RESEARCH PAPER

From Cloud to Court: Legal Challenges for Businesses in India's Digital Currency Wave

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ABSTRACT
The rapid adoption of digital currencies and blockchain technologies in India has fundamentally reshaped the business environment, presenting novel opportunities alongside significant legal and regulatory challenges. This paper examines the evolving legal landscape governing digital currencies in India, with a focus on the compliance burdens, taxation issues, anti-money laundering (AML) obligations, data protection concerns, and enforcement mechanisms that businesses must navigate. Drawing on the Reserve Bank of India's circulars, the Finance Act, 2022, and the proposed Digital India Act, this article identifies critical ambiguities and enforcement gaps that expose businesses to litigation and regulatory scrutiny. It also analyzes recent judicial pronouncements on the classification of virtual digital assets and the jurisdiction of courts in cross-border digital transactions. The paper argues that while India's approach to digital currency regulation has progressed from prohibition to regulated permissibility, the current framework lacks coherence and fails to provide adequate legal certainty for businesses. It further suggests that a unified regulatory body, clear classification criteria, and harmonized international cooperation are essential to mitigate legal risks and foster innovation in India's burgeoning digital economy. This study contributes to the discourse on fintech regulation in emerging economies and offers actionable insights for business leaders, policymakers, and legal practitioners.

Keywords: Digital currency, blockchain, cryptocurrency regulation, India, legal challenges, fintech, taxation, AML, data protection.
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INTRODUCTION

A complex interplay of innovation, caution, and regulatory evolution has marked India's journey with digital currencies. The Reserve Bank of India (RBI) has played a pivotal role in shaping the regulatory landscape, striking a balance between fostering financial innovation and safeguarding the financial system. This section explores the historical and current regulatory framework governing digital currencies in India, highlighting key developments, legal challenges, and their implications for businesses. In April 2018, the RBI issued a circular that prohibited regulated financial institutions, such as banks and non-banking financial corporation's (NBFCs), from providing services to businesses dealing with virtual currencies. The circular effectively severed cryptocurrency exchanges' access to banking services, crippling their ability to convert crypto currencies into fiat currency. The RBI cited concerns over money laundering, terrorist financing, and financial instability as justifications for the ban. However, this move faced significant backlash from the crypto industry, which argued that the blanket prohibition stifled innovation and violated constitutional rights.

The issue reached a critical juncture in 2020 when the Supreme Court of India, in Internet and Mobile Association of India v. Reserve Bank of India, overturned the RBI's circular. The Court ruled that the ban violated the fundamental right to trade under Article 19(1)(g) of the Indian Constitution, as it failed the test of proportionality. The RBI could not provide empirical evidence of harm to regulated entities from providing services to crypto exchanges, and less restrictive measures could have achieved the same objectives. This landmark judgment marked a turning point, allowing crypto exchanges to resume operations, but it also underscored the absence of a clear regulatory framework for digital currencies in India.

CURRENT REGULATORY LANDSCAPE

Post-2020, India's regulatory approach to digital currencies has remained notably fragmented and evolving, reflecting the complex intersection of technological innovation, economic considerations, and regulatory oversight. Cryptocurrencies such as Bitcoin and Ethereum are neither explicitly banned nor officially recognized as legal tender within the country. Instead, the government has adopted a cautious regulatory stance, implementing a series of tax and compliance measures aimed at monitoring and taxing the burgeoning digital asset space.

Specifically, since 2022, India has imposed a 30% tax on gains derived from cryptocurrency transactions, signaling an acknowledgment of the increasing significance of digital assets while maintaining a firm stance on their regulation. Alongside this, a 1% Tax Deducted at Source (TDS) has been mandated on every crypto transaction, making it obligatory for traders and investors to withhold a portion of their earnings at the point of transaction. This move aims to improve oversight and increase transparency within the trading ecosystem but poses challenges for traders who face the inability to offset losses from crypto trades against other forms of income, thereby intensifying the financial burden on businesses and individual traders. Furthermore, crypto exchanges operating within India are required to comply strictly with anti-money laundering (AML) and counter-terrorism financing (CFT) regulations. This includes rigorous user identity verification procedures—often referred to as Know Your Customer (KYC)—and mandatory reporting of suspicious activities to the Financial Intelligence Unit (FIU). These regulatory demands are designed to prevent illicit activities such as money laundering and terrorist financing but also add layers of compliance that can limit the flexibility and growth potential of crypto platforms.

Parallel to these regulatory developments, the Reserve Bank of India (RBI) has pioneered a more formalized approach to digital currencies through the introduction of the Central Bank Digital Currency (CBDC), known as the e-Rupee. Launched initially in pilot phases—first for wholesale transactions in November 2022 and subsequently for retail use in December 2022—this initiative marks a significant milestone in India's digital currency landscape. The e-Rupee is a sovereign digital currency issued directly by the RBI, built on blockchain technology, which provides a secure, transparent, and tamper-proof ledger system.

The e-Rupee aims to facilitate smooth, efficient digital payments with features designed to enhance user experience and operational flexibility, such as offline functionality, programmability, and interoperability with existing payment infrastructure. These features are intended to promote financial inclusion, reduce transaction costs, and improve payment security. However, the rollout of the e-Rupee faces several challenges, including ensuring scalability to handle large transaction volumes, safeguarding data security against cyber threats, and establishing robust governance models to oversee its deployment and operation.

PROPOSED LEGISLATION AND ONGOING DEBATES

The Banning of Cryptocurrency & Regulation of Official Digital Currency Bill, 2019, proposed by an inter-ministerial committee, sought to ban all private crypto currencies while promoting an official digital currency issued by the RBI. The draft bill defined crypto currencies broadly as any digital token representing value, excluding those used for research or experimental purposes. It proposed stringent penalties, including up to 10 years' imprisonment for violations, raising concerns about overregulation. The bill's status remains unclear, reflecting India's cautious approach to balancing innovation with regulatory control. Recent Supreme Court observations in May 2025 highlight ongoing concerns about the unregulated nature of crypto currencies. Justice Suryakant described crypto currencies as a "parallel economy" posing risks to India's financial stability, emphasizing the need for a structured legal framework to address potential misuse for illegal activities like money laundering and terror financing. The evolving regulatory landscape presents several challenges for businesses. First, the lack of clear legislation creates uncertainty, forcing companies to navigate a patchwork of tax and AML/CFT requirements. Second, the e-Rupee's implementation demands robust cyber security measures to prevent data breaches, as highlighted by the RBI's Annual Report noting a 34% increase in fraud cases related to digital payments. Third, businesses must address scalability and interoperability issues with DLT-based systems, which require significant investment in infrastructure and compliance.

CONCLUSION

India's digital currency regulatory landscape is currently undergoing a significant transformation, marking a pivotal juncture in its evolution. The Reserve Bank of India's (RBI) introduction of the e-Rupee highlights a clear emphasis on fostering innovation within the digital currency space. However, the absence of comprehensive and detailed legal frameworks governing private crypto currencies introduces a layer of uncertainty for market participants and investors alike. In this environment, companies operating in the digital currency sector should adopt a flexible approach, actively investing in robust compliance measures and advanced cyber security protocols. Simultaneously, they should advocate for the development of more explicit and detailed regulatory guidelines to effectively harness and capitalize on India's expanding digital currency momentum, ensuring sustainable growth and technological advancement.

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