BHARAT WEB3 ASSOCIATION

A MODEL REGULATORY FRAMEWORK

For VDASPs In India

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Prepared by :

Bharat Web3 Association

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WEB: https://bwaind.in/

E-MAIL: secretariat@bharatweb3association.com

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EXECUTIVE SUMMARY

Virtual digital assets (alternatively referred to as crypto-assets, crypto, virtual assets, digital assets, etc.) are integral to public blockchains as they enable users to own digital elements and incentivize network participants to keep the network running. This concept has been recognized by leading scholars and has played out in the real-world with several government blockchain use-cases relying on virtual digital assets as the underlying fuel of the blockchain network. Public blockchain networks are an opportunity to keep the internet open and democratic (through decentralised governance, transparency and equal access) rather than gated and centralised. By moving power and control of the network to the 'edges' rather than the center, they help users derive more value out of the internet.

At the same time, it is undeniable that virtual digital asset activities pose various risks. Therefore, new regulatory measures for virtual digital assets, the tokens that support blockchain networks, are required in India for a variety of reasons, including the fast pace of adoption.

A study by a leading analytics firm in 2024[1] reported that India is the top-ranked country in terms of virtual digital asset adoption in the world when adjusted for purchasing power and population for two years in a row. Recent statements of leading Indian Government officials indicate that the Indian regulatory approach will be developed on the basis of global consensus since virtual digital assets are a global phenomenon and no country can move in isolation.[2]

The current supervisory framework on virtual digital assets in India covers limited ground, being focused on income tax and anti-money laundering. To protect consumer interest and hence foster a healthy Web3 ecosystem, there is a need for overarching regulatory and governance framework of virtual digital asset service providers – entities that hold consumer value in trust, or otherwise act in a fiduciary capacity for consumers. For the smooth implementation of most Web3 use-cases, there is also a need to address ambiguities under existing regulatory frameworks.

Policy consensus is gradually emerging globally, particularly after the adoption of the G20 Roadmap on Crypto-Assets (which came on the back of India's G20 presidency in 2022-23) and the European Union's (**EU**) passage of the Markets in Crypto-Assets Regulation (**MiCA**) in 2023. That said, there is no established formula globally to regulate virtual digital asset markets even after over fifteen years since the advent of blockchains. This is primarily because: (a) blockchains are global and decentralized; (b) different virtual digital assets, depending on how they are designed and programmed, can have different legal characteristics and have been difficult to be classified as per existing norms; (c) the types of models and activities in the industry have evolved rapidly; and (d) each jurisdiction's legal framework and policy priorities vary. For instance, India is an emerging economy with unique considerations such as exchange control restrictions that any new framework must be tailored to. Crafting the right regulatory approach for India on virtual digital assets is, hence, non-trivial.

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[1] https://www.chainalysis.com/wp-content/uploads/2024/10/the-2024-geography-of-crypto-report-release.pdf.

[2] PM Narendra Modi advocates for global crypto regulatory framework (https://www.forbesindia.com/article/cryptocurrency/pm-narendra-modi-advocates-for-global-crypto-regulatory-framework/87823/1); Finance Minister Nirmala Sitharaman calls for global crypto regulations (https://www.forbesindia.com/article/crypto-made-easy/finance-minister-nirmala-sitharamancalls-for-global-crypto-regulations/75529/1)

As recognized by the 'IMF-FSB Synthesis Paper: Policies for Crypto-Assets' (**IMF-FSB Paper**),[3] which formed the basis for the G20 Roadmap on Crypto-Assets, there are two approaches to addressing gaps in the existing regulatory regime:

1. New Legislation: Regulating virtual digital asset activities under a new legal framework is the approach adopted by the EU with MiCA and Dubai with VARA.

   In furtherance of this first approach, this paper sets out a draft bill, the Virtual Digital Assets Regulatory Authority Bill (**Draft Bill**). Key features of the Draft Bill include: the formation of a new multi-stakeholder regulator for virtual digital asset activity that would have expertise across finance, technology, markets regulation, economics, and law; streamlining of definitions and jurisdictional boundaries across currency, securities, and virtual digital assets; being drafted in an Indian law paradigm yet drawing from global models like MiCA and VARA; remaining principles-based; amending existing legislations where necessary; regulating market participants; and, focusing on safekeeping of customer value. Like in the approach taken by VARA, all virtual digital assets, irrespective of their nature, are proposed to be regulated solely by the Authority, drawing from the expertise of the Authority given its composition.

2. Amending Existing Legislations: Regulating virtual digital asset activities by amending existing legal frameworks. This is the approach adopted by Japan and Singapore with their payment services legislation.

   This second approach of amending existing legislation, rather than introducing a new regulator and regulatory framework, may also be considered if enough new regulatory capacity is built up within existing regulators and if the amendments are thoughtful and thorough. This approach will also need a decision to be made as to which existing regulator will have the responsibility of regulating the sector. Accordingly, the relevant statute(s) can be amended to introduce new provisions. Such new provisions would likely include nearly all the provisions of the Draft Bill which are unique to virtual digital assets, while omitting provisions pertaining to the constitution of the new authority.

In both cases, (a) existing regulatory frameworks are proposed to be amended to allow for the regulation of the virtual digital assets; and (b) the objective is to provide clear guidelines and criteria for classifying these assets to minimize legal ambiguity and ensure harmonious application of the law across different regulatory bodies.

[3] https://www.fsb.org/wp-content/uploads/R070923-1.pdf

I. DRAFT VIRTUAL DIGITAL ASSETS REGULATORY AUTHORITY BILL

In the background of the above approach paper, we have proposed the Draft Bill as a suggested draft legislation approach to govern the sector in India. The below explanatory notes set out various directional aspects of the Draft Bill, followed by the text of the Draft Bill.

1. Explanatory Notes

- Scheme: The statutory scheme of the Draft Bill has been modelled on existing Indian regulatory legislations with similar contexts, including the International Financial Services Centres Authority (**IFSCA**) Act, 2019 (**IFSCA Act**) (with respect to the establishment and constitution of a multi-stakeholder regulatory body), the SEBI Act, 1992 (**SEBI Act**) (with respect to an authority tasked with regulating markets and a range of market participants), and the Payment and Settlement Systems Act (with respect to market participants acting as custodians of customer value). The Draft Bill, of course, has been adapted to the context of virtual digital assets. The regulatory objectives of the Draft Bill are in line with global best practices, including as set out in the IMF-FSB Paper i.e., macroeconomic stability, financial stability, consumer protection, and market and financial integrity. The Draft Bill is largely principles-based and, similar to the SEBI Act and IFSCA Act, will rely to a significant degree on subordinate legislation for prescriptive regulatory norms.

- Terminology and title (Clause 1): The Draft Bill uses the term 'virtual digital assets' given the existing usage of this term under prior legislations i.e., the Income Tax Act and the PMLA. While globally, the terms 'crypto-assets' (used by the G20 and MiCA) and 'virtual assets' (used by the Financial Action Task Force) have gained prominence, it may be less disruptive in the current Indian context to use the term already used under existing legislations.

- Definition of virtual digital asset (Clause 2(8) read with the First Schedule): The Draft Bill's definition of 'virtual digital asset': (1) modifies the existing definition under Section 2(47A) of the Income Tax Act,, and replaces it with a more streamlined clause. This clause is in sync with international developments, being derived from MiCA's definition of 'crypto-asset' which underwent elaborate consultation and iterations. Aligning the definition with international best practices will be in line with India's stated intent to move in sync with international consensus on the regulation of virtual digital assets; (2) empowers the Authority to include or exclude instruments from the definition; (3) creates a framework of avoiding jurisdictional overlap with financial instruments, this is proposed to be achieved by taking an approach such as in VARA wherein the authority under VARA is vested the jurisdiction to regulate all virtual digital assets, despite its innate nature.

  The existing regulators in turn will need to factor in digital assets into their regulatory and enforcement practices by enacting amendments to provide the proposed Authority the jurisdiction over such virtual digital assets that may otherwise impede their jurisdiction, this can be achieved given the multi-stake holder approach for the composition of the Authority is proposed to be drawn from the RBI and SEBI, etc., providing effective representation and expertise to the Authority.

The Draft Bill hence follows the now globally emerging principle of "**same activity, same risk, same regulation**", as recognized by the FSB.

As the definition of virtual digital assets under the Income Tax Act, is sought to be amended to effect this change, the resulting clarity will also have benefits for the taxation regime and anti-money laundering regime (as the definition under the PMLA in turn references the definition under the Income Tax Act). For instance, under today's widely-worded definition under the Income Tax Act, a dematerialised unit of a share may also, on a technical and literal reading, be categorised as a virtual digital asset, which does not appear to be the legislative intention.

- Definition of virtual digital asset service providers(Clause 2(9)): Virtual digital asset service providers are the focus of regulation under the Draft Bill. The Draft Bill defines such entities in line with the notification dated 7 March 2023 under the PMLA which identified five activities carried out in the course of business on behalf of another person, and hence classified virtual digital asset exchanges, custodial wallet providers, and others as reporting entities under the PMLA. The same five activities are recognized as being the basis of the definition of 'virtual asset service provider' in the Commonwealth Model Law. The Draft Bill includes the additional activities of the provision of professional advice pertaining to virtual digital assets and of portfolio management as covered regulated activities. This is in line with global precedent like MiCA as well as Indian regulatory approaches to existing markets like the securities market, where investment advisers and portfolio managers are regulated entities.

- Codifying the situs of a virtual digital asset (Explanation to Clause 2): The location or *lex situs* of a virtual digital asset becomes relevant in the context of cross-border virtual digital asset transactions, and determining when there is a cross-border transaction of a virtual digital asset. To avoid ambiguity in light of the decentralized nature of virtual digital assets, the Draft Bill codifies the common law concept of *mobilia sequuntur personam* (movables follow the person). This maxim has been applied by Indian courts in the context of intellectual property to hold that the situs of an intangible property is where its owner resides.[4] While there are no Indian judicial decisions on this concept in the context of virtual digital assets specifically, courts in the United Kingdom have followed a similar approach with regard to determining the *lex situs* of virtual digital assets.[5]

- Establishment and composition of the Authority (Chapters II and IV):

  The new Authority is intended to have expertise across finance, technology, markets regulation, economics, and law. The Authority will be comprised of financial sector regulatory experts (from the RBI, SEBI, Ministry of Finance and MEITY), a serving or retired Supreme Court or High Court Judge, persons selected by a selection committee who have expertise in the virtual digital assets industry, and representatives from the virtual digital assets industry. Members other than those selected by the selection committee are required to have expertise in law, finance,

[4] E.g., *Cub Pty Limited v. Union of India*, 2016 SCC OnLine Del 4070.

[5] E.g., *Tulip Trading Limited v. Bitcoin Association for BSV*, [2022] EWHC 667 (Ch).

economics, science or technology. The composition of the Authority has been partly derived from the model adopted for the IFSCA, which has a similar composition.

While existing Indian legislations can alternatively be amended to introduce the new norms and bring the subject-matter within the jurisdiction of existing regulators, this approach may not address the issue of regulatory capacity since each existing framework is tied to an existing regulator with a limited and focused regulatory capacity, and expanding their remit to cover virtual digital assets without significant enhancement of their capacity could lead to regulatory inefficiencies, inconsistencies, and gaps in oversight. It was for similar reasons that the IFSCA was also formed in 2019 as a new, multi-stakeholder Indian authority.[6] Further, no single existing regulatory framework is structured to address all the aspects of virtual digital asset activity that may need to be addressed.

