INTERNET AND MOBILE ASSOCIATION OF INDIA VERSUS RESERVE BANK OF INDIA

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Abstract

A statement issued by RBI led to a flurry of activities by different stakeholders for almost 5 years. The summary of the judgement issued by the Supreme Court in the case of the Internet and Mobile Association of India versus the Reserve Bank of India sets out the context, arguments, and conclusion of the conflict between those who regulate and those to propose to push the boundaries of technology and finance further. While the nature of cryptocurrency itself is difficult to understand, what is clear is the impact it has had in the world. The Inter-Disciplinary Committee has categorically recommended that the use of cryptocurrency should be stopped, because the dangers of unregulated currency include money laundering, tax evasion and terrorist financing. This case law itself captures the genesis of virtual currency and block chain, the response of the world to virtual currency, and the stand taken by India in this context. Anonymity is the backbone of virtual currency and naturally the government cannot regulate what it does not know. At the moment, it seems like the judiciary has reaffirmed the government's stand. However, the future does hold some form of regulated cryptocurrency, which, ideally, can be safe, encrypted, and accessible.

Keywords: RBI, Cryptocurrency, bit coin, Internet Mobile Association of India, Encryption, Supreme Court

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WHAT HAS HAPPENED TILL NOW?

On April 05, 2018, the Reserve Bank of India ("**RBI**") issued a "*Statement on Development and Regulatory Policies*" which directed entities regulated by RBI to (i) not deal with/provide services to any individual/business dealing with/settling virtual currencies; (ii) to exit the relationship, if they already have one, with such individuals/business entities, dealing with/settling virtual currencies ("**VC**"). A circular was released on April 06, 2018 which reiterated the same prohibition on dealing with VC.

The internet and mobile association of India ("**IAMAI**") is an association which represents the interests of online and digital services industry and have filed a writ petition to challenge this prohibition.

IAMAI'S ARGUMENT

Some of IAMAI's arguments can be summarized as follows:

a. RBI does not have the power to prohibit the activity of trading in VC through VC exchanges ("**VCEs**") since VC are not legal tender but tradeable commodities/digital goods, not falling within the regulatory framework of the Reserve Bank of India Act, 1934 ("**RBI Act**") or the Banking Regulation Act, 1949.

b. All other stake holders such as the Department of Economic Affairs of the Government of India, Securities and Exchange Board of India, Central Board of Direct Taxes, etc., have actually recognized the positive and beneficial aspects of cryptocurrencies as digital assets but RBI has taken a contra position without any rational basis.

c. Many of the developed and developing economies of the world, multinational and international bodies and the courts of various countries have scanned crypto currencies but found nothing pernicious about them and even the attempt of the Government of India to bring a legislation banning crypto currencies, is yet to reach its logical end.

d. RBI should have considered the fact that the members of IAMAI would have taken necessary precautions including avoiding cash transactions, ensuring compliance with KYC norms, of their own accord and allowing peer-to-peer transactions only within the country.

e. RBI has not applied its mind to the fact that not every crypto currency is anonymous. The report of the European Parliament also classified VCs into anonymous and pseudo-anonymous. Therefore, if the problem

sought to be addressed is anonymity of transactions, the same could have been achieved by resorting to the least invasive option of prohibiting only anonymous VCs.

f. It is a paradox that block chain technology is acceptable to RBI, but crypto currency is not.

RBI'S RESPONSE

Some of RBI's responses can be summarized as follows:

a. VC (i) do not satisfy the criteria such as store of value, medium of payment and unit of account, required for being acknowledged as currency; (ii) are capable of being used for illegal activities due to their anonymity/pseudo-anonymity; (iii) use would eventually erode the monetary stability of the Indian currency and the credit system; and (iv) VCEs do not have any formal or structured mechanism for handling consumer disputes/ grievances.

b. The impugned decision of RBI (i) is legislative in character and is in the realm of an economic policy decision taken by an expert body warranting a hands-off approach from the Court; (ii) is within the range of wide powers conferred upon RBI under the Banking Regulation Act, 1949, the RBI Act and the Payment and Settlement Systems Act, 2007; and (iii) are not excessive, confiscatory or disproportionate; (iv) were necessitated in public interest to protect the interest of consumers, the interest of the payment and settlement systems of the country and for protection of regulated entities against exposure to high volatility of the virtual currencies.

