth while accounting for potential risks. While the bill was never enacted, it resulted in a debate about the policy issues and laid the groundwork for India's current regulatory and oversight approach rather than a ban approach. The Indian government wants to implement a Central Bank Digital Currency (CBDC), popularly known as the Digital Rupee. The vision is to establish a digital currency that will essentially mirror other successful state backed digital money initiatives around the world, including China. The Digital Rupee will serve as a sovereign currency issued by the Reserve Bank of India (RBI). It will function like any paper rupee, except it will exist entirely electronically. Whereas the government considers private cryptocurrencies to be speculative and risky, theoretically, a CBDC would be regulated, stable, and also receive the full trust of the state. The introduction of a CBDC fits into India's desire to modernize payment systems, reduce reliance on cash, improve efficiency for cross border payments, and ultimately regain greater control over monetary policy. There has also been a desire to use blockchain or similar technologies in a way that disassociates it from the volatile world of decentralized crypto assets. This approach is consistent with Central Banks internationally, particularly China, which has already launched its digital yuan and several other jurisdictions exploring central bank–issued tokens. In India, the Digital Rupee is seen as a safe alternative to private

digital currencies, aligning with the RBI's desires to increase digital payments while upholding monetary sovereignty. The Digital Rupee is meant to operate alongside physical currency, which will provide citizens and businesses with an official government resumed digital currency option that is fast, secure, and less expensive for digital transactions.

8. Critical Analysis of India's Approach

8.1 Is India's regulatory stance vague or evolving?

The prospects for cryptocurrencies in India are inaccurate, but still very uncertain. While the central government and Reserve Bank of India (RBI) have both stated concerns concerning the risks of private cryptocurrencies and offered to create comprehensive legislation either to regulate or ban their use, no such legislation has been enacted; for the time being, attempts at regulating cryptocurrencies have depended on ad hoc frameworks, issuer policy statements, and taxation rules – such as the introduction of a 30% tax on all virtual digital assets in 2022. The climate of uncertainty has resulted in a foggy and ambiguous environment for businesses, investors, and users. While the absence of a blanket ban indicates that India may be heading towards a regulated framework, the absence of any true specific rules suggests that there is still space for ambiguity, unpredictable regulation, and changing policies. Globally, we have seen clearly delineated regulations increase investor confidence and aid in attracting foreign direct investments and responsible innovations. However, if India maintains ambiguity in regulation and does not create some form of defined regulated framework that values risk mitigation while continuing to promote innovation as part of the national digital economy strategy, there is a real risk for India to fall behind in the global digital economy, especially as we see other jurisdictions that are developing structured, transparent, and forward looking crypto policies. Leaving stakeholders out in the cold and in a period of inactivity will only slow down the future development of the ecosystem and reduce the capacity for environmental sustainability.

8.2 Impact on innovation and startups

The uncertainty and restrictive nature of India's stance on cryptocurrency have caused very serious challenges to blockchain and Web3 innovation and start ups. Escalating tax burdens, lack of clarity, and paranoia of prohibitions in the future have been dissuading investment, whether domestic or foreign. As a result, many crypto and blockchain start ups have decided to establish themselves in more hospitable countries (e.g., Singapore or Dubai), taking away the CPU and capital talent. This trend is hindering India in fulfilling its aspirations to occupy

the world's top spot in emerging technologies. Furthermore, without clearly defined guidelines, it is very difficult for entrepreneurs to plan the next phases of business strategy or attract long term funding, as these investors have concerns, as they are afraid of imminent regulatory crackdowns. The government speaks to the possibilities of blockchain and its potential beyond cryptocurrencies, but its approach to the regulation of crypto related projects limits the scope for those who wish to experiment or scale. Start ups whose product offerings include payment solutions, decentralized finance (DeFi), and NFT marketplaces are seeing the greatest challenges. The irony here is that India has ample tech talent and one of the fastest growing digital economies in the world it is a question of policy stability to maintain momentum. A moderate regulatory framework could break the shackles of innovation, allow for responsible and sustainable growth, while allowing India to be regarded as a destination for blockchain based solutions without compromising security or accountability.

8.3 Concerns of investor protection

The theme of investor protection is at the forefront of discussions related to India's cryptocurrency policy. Policymakers worry that without monitoring and regulation, retail investors could fall victim to scams, anti social behavior, fraudulent initial coin offerings (ICOs), and wild price volatility. Cryptocurrencies are a speculative asset class where prices can rise or fall, with little to no investigation or regulation, tens of thousands of dollars in a matter of mere hours, leaving investors with large losses. Reports of hacking, phishing, and rug pulling associated with cryptocurrencies in global markets underline those concerns. Without formal dispute resolution policies, however, investors have little recourse for dealing with fraud or exchange collapses. Unfortunately, the current approach mostly tax structure in legislation and informal restrictive practices does not do much to proactively protect investors. In effect, it simply pushes any trading activities to unexamined and offshore platforms that present even more risk. A substantial shift would be to actually license exchanges, monitor them, implement transparency measures for projects, and provide information and educational tools that generate public awareness of risks associated with crypto. Other nations, such as Japan, have demonstrated that areas and rules to comply with, combined with ongoing support services from stakeholders, can live together in harmony and foster widespread investment. Without safeguards in place, India's best interests remain to retain their current stance and enforce this slight legislative response, risk demonstrating how little they care for that which India professes to be a world leader in, whilst failing to shoulders the increased investment which is possible

in a regulated manner and serves all vested stakeholders as demonstrated in a data driven analysis.