The provisions relating to establishment, composition, finance, accounts and audit are broadly modelled on the IFSCA Act, 2019.

- Powers and functions of the Authority (Chapters III and VI): The Authority has been given wide-ranging powers to regulate virtual digital asset markets and market participants, including through delegated legislation. It is well recognised in Indian policy-making that delegated legislation is appropriate when subject-matters are complex and ever-evolving and all future issues cannot be accounted for at the time of enacting the primary legislation. This provides 'play in the joints' to the relevant authority to evolve standards as the sector matures. This principle has been adopted in the context of other economic statutory frameworks such as securities laws, insurance laws, and the law around international financial services centres, where the primary legislation lays down the principle-based framework and the delegated legislation lays down granular eligibility and compliance requirements. A similar approach has been sought to be adopted in the Draft Bill.

  Significantly, the Authority is granted power to regulate cross-border transactions of virtual digital assets, in consultation with the RBI. This seeks to provide a mechanism to address the current ambiguities under FEMA with regard to cross-border virtual digital asset transactions, which make several promising Web3 use-cases challenging, since public blockchains inherently involve cross-border movements of virtual digital assets.

  Going forward, the Authority will issue guidelines for its regulated entities which complement the PMLA requirements, similar to the role of the RBI and SEBI for their respective regulated entities.

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[6] "*Currently the banking, capital markets and insurance sectors in IFSC are regulated by multiple regulators i.e. RBI, SEBI and IRDAI. The dynamic nature of business in the IFSCs necessitates a high degree of inter-regulatory coordination. It also requires clarifications and frequent amendments in the existing regulations governing financial activities in IFSCs. The development of financial services and products in IFSCs would require focused and dedicated regulatory interventions. Hence a need is felt for having a unified financial regulator for IFSCs in India to provide a world class regulatory environment to financial market participants. Further, this would also be essential from an ease of doing business perspective. The unified authority would also provide the much needed impetus to further development of IFSC in India in-sync with the global best practices.*" Cabinet approves introduction of International Financial Services Centres Authority Bill, 2019 in Lok Sabha, after withdrawal from Rajya Sabha (https://pib.gov.in/PressReleseDetail.aspx?PRID=1592551).

- Authorisation of market participants (Chapter V): This chapter provides the basis for authorisation of market participants by the Authority, and the criteria based on which such authorisation may be granted. The Draft Bill provides for the Authority to prescribe further requirements to be met by virtual digital asset service providers by way of delegated legislation. In keeping with the discussion on delegated legislation above, this approach is in line with the prevailing practice under other economic legislations. For instance, Section 12 of the SEBI Act requires various market participants such as stockbrokers, portfolio managers and investment advisors to register with SEBI in accordance with regulations made under the SEBI Act. Further to this, SEBI has issued regulations specifically governing different types of intermediaries or activities such as the SEBI (Stock Brokers) Regulations, 1992, SEBI (Portfolio Managers) Regulations, 2020 and SEBI (Investment Advisers) Regulations, 2013. These regulations contain provisions on exemption from registration for certain entities, qualification requirements, net worth, period of validity of the registration etc. The Insurance Regulatory and Development Authority of India (**IRDAI**) also has the power to issue rules and regulations under the IRDAI Act, 1999 and Insurance Act, 1938. IRDAI has issued regulations governing insurance brokers, different types of insurance, regulatory sandbox, insurance aggregators, insurance-related advertising, and cybersecurity, among others. The Commonwealth Model Law has also recognised that member countries may specify additional obligations for virtual digital asset service providers based on the activities they are engaged in by way of delegated legislation. Eligibility and compliance requirements will vary among virtual digital asset service providers based on the nature of activities they are engaged in. The Authority is empowered to provide by way of delegated legislation to prescribe the minimum eligibility requirements for each type of virtual digital asset service providers, which can include minimum net worth requirements, fit and proper criteria for management, and operational and technical due diligence, in line with the practice across other similar legislations.

  A right to appeal against refusal is provided by Clause 42, which provides a general right of appeal to the Securities Appellate Tribunal.

  Upon the grant of authorisation to a person to act as a virtual digital asset service provider, the Draft Bill, under Clause 23, provides for the Authority to prescribe standards for the functioning of the virtual digital asset service provider by way of delegated legislation. Further, the Authority is also empowered to lay down policies and give directions for the regulation of virtual digital asset service providers. Chapter VII of the Draft Bill requires virtual digital asset service providers to operate in accordance with the regulations issued under the Draft Bill, the conditions based on which authorisation was granted, and directions of the Authority.

  Illustratively, we have set out below a brief overview of eligibility and compliance requirements for virtual digital asset service providers based on global legislations and Indian policy objectives, which could be considered for incorporation in delegated legislation issued under the Draft Bill.

  General eligibility and compliance requirements for virtual digital asset service provider:

1. Requirements pertaining to the form of the application for authorisation

a. Details of the applicant virtual digital asset service provider such as its legal and commercial name and incorporation documents, based on FIU's guidelines, MiCA, the VARA Act and guidelines issued by the Hong Kong Securities and Futures Commission.[7]
b. Details of the satisfaction of minimum net worth and fit and proper criteria, based on existing regulatory practice in India.
c. Details of the Indian presence of the virtual digital asset service provider and Indian directors/partners, to ensure consumer protection in India.
d. Obtaining security clearance for non-resident directors from the Ministry of Home Affairs, and requirement of Indian citizenship for certain key managerial personnel, for national security reasons.
e. A description of the services that the virtual digital asset service provider intends to provide and the internal policies of the virtual digital asset service provider, based on MiCA.
c. Proofs of having met prudential requirements, based on MiCA and the VARA Regulations, 2023[8].
d. Descriptions of the governance arrangements of the virtual digital asset service provider along with details of the virtual digital asset service provider's board, its composition and committees, based on MiCA and the VARA Regulations.
e. Descriptions and proofs of risk management and investor / customer protection arrangements, based on MiCA, VARA Regulations and guidance issued by the Hong Kong Monetary Authority.
f. Descriptions for the segregation of virtual digital assets and funds of the virtual digital asset service provider and its clients / users, based on MiCA, VARA Regulations and the guidelines on consumer protection measures issued by the Monetary Authority of Singapore[9].

2. Compliance requirements for virtual digital asset service providers generally:

a. Obligations to act in a fair and professional manner in the best interests of clients by providing clear information on risks associated with virtual digital asset transactions, policies on pricing and costs etc., based on MiCA and guidance issued by the Hong Kong Monetary Authority and the Hong Kong Securities and Futures Commission.
b. Prudential obligations relating to maintenance of required capital, manner of maintaining annual financial statements, manner of investment of assets, and procurement of an insurance policy or a comparable guarantee fulfilling certain conditions such as terms and conditions of the policy, based on MiCA.

[7] https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2023/20231222e1.pdf
[8] https://rulebooks.vara.ae/rulebook/virtual-assets-and-related-activities-regulations-2023
[9] https://www.mas.gov.sg/-/media/mas-media-library/regulation/guidelines/pso/ps-g03-guidelines-on-consumer-protection-measures-by-digital-payment-token-service-providers/ps-g03_guidelines-on-consumer-protection-safeguards-by-dpt-service-providers_vf.pdf

c. Consumer protection obligations including grievance redressal and advertising, based on MiCA and VARA Regulations.
d. Obligations relating to outsourcing, based on MiCA.
e. Obligations relating to cybersecurity, based on the Technology and Information Rulebook issued by VARA[10].

Compliance obligations for specific categories of virtual digital asset service providers

Virtual digital asset regulations in foreign jurisdictions also prescribe requirements specifically directed at certain categories of virtual digital asset service providers based on the nature of the activities carried out by them, much of which is generally left to delegated legislation. For instance, since MiCA is applicable to the many countries that are part of the European Union, it empowers national authorities in these countries along with other financial sector regulators in the European Union with adequate capacity to develop compliance standards and rules catered to national governance systems and needs. MiCA also sets out specific obligations to be fulfilled by different categories of virtual digital asset service providers.

Similarly, VARA Regulations provide for generally applicable requirements for the licensing or authorisation of virtual asset service providers. However, VARA has implemented delegated legislation to further delineate licensing requirements for specific categories of virtual asset service providers.

Purely by way of illustration, potential prescriptions for key market participants can include the following:

1. For exchanges

a. Compliance with the operating rules of the exchange and of procedures to detect market abuse which were submitted along with the application for authorisation, based on MiCA and the Exchange Services Rulebook issued by VARA[11].
b. Formulation of commercial policies which set out the terms of the relationship between the exchange service providers and its clients and descriptions of the methodology for determining the price of the virtual digital asset that the exchange service providers intend to apply, based on MiCA.
c. Execution of agreements between the exchange service providers and its clients which set out various terms such as the identities of the parties to the agreement, the nature of the services provided, custody, descriptions of the security systems in place and applicable law, based on MiCA.
d. Formulation of execution and transfer policies where the exchange service providers intends to execute orders for and transfer virtual digital assets on behalf of its clients, based on MiCA.

[10] https://rulebooks.vara.ae/rulebook/technology-and-information-rulebook
[11] https://rulebooks.vara.ae/rulebook/exchange-services-rulebook

e. Policies for business continuity and settlement, based on the Exchange Services Rulebook issued by VARA.
f. Required amounts of liquid capital and paid-up share capital, financial status, designation of responsible officers, based on guidelines and a licensing handbook for "virtual asset trading platforms" issued by the Hong Kong Securities and Futures Commission[12].

2. For custody service providers

a. Execution of agreements either with exchanges or other clients / users, as the case may be, which set out various terms on the identities of the parties, nature of the services provided along with a description, custody policy, means of communication between the market participant and the client (including the client's authentication system), security systems of the market participant, fees, costs and charges applied by the market participant and governing law, based on MiCA.
b. Formulation of a custody policy which includes a description of security systems used and the nature of custody offered, the rights and obligations of the custody service provider sand the service recipient, based on MiCA.
c. Provision of statements of balances, value and transfer of virtual digital assets to service recipients on a periodic basis, based on MiCA.
d. Segregation of virtual digital assets and funds and formulation of policies and procedures for the same, based on MiCA, the Custody Services Rulebook issued by VARA and the guidelines on consumer protection measures issued by the Monetary Authority of Singapore.
e. Formulation of policies and procedures for withdrawals, based on the Custody Services Rulebook issued by VARA.
f. Compliances relating to wallet management such as hot and cold storage of virtual digital assets, and generation, storage and use of keys, based on the Custody Services Rulebook issued by VARA.

3. For advisors

a. Provision of proofs and documentation on qualifications, expertise and competency of the natural persons engaged by the market participant to provide advice to its clients, based on MiCA and the Advisory Services Rulebook issued by VARA.
b. Obligations relating to disclosures to be made to the clients on the risks associated with transactions involving virtual digital assets and the limitations and speculative nature of the investment advice given, based on MiCA.
c. Obligations relating to disclosures to be made on any potential conflicts of interest, based on MiCA.