c. No one has an unfettered fundamental right to do business on the network of the entities regulated by RBI. RBI is empowered and duty bound to take such pre-emptive measures in public interest and the power to regulate includes the power to prohibit. RBI cautioned users, holders and traders of VCs about the potential financial, operational, legal, customer protection and security related risks they were exposing themselves to.

d. The host of material taken note of by RBI in their reports, the reports of the committees to which RBI was a party and the cautions repeatedly issued by RBI over a period of 5 years, would demonstrate the application of mind on the part of RBI, and that RBI did not proceed in haste but proceeded with great care and caution.

e. The KYC norms followed by the VCEs are far below what other participants in the payments and monetary system follow. In any case,

KYC norms are ineffective, as the inherent characteristic of anonymity of VCs does not get remedied.

f. Cross-border nature of the trade in VCs, coupled with the lack of accountability, has the potential to impact the regulated payments system managed by RBI. A large constituent of the VC universe does not hold membership of IAMAI or is not even accountable for their acts but is material and instrumental in driving the VC trade.
g. RBI would not be able to curtail, limit, regulate or control the generation of VCs and their transactions, resulting in ever-present and inevitable financial risks.

THE JUDGEMENT

The Supreme Court ("**SC**") acknowledged that (i) that RBI has not so far found, in the past 5 years or more, the activities of VCEs to have actually impacted adversely the way the entities regulated by RBI function; (ii) that the consistent stand taken by RBI has not prohibited VCs in the country; and (iii) that even the Inter-Ministerial Committee which initially recommended a specific legal framework (including the introduction of the Crypto-token Regulation Bill 2018) was of the opinion that a ban might be an extreme tool and that the same objectives can be achieved through regulatory measures. The SC stated that the concern of RBI should be about the entities regulated by it, and till date, RBI has not come out with any stand that that any of the entities regulated by it have suffered any loss, directly or indirectly, on account of the interface that the VCEs had with any of them.

In ***State of Maharashtra v. Indian Hotel and Restaurants Association***[1]**,** the SC held that there must have been at least some empirical data about the degree of harm suffered by the regulated entities (after establishing that they were harmed). It is not the case of RBI that any of the entities regulated by it has suffered on account of the provision of banking services to the online platforms running VCEs. The SC held as follows: "*It is no doubt true that RBI has very wide powers in view of the special place and role that it has in the economy of the country. These powers can be exercised both in the form of preventive as well as curative measures. But the availability of power is different from the manner and extent to which it can be exercised. While we have recognized the power of RBI to take a pre-emptive action, we are testing in this part of the order the proportionality of such measure, for the determination of which RBI needs to show at least some semblance of any damage suffered by its regulated entities. But there is none.*

When the consistent stand of RBI is that they have not banned VCs and when the Government of India

[1] *(2013) 8 SCC 519*

is unable to take a call despite several committees coming up with several proposals including two draft bills (Crypto-token Regulation Bill 2018 and Banning of Cryptocurrency and Regulation of Official Digital Currency Bill, 2019), both of which advocated exactly opposite positions, it is not possible for us to hold that the impugned measure is proportionate." To sum it up, RBI circular banning VC is to be set aside on the ground of proportionality.

CONCLUSION

While this judgement is a relief for the VC industry, the SC actually has not commented on the legality of VC itself. This is important to remember, especially since the "*Banning of Cryptocurrency and Regulation of Official Digital Currency Bill, 2019*" ("**Draft Bill**") has been drafted and submitted by an Inter-Ministerial Committee, constituted by the Ministry of Finance, which is looking to prohibit the using, mining, holding, selling, trade, issuance, disposal or use of VC in India. However, the Draft Bill (i) permits the use of processes or technology underlying any cryptocurrency for experiment, research, or teaching; and (ii) states that the Central Government may, in consultation with the central board of the RBI, approve digital rupee to be legal tender. The RBI may also notify a foreign digital currency as a foreign currency. In this context, if this Draft Bill is passed, then the legality and validity of VC will be reinforced.