8.4 Financial inclusion vs. risks (terror funding, scams, volatility)

Cryptocurrencies could boost financial inclusion in India through the provision of digital payment access to unbanked populations, affordable cross border payments, and the provision of access to services in decentralized finance. This could provide transparency and access to those in underserved, rural communities through blockchain systems that are beyond the traditional banking system. But the legitimate concerns cause the government to hesitate. The anonymity of crypto can be abused for illicit purposes such as terror financing and the laundering of money, and the volatility of cryptocurrencies can wipe out neighborhoods of financially vulnerable groups in speculation, resulting in loss of savings and loss of hope. Scams and frauds have a disproportionate effect on individuals who lack the digital literacy to distinguish legitimate offerings. Politically, the challenge is to strike the right equilibrium the benefits of blockchain can be encouraging for inclusion, but in doing so, states need to develop robust anti money laundering (AML) and counter terrorist financing frameworks (CTF). An outright ban on cryptocurrencies would forfeit the benefits based potential of increasing social and economic activity among marginalized groups, but free and unregulated use would increase the risk of illicit behaviors. A middle ground that includes robust KYC processes, real time transaction monitoring, and the use of awareness campaigns, onerous penalties for misuse could position India in a better position to discover the inclusive potential of digital assets without tax losses to the benefit of national security or findings for financial stability, is essential to a sustainable transition in the future.

9. Challenges in Regulating Cryptocurrency

9.1 Jurisdictional issues

Cryptocurrencies have decentralized structures, making regulation difficult, especially when the users are in different jurisdictions. While a transaction might be made between users in different countries, the law in the country of the platform would have no ability to reach an arbitrator in the jurisdiction where the crypto transaction takes place. Even if one country decided to ban or regulate crypto, interested users would like find other pathways to access the market by using exchanges in other countries, decentralized exchanges, and privacy wallets. The borderless nature of these transactions also poses complications in the enforcement against

illicit activities, both from regulatory and law enforcement perspectives, as proving a crime is further complicated by the need to prove that crime occurred across borders, which often is too complex for cooperation inter governmentally. Regulators would need to cooperate across borders in order to keep the playing field as level as practicable, but in many cases, countries hold very different priorities that do not align with one another. In the absence of cooperation between countries, regulation could easily push compliance into unregulated corners of cryptocurrency activity.

9.2 Difficulty in classification

The confusion over how to categorize cryptocurrencies is a primary regulatory barrier. Some tokens function as currencies, commodities, securities, or utilities and many operate in or near the middle of these categories. Misclassification causes both over regulation that threatens dynamic innovation, and under regulation that produces avenues of regulatory arbitrage that may allow users to misuse tokens, without sufficient regulatory scrutiny. In India for example, the regulators have not yet designated cryptocurrencies according to financial regulations so there is some ambiguity over issues like taxes, compliance, and investor rights. Internationally, in addition to the sector's fragmented nature, disparate categorization has been an obstacle to establishing clarity with respect to regulatory governance. The absence of definitional clarity nonetheless renders it less straightforward for both Courts and regulators to apply existing law appropriately, which complicates regulatory scrutiny even more.

9.3 Volatility and consumer risk

Cryptocurrencies are incredibly volatile, often losing or gaining double digit percentages in the space of hours. While volatility exposes consumers to significant losses, it is especially perilous for naive consumers caught up in hype. Add to that the risks created by rampant market manipulation, pump and dump schemes and the absence of guarantees and you have real consumer risk. They may experience harm from fraud (real or perceived) as a result of a lack of regulation. Finally, if exchanges collapse, consumers may even experience a loss of access to their funds, and in India they have no protections to speak of in relation to investor protection. Regulation will not limit volatility but can protect consumer interest by agreeing to regulations requiring transparency, mandating disclosures to consumers, and regulating exchanges to allow consumers fair, transparent practices that limit harm to retail consumers.

9.4 Money laundering and cybercrime

Cryptocurrencies can be lucrative to criminals for illicit activities such as money laundering, ransomware payments, and funding terrorism, due to their pseudonymous nature. Law enforcement faces increased difficulty in identifying, intercepting, and dissuading criminal activity because these users have the ability to utilize decentralized exchanges (DEX) and privacy coins to further bury their transactions. In India, regulators have flagged concerns over the risks associated with cryptocurrencies generally but particularly taking into consideration the number of potential vulnerabilities in the country to cross border terror financing activity. Regulating criminal market behaviors in the digital asset space will be virtually impossible, unless some form of exceedingly robust KYC, AML and CTF protocols are developed, allowing unsafe market behaviors to become protected enclaves for illicit transactions. Given the need to mitigate the risks to financial system integrity posed by these transactions while still allowing for legitimate uses of cryptocurrencies to thrive, international collaboration will be essential and the use of blockchain analytics tools along with real time monitoring will be crucial.