- Disclosures and protection of customer value (Clauses 34 and 35): For consumer protection, the Draft Bill provides that virtual digital asset service providers should

[12] https://www.sfc.hk/-/media/EN/assets/components/Guidelines/File-current/Licensing-Handbook-for-VATPs-31-05-2023.pdf?rev=a94fa7324a964e328dd2415815611d76

disclose to their customers applicable terms and conditions, including charges and limitations of liability. Customer value is sought to be protected with a provision modeled on Section 23A of the Payment and Settlement Systems Act, and Article 70 of MiCA which prioritizes the safekeeping of customer value, particularly in the event of an insolvency. The Draft Bill also requires virtual digital asset service providers to hold and maintain insurance commensurate with the size and complexity of their business and the virtual digital asset activities they engage in. The purpose of this provision is to provide virtual digital asset service providers preliminary protection from unforeseen events such as cybersecurity incidents and hence aid in improving the confidence of the public in the virtual digital asset ecosystem. Both MiCA and delegated legislation provided for by VARA impose insurance-related requirements on virtual digital asset service providers.

- Penalties and adjudication (Chapter VIII): In line with recent policy, the Draft Bill does not contain criminal provisions but rather imposes civil penalties for contraventions. The Authority can issue directions and can consider factors to be taken in account while adjudicating penalties based on the amount of loss, repetitive nature of the default and disproportionate gain/unfair advantage resulting from the default, hence allowing for a graded approach towards penalties. An adjudicating authority, modeled on the SEBI Act, is tasked with quasi-judicial adjudications. Appeals to the Securities Appellate Tribunal are provided as a matter of right from any decision of the Authority, followed by appeals to the Supreme Court. Among the existing appellate tribunals, the Securities Appellate Tribunal may be most suited to the present function, given the capacity to adjudicate appeals pertaining to a variety of market intermediaries (e.g., securities and insurance intermediaries). The Draft Bill also provides for a settlement mechanism with respect to alleged compliance defaults, modelled on Section 15JB of the SEBI Act.

2. Draft Bill

THE VIRTUAL DIGITAL ASSETS REGULATORY AUTHORITY BILL, 2024

ARRANGEMENT OF SECTIONS

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THE VIRTUAL DIGITAL ASSETS REGULATORY AUTHORITY BILL, 2024

BILL NO __ OF 2024

[DATE]

A Bill to provide for the establishment of an Authority to protect the interests of holders of virtual digital assets and to promote the development of, and to regulate, the virtual digital asset industry, and for matters connected therewith or incidental thereto.

BE it enacted by Parliament in the _____ Year of the Republic of India as follows:—

CHAPTER I

PRELIMINARY

1. Short title and commencement.—

(1) This Act may be called the Virtual Digital Assets Regulatory Authority Act, 2024.

(2) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint; and different dates may be appointed for different provisions of this Act, and any reference in any provision to the commencement of this Act shall be construed as a reference to the coming into force of that provision.

2. Definitions. — In this Act, unless the context otherwise requires,—

(1) "Authority" means the Virtual Digital Assets Regulatory Authority established under sub-section (*1*) of section 3;

(2) "Member" means a Member of the Authority and includes the Chairperson;

(3) "notification" means a notification published in the Official Gazette, and the expressions "notified" and "notify" shall be construed accordingly;

(4) "prescribed" means prescribed by rules made by the Central Government under this Act;

(5) "regulations" means the regulations made by the Authority under this Act;

(6) "Securities Appellate Tribunal" means the Securities Appellate Tribunal established under section 15K of the Securities and Exchange Board of India Act, 1992 (15 of 1992);

(7) "virtual digital asset" means –

a. a digital representation of a value or of a right which may be transferred and stored electronically, using distributed ledger technology or similar technology;
b. a non-fungible token or any other token of similar nature, by whatever name called;
c. any other digital asset, as the Authority may, by notification in the Official Gazette, specify;

Provided that the Authority may, by notification in the Official Gazette, exclude any digital asset from the definition of virtual digital asset subject to such conditions as may be specified therein:

Provided further that the determination of the Authority as to whether a digital asset amounts to a virtual digital asset shall be final.

Provided also that all notifications issued by the Central Government under sub-section (47A) of section 2 of the Income Tax Act, 1961 (43 of 1961) till the date of this Act coming into force shall be deemed to have been issued under this Act as if this Act had been in force on the date on which such notifications were issued and shall continue to be in force unless and until they are amended or superseded by any notifications issued or rules or regulations made under this Act.

Explanation.—For the purposes of this clause,—

(a) "non-fungible token" means such digital asset or class of digital asset as the Authority may, by notification in the Official Gazette, specify;
(b) “digital asset” means such virtual digital asset as has been defined under section 2 (8) (a) of this Act;
(c) "distributed ledger technology" means a technology that enables the operation and use of distributed ledgers;
(d) “distributed ledger” means an information repository that keeps records of transactions and that is shared across, and synchronised between, a set of distributed ledger network nodes using a consensus mechanism;
(e) "consensus mechanism” means the rules and procedures by which an agreement is reached, among distributed ledger network nodes, that a transaction is validated;
(f) “distributed ledger network node” means a device or process that is part of a network and that holds a complete or partial replica of records of all transactions on a distributed ledger;

(8) “virtual digital asset service provider” means any person (whether Indian or foreign person) that carries on any of the following activities for or on behalf of another natural or legal person in the course of business — exchange between virtual digital assets and fiat currencies;

(a) exchange between one or more forms of virtual digital assets;

(b) transfer of virtual digital assets;

(c) safekeeping or administration of virtual digital assets or instruments enabling control over virtual digital assets;

(d) rendering or agreeing to render advice on, or soliciting, for the purposes of buying, selling, subscribing to, a virtual digital asset (other than advice which is made widely available to the public);

(e) managing virtual digital asset portfolios in accordance with mandates given by clients on a discretionary client-by-client basis;

(f) any other activity that may be notified by the Central Government from time to time.

Explanation.— A virtual digital asset shall be deemed to be situated at the place at which its owner resides, and whether the owner is resident in India or not shall be determined in accordance with the Foreign Exchange Management Act, 1999.

CHAPTER II

ESTABLISHMENT OF AUTHORITY

3. Establishment and incorporation of Authority.—

(1) The Central Government shall, by notification, for the purposes of this Act, establish an Authority by the name of the Virtual Digital Assets Regulatory Authority.

(2) The Authority shall be a body corporate having perpetual succession and a common seal, and subject to the provisions of this Act, with power to enter into and execute contracts, acquire, hold and dispose of property, both movable and immovable, and shall, by the said name, sue and be sued.

(3) The head office of the Authority shall be at such place as the Central Government may, by notification, decide.

(4) The Authority may, with the prior approval of the Central Government, establish its offices at other places in India or outside India.

4. Composition of Authority.—

(1) The Authority shall consist of the following Members, to be appointed by the Central Government, namely:—

a Chairperson;

one Member each to be nominated by—

(i) the Reserve Bank of India, *ex officio;* and,

(ii) the Securities and Exchange Board of India, *ex officio;*

(a) one Member, who is, or has been, a Judge of the Supreme Court or a Chief Justice of a High Court or a Judge of a High Court for at least seven years, to be nominated by the Chief Justice of India;

(b) one Members, from amongst the officials of the Ministry dealing with Finance, to be nominated by the Central Government, *ex officio*; and

(c) one Member, from amongst the officials of the Ministry dealing with Information Technology, to be nominated by the Central Government.

(d) two Members to be appointed by the Central Government on the recommendation of a Selection Committee, and

(e) two Members to be appointed by the Central Government on the recommendation of a self-regulatory organisation.

(2) The Chairperson shall be a whole-time Member and other Members referred to in clause (*d*) of sub-section (1) may be appointed as whole-time or part-time Members as the Central Government may deem fit.

(3) The Members referred to in clauses (a), (b), (c), and (d) of sub-section (1) shall be persons of ability, integrity and standing who have special knowledge of, and professional experience in, management, law, finance, economics, science or technology.

(4) The Members referred to in clause (e) and clause (f) of sub-section (1) shall be persons of ability, integrity and standing who have special knowledge of, and professional experience in, matters relating to the virtual digital asset industry.

(5) The Selection Committee referred to in clause (*e*) of sub-section (*1*) shall consist of such Members and constituted by the Central Government in such manner as may be prescribed.

(6) The Members referred to in clause (g) of sub-section (1) shall be persons who are active participants of the virtual digital asset industry and have significant professional experience in virtual asset service providers.

5. Terms of office and conditions of service of Chairperson and other Members .—

(1) The Chairperson and a Member shall hold office for a term of three years from the date on which they enter upon their office and shall be eligible for re-appointment:

Provided that no person shall hold office as a Chairperson after they have attained the age of sixty-five years or as a whole-time member, save and except for a Member referred to under clause (c) of sub-section (1) of section 4, after they have attained the age of sixty-two years.

(2) The salaries and allowances payable to, and other terms and conditions of service of, the Members, other than *ex officio* Members, shall be such as may be prescribed.

(3) Notwithstanding anything in sub-section (*1*), a Member may—

(a) resign from their office by giving in writing to the Central Government a notice of not less than three months; or

(b) be removed from their office in accordance with the provisions of section 6.

(4) No Member, other than an *ex officio* Member, shall, for a period of one year from the date on which they cease to hold office as such, except with the previous approval of the Central Government, accept— (*a*) any employment either under the Central Government or under any State Government; or (*b*) appointment in any virtual digital asset service provide.

6. Removal of Member from office.—The Central Government may remove from office a Member, who—

(a) is, or at any time has been, adjudged as insolvent; or

(b) has become physically or mentally incapable of acting as a Member; or

(c) has been convicted of an offence which in the opinion of the Central Government involves moral turpitude; or

(d) has acquired such financial or other interest as is likely to affect prejudicially their functions as a Member; or

(e) has so abused their position so as to render their continuance in office detrimental to public interest:

Provided that no Member shall be removed from office under clause (*d*) or clause (*e*) unless they have been given a reasonable opportunity of being heard in the matter.

7. Meetings of Authority .—

(1) The Authority shall meet at such times and places, and shall observe such rules of procedure in regard to the transaction of business at its meetings (including quorum at such meetings) as may be specified by regulations.

(2) If the Chairperson is, for any reason, unable to attend a meeting of the Authority, any other Member chosen by the Members present from amongst themselves at the meeting shall preside at the meeting.

(3) All questions which come up before any meeting of the Authority shall be decided by a majority of votes of the Members present and voting, and, in the event of an equality of votes, the Chairperson, or in their absence, the person presiding, shall have a casting vote.

(4) Any Member who has any direct or indirect interest in any matter likely to come up for consideration at a meeting of the Authority shall, as soon as possible after the relevant circumstances have come to their knowledge, disclose in writing, the nature of their interest at such meeting and such disclosure shall be recorded in the proceedings of the Authority and such Member shall not take part in any deliberation or decision of the Authority with respect to that matter.

8. Administrative powers of Chairperson .—The Chairperson shall have the powers of general superintendence and direction in respect of all administrative matters of the Authority.

9. Offices and other employees of Authority .—

(1) The Authority may appoint such officers and other employees as it considers necessary for the efficient discharge of its functions under this Act.

(2) The salaries and allowances payable to, and other terms and conditions of service of, officers and other employees of the Authority appointed under sub-section (*1*) shall be such as may be specified by regulations.

CHAPTER III

POWERS AND FUNCTIONS OF AUTHORITY

10. Functions of Authority.—

(1) Subject to the provisions of this Act, it shall be the duty of the Authority to protect the interests of holders of virtual digital assets and to promote the development of, and to regulate the virtual digital asset industry, in accordance with sub-section (2).

(2) In order to fulfil the purposes set out under sub-section (1) above, the Authority may take any or all of the following measures--

(a) authorising and regulating the business of virtual digital asset service providers;

(b) regulating virtual digital asset markets;

(c) regulating cross-border transactions of virtual digital assets, in consultation with the Reserve Bank of India;

(d) promoting and regulating self-regulatory organisations;

(e) prescribing cybersecurity standards for virtual digital asset service providers;

(f) prohibiting fraudulent and unfair trade practices relating to virtual digital asset markets;

(g) promoting education of holders of virtual digital assets and training of persons associated with virtual digital assets service providers;

(h) calling for information from, undertaking inspection, and conducting inquiries and audits of virtual digital asset market participants, other persons associated with the virtual digital asset industry, and self-regulatory organisations in the virtual digital asset industry;

(i) calling for information and records from any person including any bank or any other authority or board or corporation established or constituted by or under any Central or State Act which, in the opinion of the Authority, shall be

relevant to any investigation or inquiry by the Authority in respect of any transaction in virtual digital assets;

(j) calling for information from, or furnishing information to, other authorities, whether in India or outside India, having functions similar to those of the Authority, in the matters relating to the prevention or detection of violations in respect of laws pertaining to virtual digital assets, subject to the provisions of other laws for the time being in force in this regard:

Provided that the Authority, for the purpose of furnishing any information to any authority outside India, may enter into an arrangement or agreement or understanding with such authority with the prior approval of the Central Government;

(k) levying fees or other charges for carrying out the purposes of this section;

(l) conducting research for the above purposes;

(m) calling from or furnishing to any such agencies, as may be specified by the Authority, such information as may be considered necessary by it for the efficient discharge of its functions;

(n) performing such other functions as may be prescribed.

(3) Notwithstanding anything contained in any other law for the time being in force while exercising the powers under (g) or clause (h) of sub-section (2), the Authority shall have the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908) while trying a suit, in respect of the following matters, namely:---

(a) the discovery and production of books of accounts and other documents, at such place and such time as may be specified by the Authority;

(b) summoning and enforcing the attendance of persons and examining them on oath;

(c) inspection of any books, registers and other documents of any virtual digital asset service provider at any place;

(d) issuing commissions for the examination of witnesses or documents.

(4) Without prejudice to the provisions contained in sub-sections (1), (2), and (3), and subject to the concerned person being granted the opportunity to be heard, the Authority may, by an order, for reasons to be recorded in writing, in the interests of general public or the virtual digital asset market, take any of the following measures, on completion of any investigation or inquiry, which shall be in place for such time period as may be necessary for the purpose of completion of the investigation or inquiry, namely:---

(a) suspend the trading of any virtual digital asset by any virtual digital asset service provider enabling such trading;

(b) restrain persons from accessing the virtual digital asset market and prohibit any person associated with the virtual digital asset market from buying, selling or dealing in virtual digital assets;

(c) suspend any office-bearer of any virtual digital asset service provider or self-regulatory organisation from holding such position;

(d) impound and retain the proceeds or virtual digital assets in respect of any transaction which is under investigation;

(e) direct any virtual digital asset service provider or any person associated with the virtual digital asset market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation:

Provided that the Authority shall, either before or after passing such orders, give an opportunity of hearing to such service providers or persons concerned.

(5) The Authority may, in addition to the above, specify by regulations the manner in which the functions may be performed by the Authority for carrying out the provisions of this section.

(6) The Authority shall ensure transparency while ensuring exercising its power and discharging its functions in line with the Pre Legislative Consultation Policy of the Government of India

CHAPTER IV

FINANCE, ACCOUNTS AND AUDIT

11. Grants by Central Government.— The Central Government may, after due appropriation made by Parliament by law on this behalf, make to the Authority grants of such sums of money as the Central Government may think fit for being utilised for the purposes of this Act.

12. Fund of Authority .—

(1) There shall be constituted a Fund to be called the Virtual Digital Assets Regulatory Authority Fund and there shall be credited thereto—

(a) all grants, fees and charges received by the Authority under this Act; and

(b) all sums received by the Authority from the sources as may be decided upon by the Central Government.

(2) The Fund shall be applied for meeting—

(a) the salaries, allowances and other remuneration of Members, officers and other employees of the Authority; and

(b) other expenses incurred by the Authority in connection with the discharge of its functions and for the purposes of this Act.

13. Accounts and audit .—

(1) The Authority shall maintain proper accounts and other relevant records and prepare an annual statement of accounts in such form as may be prescribed by the Central Government in consultation with the Comptroller and Auditor-General of India.

(2) The accounts of the Authority shall be audited by the Comptroller and Auditor-General of India at such intervals as may be specified by them and any expenditure incurred in connection with such audit shall be payable by the Authority to the Comptroller and Auditor-General of India.

(3) The Comptroller and Auditor-General of India and any other person appointed by them in connection with the audit of the accounts of the Authority shall have the same rights and privileges and authority in connection with such audit as the Comptroller and Auditor-General of India generally has in connection with the audit of the Government accounts and, in particular, shall have the right to demand the production of books, accounts, connected vouchers and other documents and papers and to inspect any of the offices of the Authority.

(4) The accounts of the Authority as certified by the Comptroller and Auditor-General of India or any other person appointed by them in this behalf together with the audit report thereon shall be forwarded annually to the Central Government and that Government shall cause the same to be laid before each House of Parliament.

14. Performance Review Committee .—

(1) The Authority shall constitute a Performance Review Committee, consisting of at least two Members of the Authority to review the functioning of the Authority, whether—

(a) it has adhered to the provisions of the applicable laws while exercising powers or performing functions under this Act;

(b) the regulations made by the Authority to give effect to the provisions of this Act promote transparency and best practices of governance; and

(c) the Authority is managing risks to its functioning in a reasonable manner.

(2) The Performance Review Committee shall make the review under sub-section (*1*) at least once every financial year, and submit a report of its findings to the Authority which shall forward a copy thereof along with action taken, if any, pursuant to such report to the Central Government within a period of three months from the date of receipt of the report.

(3) The Performance Review Committee shall maintain a system by which any person may submit to the committee, any incidence of—

(a) non-adherence of the provisions of any applicable law by the Authority;

(b) misappropriation of resources of the Authority by any person;

(c) abuse of powers of the Authority by any Member or employee of the Authority; or

(d) non-compliance of any decision of the Authority by any Member or employee of the Authority.

(4) The Authority shall make regulations governing the information to be provided to the Performance Review Committee, and the provision of adequate resources to enable the committee to discharge its functions under this section.

15. Maintenance of website.—

(1) The Authority shall maintain such website or any other universally accessible repository of electronic information as may be specified by regulations.

(2) All the regulations and orders issued by the Authority shall be published in its website or repository maintained under sub-section (*1*).

(3) The Authority shall review the quality of the website or the repository, based on international best practices, once every year and publish the report containing its findings with the annual report.

16. Returns and reports .—

(1) The Authority shall furnish to the Central Government at such time and in such form and manner as may be prescribed or as the Central Government may direct, such returns and statements and such particulars with regard to any proposed or existing programme for the development and regulation of virtual digital asset markets or virtual digital asset service providers, as the Central Government may, from time to time, require.

(2) Without prejudice to the provisions of sub-section (*1*), the Authority shall, within ninety days after the end of each financial year, submit to the Central Government, a report in such form, as may be prescribed, giving a true and full account of its activities, policies and programmes during the previous financial year.

(3) A copy of the report received under sub-section (*2*) shall be laid, as soon as may be after it is received, before each House of Parliament.

CHAPTER V

AUTHORISATION OF VIRTUAL DIGITAL ASSET SERVICE PROVIDERS

17. Virtual digital asset service providers not to operate without authorisation .— No person shall act as a virtual digital asset service provider except under and in accordance with an authorisation issued by the Authority under the provisions of this Act:

Provided that a person acting as a virtual digital asset service provider immediately before the establishment of the Authority for which no authorisation was necessary prior to such establishment, may continue to do so for a period of six months from such establishment or, if

it has made an application for such registration within the said period of three months, till the disposal of such application;

Provided further nothing contained in this section shall apply to any person whom the Authority may, after considering the interests of holders of virtual digital assets, virtual digital asset service providers generally, or for any other reason, by notification, exempt from the provisions of this section.

18. Application for authorisation .—

(1) Any person desirous of acting as a virtual digital asset service provider may apply to the Authority for an authorisation under this Act.

(2) An application under sub-section (*1*) shall be made in such form and in such manner and shall be accompanied by such fees as may be prescribed.

19. Inquiry by the Authority.— After the receipt of an application under section 18, and before an authorisation is issued under this Act, the Authority may make such inquiries as it may consider necessary for the purpose of satisfying itself about the genuineness of the particulars furnished by the applicant, its capacity to operate the virtual digital asset service provider, or for any other reason and when such an inquiry is conducted by any person authorised by it in this behalf, it may require a report from such person in respect of the inquiry.

20. Issue or refusal of authorisation.----

(1) The Authority may, if satisfied, after any inquiry under section 19 or otherwise, that the application is complete in all respects and that it conforms to the provisions of this Act and the regulations issue an authorisation for operating the virtual digital asset service provider under this Act having regard to standards prescribed under this Act, including:—

(a) the services proposed to be undertaken by it;

(b) if the applicant is an entity duly registered in the Republic of India as per Companies Act, 2013

(c) if the applicant meets the technical standards ;

(d) the financial status (including net worth), experience of management and integrity of the applicant;

(e) interests of consumers, including the terms and conditions governing their relationship with the virtual digital asset service provider; and

(f) such other factors as may be considered relevant by the Authority.

(2) An authorisation issued under sub-section (*1*) shall be in such form as may be prescribed and shall—

(a) state the date on which it takes effect;

(b) state the conditions subject to which the authorisation shall be in force;

(c) indicate the payment of fees, if any, to be paid for the authorisation to be in force;

(d) if it considers necessary, require the applicant to furnish such security for the proper conduct of the virtual digital asset service provider under the provisions of this Act;

(e) continue to be in force till the authorisation is revoked.

(3) Where the Authority considers that the application for authorisation should be refused, it shall give the applicant a written notice to that effect stating the reasons for the refusal:

Provided that no such application shall be refused unless the applicant is given a reasonable opportunity of being heard.

(4) Every non-deficient application for authorisation shall be processed by the Authority as soon as possible and an endeavour shall be made to dispose of such application within two months from the date of filing of such application.

21. Revocation of authorisation.—

(1) If a virtual digital asset service provider,—

(a) does not comply with the regulations, or

(b) fails to comply with the orders or directions issued by the Authority, or

(c) operates contrary to the conditions subject to which the authorisation was issued,

the Authority may, by order, revoke the authorisation given to such virtual digital asset service provider under this Act:

Provided that no order of revocation under sub-section (*1*) shall be made—

(a) except after giving the virtual digital asset service provider a reasonable opportunity of being heard; and

(b) without prejudice to the direction of the Authority to the virtual digital asset service provider that the operation of the virtual digital asset service provider shall not be carried out till the order of revocation is issued.

(2) The order of revocation issued under sub-section (1) shall include necessary provisions to protect and safeguard the interests of persons affected by such order of revocation.

(3) Where a virtual digital asset service provider becomes insolvent or dissolved or wound up, such virtual digital asset service provider shall inform that fact to the Authority and thereupon the Authority shall take such steps as deemed necessary to revoke the authorisation issued under this Act to such virtual digital asset service provider.