9.5 Technological complexity

The blockchain technology that comprises the cryptocurrency segments is so technical, that it may be true that regulators do not have the knowledge and skills to fully understand how it operates. While the lack of knowledge is a potential reason for regulatory inaction there could be many other drivers. Knowledge voids can easily evolve into delays in policy development, a policy development, and/or an incomplete policy response, regulatory gaps, and/or ineffective enforcement. Further, the crypto technologies with decentralized finance (DeFi) applications, smart contracts, and cross chain applications are changing and evolving rapidly enough that the technology has likely evolved long before a regulator can respond. Sadly, laws can even be enacted into law, before they have become outdated. Closing the knowledge gap will require building capabilities at regulatory agencies, engagement with technical experts, and adjusting regulatory laws that are adaptable and technology neutral, in order to follow the ongoing developments of the space.

10.Recommendations

Need for a balanced, technology neutral legal framework

India should pursue a balanced and technology neutral regulatory approach based on principles, not tied to specific technologies. The goal is to regulate the function and risk of crypto assets without naming technologies that could hinder innovation from strong definitions or outdated legislation. A clear, principles based, and adaptable framework would support consumer protection and fraudulent and other illicit conduct while also supporting innovation. A balanced regulatory approach would protect legitimate blockchain applications and allow them to flourish. These rules would be intended to address threats of volatility, scams, and money laundering, and their respective crimes. By constructing rules that are malleable to future technological developments, India would allow itself opportunities to future proof regulations in the digital economy and remain competitive in the global digital economy.

Categorization of crypto: payment token, utility token, security token

Appropriate categorization is critical to regulatory success. Cryptocurrencies can be classified as payment tokens (cryptocurrencies utilized as a mechanism for payment in a transaction), utility tokens (those tokens that allow access to a product or service), and securities tokens (those tokens, that are used for investment or ownership). This classification allows the regulator to determine the correct laws to apply (requiring the payment tokens to meet requirements for payment tokens and to require the securities token to meet requirements for securities). This would also allow taxing authorities and consumer protection agencies to apply the same rules. While some tokens clearly present risks to investors or users, certain definitions may prevent plainly innocent projects from being overregulated or obviously high risk assets from being underregulated.

Learning from international best practices

India could learn from regulatory models in other countries such as Japan, Singapore, Switzerland, and the EU. These jurisdictions have developed some regulatory frameworks (such as licensing, investor protection, and fraud protection) that develop certain safeguards against risks while allowing business growth. These models still allow for innovation and if India can adapt successful aspects of those models, there is a strong chance to avoid some of the many mistakes that other jurisdictions have made, while speeding up regulatory clarity and ultimately positioning India as a responsible, forward thinking, participant in the global crypto

debate.

Public education and investor awareness

Awareness campaigns to community outreach are an important way to ensure that every individual in society can be aware of the opportunities cryptocurrencies have to offer, and the dangers to look out for. It is the responsibility of educators to provide information and educate on the risks of volatility, scams and detective measures, security best practices, and legal obligations. Education and public awareness may lessen a person's chance of becoming a victim to scams and speculative bubbles and ultimately help build an informed and educated group of investors. In the end, the more protection that individuals have, the better stability and reliability there will be for the digital asset ecosystem in India.

11.Conclusion

The regulation of cryptocurrency in India is complex and continues to evolve with the journey between realization and financial stability. Progressive jurisdictions include countries like Japan and Singapore, the European Union, the United Kingdom and some parts of the USA, some being increasingly clearer and structured, yet India is still depending on indirect methods for regulation, like taxation for example, anti money laundering measures, and central bank advisories, and has yet to enact an actual cryptocurrency law. India's cautious approach has helped to mitigate certain types of systemic risks, but it has also created uncertainty, and most of the cryptography industry's activity has moved offshore, as has the opportunity for India to take a share of blockchain related growth. The Supreme Court's 2020 decision to recognize the rights of companies engaged in payment processing and digital currencies marked a turning point, and we are now able to engage with such businesses without the risk of insolvency, but following the Supreme Court's decision, there has yet to be definitive regulation for the virtual assets and cryptocurrency industry in India. Going forward, India needs an established, responsive, technology neutral regulatory agenda to define the boundaries around cryptocurrency, define compliance thresholds, and foster continuous creativity and innovation. This would not only provide protection to consumers and others in the financial system but it also may help create a self resilient body of participants in this space to advance India's prospects as a viable competitor in the rapidly growing global digital economy.

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