CHAPTER VI

REGULATION AND SUPERVISION BY THE AUTHORITY

22. **Power to determine standards .—** The Authority may, from time to time, prescribe the manner of, and the standards for, the functioning of any virtual digital asset service provider or class of virtual digital asset service providers, having regard to the interests of virtual digital asset service providers and holders of virtual digital assets.

The Authority shall ensure transparency while exercising this power, in line with the Pre Legislative Consultation Policy of the Government of India

23. **Requirement for obtaining prior approval in case of transfer of business activities or in case of a Change of Control of the virtual digital asset service provider —**

(1) No virtual digital asset service provider shall effect any material change in the structure or the operation of the virtual digital asset service provider without the prior approval of the Authority. Provided that, a "change of control" shall mean any event in which more than [50%] of the voting shares or equity interests of the virtual digital asset service provider offering services, are directly or indirectly transferred (including by way of a merger, consolidation, or other corporate reorganization).

(2) Where the Authority has any objection to the proposed change for any reason, it shall communicate such objection to the virtual digital asset service provider within two weeks of receipt of the intimation of the proposed changes from the virtual digital asset service provider, failing which the proposed changes shall be deemed to be approved.

(3) The virtual digital asset service provider shall, within a period of two weeks of the receipt of the objections from the Authority forward its comments to the Authority and the proposed changes may be effected only after the receipt of approval from the Authority.

24. **Power to call for returns, documents or other information .—**The Authority may call for from any virtual digital asset service provider such returns or documents as it may require or other information in regard to its operation at such intervals, in such form and in such manner, as the Authority may require from time to time or as may be prescribed and such order shall be complied with.

25. **Access to information .—**The Authority shall have the right to access any information relating to the operation of any virtual digital asset service provider and such virtual digital asset service provider shall provide access to such information to the Authority, provided a written intimation is given to the service provider, as deemed fit. Provided further that the Authority shall not ask for or collect information with respect to storage, management or operation of private keys and any other means of effective control of virtual digital assets held by the virtual digital asset service provider.

26. **Power to enter and inspect .—**Any officer of the Authority duly authorised by it in writing in this behalf, may, for ensuring compliance with the provisions of this Act or any

regulations, enter any premises where a virtual digital asset service provider is being operated and may inspect any equipment, including any computer system or other documents situated at such premises and call upon any employee of such virtual digital asset service provider or any other person working in such premises to furnish such information or documents as may be required by such officer, provided a written intimation is given to the service provider, as deemed fit.

27. Information, etc., to be confidential .—

(1) Subject to the provisions of sub-section (*2*), any document or information obtained by the Authority under sections 24 to 26 (both inclusive) shall be kept confidential.

(2) Notwithstanding anything contained in sub-section (*1*), the Authority may disclose any document or information obtained by it under sections 24 to 26 (both inclusive) to any person to whom the disclosure of such document or information is considered necessary for protecting the integrity, effectiveness or security of the virtual digital asset markets or in public interest, and such person shall be bound to keep such document or information confidential.

28. Power to carry out audit and inspection.— The Authority may, for the purpose of carrying out its functions under this Act, conduct or get conducted audits and inspections of a virtual digital asset service provider or participants thereof and it shall be the duty of the virtual digital asset service providers to assist the Authority to carry out such audit or inspection, as the case may be.

29. Power to issue directions.—(1) Where the Authority is of the opinion that,—

(a) a virtual digital asset service provider is engaging in, or is about to engage in, any act, omission or course of conduct that results, or is likely to result, in systemic risk being inadequately controlled; or

(b) any action under clause (*a*) is likely to adversely affect the holders of virtual digital assets in the country,

the Authority may issue directions in writing to such virtual digital asset service provider requiring it, within such time as the Authority may specify—

(i) to cease and desist from engaging in the act, omission or course of conduct; or

(ii) to perform such acts as may be necessary, in the opinion of the Authority, to remedy the situation.

(c) Without prejudice to the provisions mentioned above, the Authority will be bound by the the provisions prescribed by The Limitations Act, 1963.

30. Power of Authority to give directions generally.—Without prejudice to the provisions of the foregoing, the Authority may, if it is satisfied that for the purpose of enabling it to regulate any virtual digital asset service provider in particular or virtual digital asset service providers generally, or in public interest, it is necessary so to do, lay down policies relating to the regulation of virtual digital asset service providers and give such directions in writing as it may consider necessary to virtual digital asset service providers.

31. **Directions of Authority to be complied with .—**Every person to whom a direction has been issued by the Authority under this Act shall comply with such direction without any delay and a report of compliance shall be furnished to the Authority within the time allowed by it.

CHAPTER VII

RIGHTS AND DUTIES OF A VIRTUAL DIGITAL ASSET SERVICE PROVIDER

32. **Virtual digital asset service provider to act in accordance with the Act, regulations, etc.—** Every virtual digital asset service provider shall operate in accordance with the provisions of this Act, the regulations hereunder, the conditions subject to which the authorisation is issued, and the directions given by the Authority from time to time.

33. **Duties of a virtual digital asset service providers.—** Without prejudice to the duties and obligations set out elsewhere in this Act, -

(1) Every virtual digital asset service provider shall disclose to its customers the terms and conditions of its service.

34. Every virtual digital asset service provider shall provide its customers with a readily available means of grievance redressal. **Protection of virtual digital assets and funds of customers.—**

(1) The Authority, in public interest or in the interest of holders of virtual digital assets or to prevent the affairs of one or more virtual digital asset service providers from being conducted in a manner prejudicial to the interests of its customers, require any virtual digital asset service provider or class of virtual digital asset service providers

(a) to maintain liquid assets, in such manner and form as it may specify from time to time, of an amount equal to such percentage of the funds or other assets held by the virtual digital asset service provider of its customers and remaining outstanding, as may be specified by the Authority from time to time, provided that the Authority may specify different percentages of liquid assets and the manner and forms of maintaining liquid assets for different categories of virtual digital asset service providers.

(2) The liquid assets and customer funds maintained in accordance with sub-section (*1*) shall not be utilised for any purpose other than for discharging the liabilities arising on account of the usage of the virtual digital asset service provider's facilities by the customers or for repaying to the customers or for such other purpose as may be specified by the Authority from time to time.

(3) Notwithstanding anything contained in the Banking Regulation Act, 1949 (10 of 1949), or the Companies Act, 1956 (1 of 1956) or the Companies Act, 2013 (18 of 2013) or the Insolvency and Bankruptcy Code, 2016 or any other law for the time being in force, the customers referred to under sub-section (2) shall have a first and paramount charge on customer funds maintained in accordance with sub-section (*1*) and the liquidator or receiver or assignee (by whatever name called) of the virtual digital asset service provider, whether appointed as provisional or otherwise, shall not utilise the said customer funds for any other purposes until all such customers are

paid in full or adequate provision is made therefor. Provided that customers referred to in sub-section (2) shall have a charge over the liquid assets maintained by the virtual asset service provider in accordance with sub-section (1), to the extent that the customer funds are insufficient to fully satisfy the liabilities owed by such virtual digital service provider to such customers.

(4) Virtual digital asset service providers may hold and maintain the following types of insurance adequate to the size and complexity of the business and virtual digital asset activities and in the manner specified by the Authority in its authorisation: (a) professional indemnity insurance; (b) directors' and officers' insurance; (c) cybersecurity insurance, commercial crime insurance or similar types of insurance to secure all virtual digital assets stored in virtual digital asset wallets; and (d) any other type of insurance as assessed by the Authority to be appropriate for a virtual digital asset service provider's business and activities and stipulated in the conditions to its authorisation. Such insurance must be provided by an insurer granted a certificate of registration by the Insurance Regulatory and Development Authority of India established under Section 3 of the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999).

CHAPTER VIII

PENALTIES AND ADJUDICATION

35. Penalties.—

(1) Where a person contravenes the provisions of section 17 of this Act, they shall be liable to a penalty which may extend to XXX rupees and to a further penalty which may extend to XXX rupees for every day after the first during which the contravention or failure to comply continues.

(2) Where a person fails to comply with the terms and conditions subject to which the authorisation has been issued under section 20, they shall be liable to a penalty which may extend to XXX rupees and to a further penalty which may extend to XXX rupees for every day after the first during which the contravention or failure to comply continues.

(3) Whoever in any application for authorisation or in any return or other document or on any information required to be furnished by or under, or for the purpose of, any provision of this Act, wilfully makes a statement which is false in any material particular, knowing it to be false or wilfully omits to make a material statement, shall be liable to a penalty which shall not be less than XXX rupees and which may extend to XXX rupees.

(4) If any person fails to produce any statement, information, returns or other documents, or to furnish any statement, information, returns or other documents, which under section 24 or under section 25, it is their duty to furnish or to answer any question relating to the operation of a virtual digital asset service provider which is required by an officer making inspection under section 26, they shall be liable to a penalty which may extend to xxx rupees in respect of each contravention and if they persist in such refusal, to a further penalty which may extend to xxx rupees for every day for which the contravention continues.

(5) Where a direction issued under this Act is not complied with within the period stipulated by the Authority or where no such period is stipulated, within a reasonable time, the virtual digital asset service provider which has failed to comply with the direction or to pay the penalty shall be liable to pay a penalty which may extend to XXX rupees or with both and where the failure to comply with the direction continues, with a further penalty which may extend to XXX rupees for every day after the first during which the contravention continues.

(6) If any provision of this Act is contravened, or if any default is made in complying with any other requirement of this Act, or of any regulation, order or direction made or given or condition imposed thereunder and in respect of which no penalty has been specified, then, the person guilty of such contravention or default, as the case may be, shall be liable to pay a penalty which may extend to XXX rupees and where a contravention or default is a continuing one, with a further penalty which may extend to XXX rupees for every day after the first during which the contravention or default continues.

36. Power to adjudicate.—

(1) For the purpose of adjudging under section 36, the Authority may appoint any officer not below the rank of a Division Chief to be an adjudicating officer for holding an inquiry in the prescribed manner after giving any person concerned a reasonable opportunity of being heard for the purpose of imposing any penalty.

(2) While holding an inquiry the adjudicating officer shall have power to summon and enforce the attendance of any person acquainted with the facts and circumstances of the case to give evidence or to produce any document which in the opinion of the adjudicating officer, may be useful for or relevant to the subject matter of the inquiry and if, on such inquiry, they are satisfied that the person has failed to comply with the provisions of any of the sections specified in sub-section (1), they may impose such penalty as they think fit in accordance with the provisions of section 35.

(3) The Authority may call for and examine the record of any proceedings under this section and if it considers that the order passed by the adjudicating officer is erroneous to the extent it is not in the interests of the virtual digital asset market, it may, after making or causing to be made such inquiry as it deems necessary, pass an order enhancing the quantum of penalty, if the circumstances of the case so justify:

Provided that no such order shall be passed unless the person concerned has been given an opportunity of being heard in the matter:

Provided further that nothing contained in this sub-section shall be applicable after an expiry of a period of three months from the date of the order passed by the adjudicating officer or disposal of the appeal under section 40, whichever is earlier.

37. Factors to be taken into account while adjudging quantum of penalty.—

While adjudging the quantum of penalty under section 35, the adjudicating officer shall have due regard to the following factors, namely:—

(a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;

(b) the amount of loss caused to investors or other members of the general public as a result of the default; and

(c) the repetitive nature of the default.

38. Settlement of administrative and civil proceedings.—

(1) Notwithstanding anything contained in any other law for the time being in force, any person, against whom any proceedings have been initiated or may be initiated under section 10, or 35, may file an application in writing to the Authority proposing for settlement of the proceedings initiated or to be initiated for the alleged defaults.

(2) The Authority may, after taking into consideration the nature, gravity and impact of defaults, agree to the proposal for settlement, on payment of such sum by the defaulter or on such other terms as may be determined by the Authority in accordance with the regulations made under this Act.

(3) The settlement proceedings under this section shall be conducted in accordance with the procedure specified in the regulations made under this Act.

(4) No appeal shall lie under section 40 against any order passed by the Authority under this section.

(5) All settlement amounts, excluding the disgorgement amount and legal costs, realised under this Act shall be credited to the Consolidated Fund of India.

39. Crediting sums realised by way of penalties to Consolidated Fund of India.— All sums realised by way of penalties under this Act shall be credited to the Consolidated Fund of India.

40. Appeal to Securities Appellate Tribunal.—

(1) Any person aggrieved—

(a) by any decision or order of the Authority made under this Act, the rules or regulations made thereunder; or

(b) by any decision or order made by the Authority by way of adjudication under this Act,

may prefer an appeal to the Securities Appellate Tribunal having jurisdiction in the matter.

(2) Every appeal made under sub-section *(1)* shall be filed within a period of forty-five days from the date on which a copy of the order made by the Authority is received by them and it shall be in such a form and be accompanied by such fees as may be prescribed:

Provided that the Securities Appellate Tribunal may entertain an appeal after the expiry of the said period of forty-five days if it is satisfied that there was sufficient cause for not filing it within that period.

(3) On receipt of an appeal under sub-section *(1)*, the Securities Appellate Tribunal] may, after giving parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, conforming, modifying or setting aside the order appealed against.

(4) The Securities Appellate Tribunal shall make available a copy of order made by it to the Authority and parties.

(5) The appeal filed before the Securities Appellate Tribunal under sub-section *(1)* shall be dealt with by it as expeditiously as possible and endeavour shall be made by it to dispose of the appeal finally within six months from the date of receipt of appeal.

(6) The procedure for filing and disposing of an appeal shall be such as may be prescribed.

(7) The provision contained in section 15U, section 15V, section 15W, section 15Y and section 15Z of the Securities and Exchange Board of India Act, 1992 (15 of 1992) shall apply to the appeals arising out of the provisions of this Act, as they apply to the appeals under the Securities and Exchange Board of India Act, 1992 (15 of 1992).

CHAPTER IX

MISCELLANEOUS

41. Delegation of powers .—

(1) The Authority may, by general or special order in writing, delegate to any Member or officer of the Authority subject to such conditions, if any, as may be specified in the order, such of its powers and functions under this Act (except the powers under section 27) as it may deem necessary.

(2) The Authority may, by a general or special order in writing, also form committees of the Members and delegate to them the powers and functions of the Authority, as may be specified by regulations.

42. Members, officers and employees of the Authority to be public servants.—The Members, officers and employees of the Authority shall be deemed, when acting or purporting to act in pursuance of any of the provisions of this Act, to be public servants within the meaning of section 21 of the Indian Penal Code (45 of 1860).

43. Protection of action taken in good faith.—No suit, prosecution or other legal proceedings shall lie against the Central Government or the Authority or its Members, officers or other employees, for anything which is done, or intended to be done, in good faith under this Act.

44. Exemption from tax.—Nothing contained in any other law or enactment for the time being in force, in relation to taxation, including the Income-tax Act,1961 (43 of 1961), shall make

the Authority liable to pay income-tax or any other tax or duty with respect to its income, services or profits or gains.

45. Power to make rules.—

(1) The Central Government may, by notification, make rules for carrying out the provisions of this Act which provide for all or any of the following matters, namely:—

(a) the composition and the manner of constitution of the Selection Committee under sub-section (*5*) of section 4;

(b) the salaries and allowances and other terms and conditions of service of Members under sub-section (*2*) of section 5;

(c) other functions to be performed by the Authority under clause (*m*) of sub-section (*2*) of section 10;

(d) the form in which the accounts and other relevant records to be maintained and annual statement of accounts to be furnished under sub-section (*1*) of section 14;

(e) the form and manner of furnishing of returns and statements and other particulars under sub-section (*1*) of section 16;

(f) the form of annual report of activities, policies and programmes under sub-section (*2*) of section 16;

(g) the form and manner in which an application for authorisation for acting as a virtual digital asset service provider shall be made and the fees which shall accompany such application under sub-section (*2*) of section 18;

(h) the form in which an authorisation to act as a virtual digital asset service provider under this Act shall be issued under sub-section (*2*) of section 20;

(i) the intervals at which and the form and manner in which the information or returns required by the Authority shall be furnished under section 24;

(j) the form in which an appeal may be preferred under sub-section (2) of section 40 and the fee payable in respect of such appeal and the procedure for filing and disposing of an appeal under sub-section (6) of section 40;

(k) any other matter which is to be, or may be, prescribed.

46. Power to make regulations .—

(1) The Authority may, by notification, make regulations consistent with this Act and the rules made thereunder for carrying out the provisions of this Act.

(2) In particular, and without prejudice to the generality of the foregoing power, such regulations may provide for all or any of the following matters, namely:—

(a) the time and place of meetings and the rules of procedure in regard to transaction of business at such meetings under sub-section (*1*) of section 7;

(b) the salaries and allowances and other terms and conditions of service of officers and other employees of Authority under sub-section (*2*) of section 9;

(c) the manner in which the Authority may perform its functions under sub-section (*5*) of section 10;

(d) the manner of providing information to the Performance Review Committee under sub-section (*4*) of section 14;

(e) the maintenance of the website or any other universally accessible repository of electronic information under sub-section (*1*) of section 15;

(f) the terms determined by the Authority for settlement of proceedings under sub-section (2) and the procedure for conducting of settlement proceedings under sub-section (3) of section 38;

(g) the powers and functions of the Authority which may be delegated under sub-section (*2*) of section 41;

(h) any other matter which is required to be or may be, specified by regulations.

47. Rules and regulations to be laid before Parliament .—Every rule and every regulation made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or regulation or both Houses agree that the rule or regulation should not be made, the rule or regulation shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule or regulation.

48. Overriding effect .—The provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act.

49. Power to modify provisions of other enactments in relation to virtual digital assets .—

(1) The Central Government may, by notification, direct that any of the provisions of any other Central Act or any rules or regulations made thereunder or any notification or order issued or direction given thereunder (other than the provisions relating to making of the rules or regulations) specified in the notification—

(a) shall not apply to virtual digital assets or virtual digital asset service providers, as the case may be; or

(b) shall apply to virtual digital assets or virtual digital asset service providers, as the case may be, with such exceptions, modifications and adaptations, as may be specified in the notification.

(2) A copy of every notification proposed to be issued under sub-section (*1*), shall be laid in draft before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in disapproving the issue of the notification or both Houses agree in making any modification in the notification, the notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses.

50. Power to remove difficulties .

(1) If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order, published in the Official Gazette, make such provisions not inconsistent with the provisions of this Act as may appear to be necessary for removing the difficulty:

Provided that no order shall be made under this section after the expiry of five years from the commencement of this Act.

(2) Every order made under this section shall be laid, as soon as may be after it is made, before each House of Parliament.

51. Amendment to certain enactments .—The enactments specified in the First Schedule shall be amended in the manner specified therein.

THE FIRST SCHEDULE

[*See* **section 51**]

AMENDMENT TO CERTAIN ENACTMENTS

1. Amendment of clause (h) of section 2 of the Foreign Exchange Management Act, 1999 (42 of 1999).— In clause (h) of section 2, after the words "as may be notified by the Reserve Bank", the words "but does not include a virtual digital asset as defined under the Virtual Digital Assets Regulatory Authority Act, 2024 (__ of 2024)" shall be inserted.

2. Amendment of clause (47A) of section 2 of the Income-tax Act, 1961 (43 of 1961).— For clause (47A) of section 2, the following section shall be substituted, namely:
""virtual digital asset" shall have the meaning assigned to it in sub-section (10) of section 2 of the Virtual Digital Assets Regulatory Authority Act, 2024 (__ of 2024)".

II. APPROACH PAPER

1. Introduction: The Value of Public Blockchain Networks

"*Blockchain networks are the only known technology that can reestablish an open, democratic internet*", argues Chris Dixon, Partner at Andreessen Horowitz, the venture capital firm, in his acclaimed recent book, 'Read Write Own'.[13]

Dixon makes out a compelling case for this proposition, in the following terms:

- The internet revolutionised the world similar to earlier technological breakthroughs like the printing press, the steam engine, and electricity. Public blockchain networks can preserve the open and democratic nature of the internet and prevent its over-centralisation.

- The internet has three eras: 'read' (the internet as a source of information) ('Web1') and 'read-write' (the internet as a source of information and tool for publishing) ('Web2') till today; and, going forward, 'read-write-own' (where a user can become a network stakeholder, gaining control and value and reaping the benefits of their own content and contributions, and paying less 'rent' to centralised businesses) ('Web3').

- Blockchain networks and as part of them, tokens / virtual digital assets, are essential to achieve such decentralised ownership. Since blockchain networks essentially work as one computer system running on multiple devices worldwide, tokens also act as the fuel powering the blockchain network, by acting as a valuable incentive to participants which maintain the network. A permissionless blockchain system hence cannot function effectively without tokens.

- Tokens enable true ownership of digital elements (e.g., from network software code to art to in-game items) whereas in traditional or Web2 networks, users are dependent on the business which owns the platform giving them a license to the digital elements.

- Perception about blockchain networks is often tainted by discussion about speculation, trading, and price movements (i.e., the 'casino' aspect). However, attention to such discussions bypasses the real use-case of tokens (or, the 'computer' aspect), which is to power useful decentralised software infrastructure and applications, and hence bring value to the network 'edges' i.e., users and developers.

- At the same time, efficient markets for tokens, and responsible market participants like exchanges, are essential to a successful blockchain ecosystem. Users wishing to use a blockchain network need to be able access a well-functioning and liquid market to purchase the token timely and at a fair price, and users who have earned incentives in such tokens similarly need to be able to exchange the same for sovereign/fiat currency.

- The fundamental goals of regulators and blockchain developers are aligned – to empower the public at large by reducing the disadvantages of centralisation.

[13] Chris Dixon, "Read Write Own: Building the Next Era of the Internet", Random House New York (2024).

We firmly believe that this is true. There needs to be a paradigm shift in the perception of the blockchain and virtual digital asset ecosystem from 'casino' to 'computer'. While various Indian Government reports (including by the Ministry of Finance, the Ministry of Electronics and Information Technology (**MeitY**) and NITI Aayog) and international perspectives recognize the importance of blockchain technology, the critical linkage of virtual digital assets with this technology, has not yet been appreciated.

As mentioned above, virtual digital assets act as the underlying fuel to make blockchain networks work in a decentralised manner. This view is well accepted by leading scholars worldwide, including Dr. Arvind Narayanan (Princeton University)[14] and Dr. Christian Catalini (Massachusetts Institute of Technology (**MIT**)).[15] In fact, the renowned MIT Professor Dr. Silvio Micali, a winner of the Turing Award, the highest award in computer science, has developed a blockchain network powered by virtual digital assets.[16] The role of virtual digital assets as an incentive mechanism has been lucidly explained by Andreas Antonopolous, the author of the well-known works, 'Mastering Bitcoin' and 'Mastering Ethereum', among others:

> "*The reason we use a blockchain is to achieve decentralisation. …The best mechanism we've found so far for decentralising the process of validation is by having a consensus algorithm that depends on competition … In order to have competition, you need risk and reward. In order to have a reward that is meaningful, you need an intrinsic token. You need something of value that people are trying to get, which keeps them playing fair. If you don't have something of value, you don't have a basis for that competition. Without a basis for that competition, you don't have security. … Without decentralisation, there's no point in doing a blockchain. You might as well use a replicated database.*"[17]

In other words, where traditional networks incentivize a centralised platform gatekeeper with platform fees under a contract, blockchain networks require tokens to incentivize all the network participants across the world in an automated manner. This automation at the protocol level (e.g., mining or staking rewards, gas fees, etc.) obviates the need for all participants to contract with each other, resulting in a system which is open to all, much like the internet. Without the token incentive mechanism, it would be more akin to the intranet of one or more organisations, rather than an open and neutral internet. Moreover, as mentioned above, the virtual digital assets of a blockchain network allow the participants to fully own various digital elements and participate in the economic upside of the network, whereas in traditional networks, only the platform operator owns such elements (simply licensing the content to users) and captures the economic upside.

Significantly, various government and regulated sector use-cases of blockchain technology in India and abroad are based on public blockchain networks which are powered by virtual digital assets. These include:

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[14] 'Bitcoin's Academic Pedigree', Arvind Narayanan and Jeremy Clark (Association for Computing Machinery Queue 2017) (https://queue.acm.org/detail.cfm?id=3136559)

[15] Dr. Christian Catalini and Joshua S. Gans, Some Simple Economics of the Blockchain (2019). Rotman School of Management Working Paper No. 2874598, MIT Sloan Research Paper No. 5191-16 (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2874598)

[16] https://algorandtechnologies.com/our-founder

[17] Extract of the auto-generated transcript of the video by Andreas Antonopoulos titled 'Bitcoin Q&A: "Blockchain, not Bitcoin"' available at https://www.youtube.com/watch?v=r2f0HlaRdgo.

- The Maharashtra State Board of Skill Development's certificate verification system, powered by the Polygon blockchain.[18] In line with the concepts discussed above, it allows students to own their digital educational certificates and verify them online, authenticated by the public blockchain.

- The Government of Maharashtra uses the Polygon blockchain to issue verifiable caste certificates to citizens residing in certain districts,[19] as well as verify Covid test results.[20]

- The Telangana State Civil Supplies Department, Government of Telangana used a Polygon-based blockchain tracking system for enhanced traceability in the department's paddy supply distribution system.[21]

- Firozabad Police (Uttar Pradesh Police) deployed a system for persons to track police complaints using the Polygon blockchain.[22]

- Internationally, the Monetary Authority of Singapore's Project Guardian saw industry participants use the Polygon blockchain in a pilot to carry out a live cross-currency transaction involving tokenised Japanese Yen and Singapore Dollar deposits.[23]

- Major industry funds investing in U.S. Government securities have recently deployed their funds "on-chain", and in a regulated manner, such that trades of fund units would reflect on the Ethereum and Stellar blockchains.[24] Over USD 1 billion (~INR 8,500 crore) in U.S. Treasury notes have been stated to be tokenized through public blockchains.[25]

In each of the above examples, virtual digital assets are necessary to power the underlying transactions (which include actions like submission of verification requests) on the blockchain network.

The Polygon blockchain, which features in many of the above illustrations, was started in 2017 by three Indian co-founders. By creating a scalability platform that supported faster, cost effective applications while remaining on the Ethereum network, Polygon has become a pivotal player in the blockchain ecosystem globally. The success story of Polygon illustrates the 'computer' aspect of virtual digital assets and blockchain technology, which often takes place steadily behind the scenes, as opposed to the 'casino' element, which is often the

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[18] https://msbsvet.edu.in/legitdoc22/index.html.

[19] https://indianexpress.com/article/technology/crypto/how-maharashtra-is-using-polygon-blockchain-to-issue-verifiable-caste-certificates-7843949/

[20] https://polygon.technology/blog/10-real-world-examples-of-blockchain-use-in-the-public-sector; https://block.dmrr.mahaonline.gov.in/report?id=2e63e5ad7e1ae7f4fa8568e8cdb49dec4ac701f9469e7289ba84d1ddb2dc385b

[21] https://polygon.technology/blog/10-real-world-examples-of-blockchain-use-in-the-public-sector; https://statwig.com/caseStudy-gunny-bags.html

[22] https://www.indiatoday.in/cryptocurrency/story/firozabad-police-to-use-polygon-blockchain-to-register-complain-2284524-2022-10-12

[23] https://www.mas.gov.sg/news/media-releases/2022/first-industry-pilot-for-digital-asset-and-decentralised-finance-goes-live#2; https://www.bloomberg.com/news/articles/2022-11-02/jpmorgan-executes-its-first-defi-trade-using-public-blockchain?embedded-checkout=true

[24] https://www.sec.gov/Archives/edgar/data/1786958/000137949121001250/filing222856581.htm; https://www.businesswire.com/news/home/20240320771318/en/

[25] https://www.coindesk.com/markets/2024/03/28/over-1b-in-us-treasury-notes-has-been-tokenized-on-public-blockchains/

subject of short-term attention and sensationalism. It also demonstrates how India can lead the way in blockchain development, the way it has on traditional software development.

In 2021, MeitY released the National Strategy on Blockchain[26], setting out its vision for the adoption of blockchain technology in various sectors such as healthcare, agriculture, finance, voting and e-governance, and building a national-level infrastructure for blockchain. In 2020, a report by NITI Aayog discussed various use-cases of blockchain technology including creating a system to manage land record transfer and ownership, self-regulation of the pharmaceutical sector through blockchain enabled trust, anti-fraud identity intelligence blockchain solution for educational certificates, and supply chain management.[27]

2. Types of Virtual Digital Assets and Market Participants

The terms 'crypto', 'crypto-assets', 'digital assets', 'tokens' (specifically, blockchain-based tokens), 'virtual assets', and 'virtual digital assets' are often used interchangeably, but they may have distinct implications depending on the context. In India, the term 'virtual digital asset' began to be used after the Finance Act, 2022 introduced the term. Globally, other terminology including 'crypto-asset' (e.g., used by EU and United Kingdom (**UK**) regulators) and 'virtual asset' (used by the Financial Action Task Force (**FATF**)), are more common. Regardless of terminology, there is no single, universally accepted definition of this concept. The Financial Stability Board (**FSB**) defines crypto-assets as "*a type of private digital asset that depends primarily on cryptography and distributed ledger or similar technology*".[28]

It is important to recognize, especially in the context of regulatory and policy discussions, that there are various types of virtual digital assets, with different legal and technical characteristics. In fact, the latest data from the market research portal coinmarketcap.com shows that there are over 10,000 fungible virtual digital assets in circulation today.

Characteristics such as the underlying consensus mechanism used (e.g., proof-of-work mining in Bitcoin or proof-of-stake validation in Ethereum), whether there is an underlying real-world asset, quantum of supply, mode of issuance, ability of redemption, transferability and fungibility, and programmability, among several others, distinguish various types of virtual digital assets. While each virtual digital asset is unique, they are often characterised into utility tokens, security tokens, and payment tokens.[29] Each can have different regulatory implications; the draft bill subsequently proposed, similar to VARA, wherein the Authority has the requisite powers of determination as to the nature of the virtual digital asset but the Authority shall have the sole jurisdiction to regulate all virtual digital assets. Non-fungible tokens (**NFTs**) are another type of virtual digital asset where each token in the standard is unique, allowing for NFTs to be able to represent unique digital or physical items (e.g., artwork, real estate, etc.).

A thoughtful regulatory approach would need to grapple with these different attributes rather than treat all virtual digital assets alike. These distinctions have been recognized in

[26] https://www.meity.gov.in/writereaddata/files/National_BCT_Strategy.pdf
[27] https://www.niti.gov.in/sites/default/files/2020-01/Blockchain_The_India_Strategy_Part_I.pdf
[28] https://www.fsb.org/work-of-the-fsb/financial-innovation-and-structural-change/crypto-assets-and-global-stablecoins/#:~:text=Crypto%2Dassets%20are%20a%20type,distributed%20ledger%20or%20similar%20technology
[29] https://www.imf.org/en/Publications/WP/Issues/2023/07/28/Digital-Tokens-A-Legal-Perspective-537041

jurisdictions globally, including the EU, Japan and Singapore, as well as by various multilateral organisations.

In addition to the diversity of virtual digital assets, another aspect that is crucial for regulators to consider is the differing roles of various participants in the ecosystem. Some, like exchanges, brokers and custodial wallet providers, play a market participant role, resulting in the need for regulation to ensure consumer protection. Others act on their own behalf and do not intermediate any transactions (e.g., users, proprietary traders, blockchain validators, and software application developers).

Blockchain market activities can broadly be subclassified into three categories as proposed by Cambridge Centre for Alternative Finance: (i) primary market activities, focused on issuance of virtual digital assets (e.g., issuers and underwriters), (ii) secondary market activities, focused on secondary market transactions (e.g., exchanges, brokers and custody providers) and (iii) ancillary activities (e.g., cybersecurity, data analytics, Know Your Customer (**KYC**) / Anti-Money Laundering (**AML**) services, and legal and accounting services).[30]

Specifically, the key participants in the blockchain ecosystem include:

(i) Users: These are the end-users of the network. They may execute transactions on their own behalf and in some cases may also act as blockchain validators (discussed below). They may use blockchain networks for a variety of purposes, including NFT creation, interacting with content platforms (e.g., social media, streaming, blogs, or gaming platforms with a blockchain layer), file storage and sharing, decentralised voting, trading, and others.

(ii) Blockchain developers: Since blockchain networks are created with software code, blockchain developers are key to the ecosystem. Such code is generally available on an open-source basis. The Polygon team falls in this category, as do other pioneering developers like Vitalik Buterin (co-founder, Ethereum). Public blockchain code is generally open source. To interact meaningfully with blockchain networks e.g., for paying gas fees for transactions, or liquidating their blockchain rewards, software developers need access to an efficient and liquid virtual digital asset market.

(iii) Blockchain validators: Validators are the blockchain network participants who maintain the integrity and security of the network and validate transactions on the network and keep it running, in exchange for rewards and fees in the blockchain's native virtual digital asset. They replace centralised gatekeepers in centralised networks. Such validation occurs through a cryptographic process known as a consensus mechanism, which varies across blockchains. For instance, in Bitcoin, the consensus mechanism is proof-of-work and validators are known as 'miners'. Miners expend computing resources to solve cryptographic problems, which in turn validate transactions. In proof-of-stake systems, e.g., Ethereum, validators are chosen to validate transactions based on the number of tokens they have 'staked' as collateral to the network. The more tokens a validator stakes, the higher their chances of being selected to validate transactions.

[30] Jason G. Allen, 'Legal and Regulatory Considerations for Digital Assets' (Cambridge Centre for Alternate Finance, 2020), https://www.jbs.cam.ac.uk/wp-content/uploads/2020/10/2020-ccaf-legal-regulatory-considerations-report.pdf

(iv) Application developers: Once the underlying protocol networks are developed and functioning, their deployment in useful applications is where the value-addition of blockchain networks is seen. Such applications can include decentralised, blockchain-based platforms for social media, e-commerce, streaming, blogging, gaming, file storage and sharing, credentialing, real asset tokenisation, voting, or any other type of internet platform conceivable.

(v) Exchanges, brokers and on- and off-ramp platforms: Virtual digital asset exchanges enable users to buy virtual digital assets with fiat currency, sell their virtual digital assets in exchange for fiat currency, and/or exchange one type of virtual digital assets with another. Brokers generally convey the trade orders of users onto exchanges. Generally, users may choose to use either broking platforms or connect directly with an exchange. On- and off-ramp platforms enable users to use their fiat currency to connect with blockchain applications, whereby a user can, for instance, use their fiat currency payment instrument to avail of a blockchain network service, without having to first purchase tokens on an exchange and then withdraw them to use the service. They help blockchain application developers in acquiring a wider base of users who do not already hold virtual digital assets.

(vi) Custody service providers: They provide users with custodial services such as wallets for holding, storing and transferring virtual digital assets. A custodial wallet provides the advantage of simplicity and convenience in the user experience, while users of non-custodial wallets may need to be more tech-savvy and ensure that their wallets' private keys remain secure. Non-custodial wallets, however, obviate the need to trust the wallet service provider with the value of the virtual digital assets stored in the wallet.

(vii) Market makers and high-volume traders: These participants generally trade on their own behalf, and given the high volume of their trades, help create liquidity and price discovery in the market, which in turn helps retail participants like users and software developers get the best value for virtual digital assets on a timely basis.

(viii) Multi-function market participants (**MFIs**): They are individual entities, or groups of affiliated entities, that combine a broad range of virtual digital asset services, products, and functions typically centered around the operation of a trading platform. Many multi-function market participants have proprietary trading and investment functions, while some are also involved in issuing, promoting, and distributing virtual digital assets or related products.

Which participants and assets should be regulated?

With such a variety of participants, it is important to analyze which of them perform functions where regulatory intervention is needed, and which do not.

In general, regulation focuses on supervising market participants rather than end-users and persons acting on their own behalf. This is because if market participants fail, there is systemic risk and a cascading harm to public interest, which is generally not so for persons acting on their own behalf.

With respect to regulating market participants, the recitals to MiCA state:

"*It is necessary to lay down specific rules for entities that provide services related to crypto-assets.*

A first category of such services consists of ensuring the operation of a trading platform for crypto-assets, exchanging crypto- assets for funds or other crypto-assets, providing custody and administration of crypto-assets on behalf of clients, and providing transfer services for crypto-assets on behalf of clients.

A second category of such services consists of the placing of crypto-assets, the reception or transmission of orders for crypto-assets on behalf of clients, the execution of orders for crypto-assets on behalf of clients, providing advice on crypto-assets and providing portfolio management of crypto-assets.

Any person that provides crypto-asset services on a professional basis in accordance with this Regulation should be deemed to be a 'crypto-asset service provider'."[31]

Similar approaches have been adopted in other jurisdictions such as Dubai, Singapore, and Japan. For instance, Law No. (4) of 2022 Regulating Virtual Assets in the Emirate of Dubai establishes the Virtual Assets Regulatory Authority (**VARA**) (**VARA Act**) to authorise and regulate virtual asset service providers. The VARA Act also ties the definition of virtual asset service providers to those persons engaged in providing any of the following activities:[32]

- Provision of virtual asset platform operation and management services.
- Provision of services for the exchange between virtual assets and national or foreign currencies.
- Provision of services for the exchange between one or more forms of virtual assets.
- Provision of virtual asset transfer services.
- Provision of virtual asset safekeeping, management, or control services.
- Provision of services related to virtual asset wallets.
- Provision of services related to offering, and trading in, virtual tokens.
- Any other activity related to virtual assets specified by VARA.

As regards MFIs, their role was recognized in the FSB's report on the 'Financial Stability Implications of Multifunction Crypto-asset Intermediaries' which concluded that the combination of different types of activities being undertaken by an MFI may exacerbate vulnerabilities and could have significant effects for virtual digital asset markets. As a result, FSB's report suggests a regulatory approach that considers the amplified risks arising from the combination of various functions by MFIs, enhances cross-border cooperation and information sharing, and has adequate disclosure and reporting requirements.[33]

The Draft Bill emphasizes the regulation of market participants within the virtual digital asset ecosystem, given their critical role in managing public-facing functions and holding customer assets. This approach is consistent with global best practices and aims to protect consumers, ensure market integrity, and mitigate systemic risks, without unduly burdening participants who do not engage in these market participant roles. Accordingly, the Draft Bill proposed regulating market participant in the virtual digital asset ecosystem as they perform such

[31] Recital 21 of MiCA.
[32] Article 16 of VARA.
[33] https://www.fsb.org/wp-content/uploads/P281123.pdf

public-facing functions (e.g., holding customer value in trust), rather than others such as users or software developers who generally do not. For instance, MiCA states, "*where crypto-asset services are provided in a fully decentralised manner without any intermediary",* they should not fall within the scope of MiCA.[34] A recent Scoping Paper released by the Law Commission of the United Kingdom on Decentralised Autonomous Organisations (**DAOs**)) also furthered this position, observing, "*decentralisation of a system eliminates the risks that a specific regulation may be intended to address. The result may be that regulation is not required because the problems that regulation is trying to address do not materialise in a system where knowledge, control and decision-making power are distributed rather than being concentrated in a particular person or small group."*[35]

MiCA explicitly excludes hardware and software providers of non-custodial wallets from its regulatory scope, recognizing that these entities do not hold or manage customer assets and thus do not pose the same risks as market participants.[36] As detailed below, this approach is consistent with global regulatory standards, including those set by FATF, which exclude entities that provide infrastructure support, such as cloud service providers, from direct regulation unless they exercise control over virtual digital assets. Additionally, the Financial Crimes Enforcement Network in the United States had released further guidance on the application of the Bank Secrecy Act (**BSA**) to business dealings with digital assets. While its main focus lies on primary and secondary market actors, the guidance also explicitly indicates that most infrastructure service providers, such as software developers, mining pool operators, miners do not qualify as money transmitters under the BSA and hence do not have to comply with BSA obligations.[37] Similarly, the FATF, in its Updated Guidance: A Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers, dated 28 October 2021,[38] required entities to have "the ability to exercise control" over virtual digital assets to qualify as virtual digital asset service providers engaged in the safekeeping or administration of virtual digital assets or instruments enabling control over virtual digital assets. In this vein, the FATF has indicated the exclusion of entities that provide ancillary infrastructure allowing an entity to carry out virtual digital asset activities (such as cloud service providers and integrity service providers) and software developers or providers of non-custodial wallets whose functions are only developing and/or selling the software/hardware from the scope of this virtual digital asset activity.

3. Indian Ecosystem and Regulatory Background

India has emerged as a global leader in virtual digital asset adoption, as recognized by Chainalysis, a leading blockchain analytics platform. In its 2024 Global Crypto Adoption Index[39], released in October 2024, India ranked number one globally in overall virtual digital asset adoption. Additionally, the size of the market in India is anticipated to reach USD 241 million (~INR 2,000 crores)[40]. By some estimates, approximately 75% of investors in the

[34] Recital 22 of MiCA

[35] https://cloud-platform-e218f50a4812967ba1215eaecede923f.s3.amazonaws.com/uploads/sites/30/2024/07/DAOs-scoping-paper-110724.pdf

[36] Recital 83 of MiCA.

[37] https://www.fincen.gov/sites/default/files/2019-10/CVC%20Joint%20Policy%20Statement_508%20FINAL_0.pdf

[38] https://www.fatf-gafi.org/content/dam/fatf-gafi/guidance/Updated-Guidance-VA-VASP.pdf.coredownload.inline.pdf

[39] https://www.chainalysis.com/wp-content/uploads/2024/10/the-2024-geography-of-crypto-report-release.pdf

[40] https://www.hilarispublisher.com/open-access/cryptocurrency-and-its-impact-on-indian-economy-98448.html#:~:text=The%20Indian%20cryptocurrency%20economy%20has,creating%20877%2C000%20jobs%20by%20then

Indian virtual digital asset market are under the age of 35.[41] This indicates a growing interest in blockchain and virtual digital assets among the younger generation and suggests a more urgent need for a suitable regulatory framework.

While India has specifically introduced income tax and AML provisions on virtual digital assets and virtual digital assets service providers (VASPs), and certain provisions in other laws pertaining to cybersecurity and annual corporate filings, there is no dedicated and comprehensive regulatory regime in place as of date. As a result, there is a less-than-ideal status quo on two fronts: platforms lack clarity on their obligations under generally applicable laws, and consumers lack the protection of a dedicated sectoral regulatory framework.

Any proposed regulatory framework for virtual digital assets in India will need to consider the regulatory evolution till date and the current status quo. A summary of the specific provisions and key legal developments on virtual digital assets in India follows:

- From 2013 to 2017, the Reserve Bank of India (**RBI**) issued cautionary press releases on the financial, operational, legal, security and consumer protection-related risks associated with virtual currencies (as virtual digital assets were then referred to) like Bitcoin.[42]

- In 2017, two successive committees were constituted by the Ministry of Finance, Government of India, to examine the regulation of virtual digital assets in India.[43]

- In April 2018, the RBI prohibited its regulated financial institutions, such as banks, from dealing in virtual digital assets and, importantly, from providing services facilitating any buying or selling of virtual digital assets (**RBI Circular**).[44] The RBI Circular deprived the industry of access to banking and payment services. Besides affecting the trading ecosystem, this also impeded blockchain developers and users from being able to purchase virtual digital assets to interact with blockchain networks, or sell virtual digital assets they may have earned as a result of participating in blockchain networks.

- The constitutional validity of the RBI Circular was challenged in *Internet and Mobile Association of India v. RBI*[45] and, in March 2020, the Supreme Court of India set aside the RBI Circular as a disproportionate restriction of trading platforms' fundamental right to do business under Article 19(1)(g) of the Constitution, primarily because:

  (i) The RBI Circular severed the lifeline of the trading platforms - banking access - despite there being no Government ban on trading virtual digital assets;

  (ii) The RBI had not found any shortcomings with the manner in which the virtual digital asset exchanges functioned; and

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[41] https://coinswitch.co/switch/crypto/india-crypto-adoption-2023/#:~:text=Coins%20India%20Loves%20The%20Most&text=Surpassing%20both%20Bitcoin%20(BTC)%20and,the%20Indian%20crypto%20investors'%20portfolio

[42] https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=30247; https://www.rbi.org.in/commonman/English/Scripts/PressReleases.aspx?Id=2152; https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=42462

[43] https://pib.gov.in/PressReleasePage.aspx?PRID=1487645; https://pib.gov.in/PressReleasePage.aspx?PRID=1579759

[44] https://www.rbi.org.in/commonperson/English/Scripts/Notification.aspx?Id=2632

[45] (2020) 10 SCC 274.

(iii) The RBI had not found any empirical evidence that the provision of banking access to virtual digital asset exchanges adversely impacted the functioning of RBI-regulated entities.

- Meanwhile, in 2019, the second inter-ministerial committee constituted in 2017, comprising key officials from the Department of Economic Affairs, Ministry of Finance, the RBI, the Securities and Exchange Board of India (**SEBI**) and the MeitY recommended the banning of all private virtual digital assets in India due to their various risks, and proposed the Banning of Virtual Digital Assets and Regulation of Official Digital Currency Bill, 2019 criminalizing the mining, generation, holding, sale, dealing in, issue, transfer, disposal of or use of virtual digital assets in India with up to 10 years' imprisonment.[46] This draft bill was not introduced in Parliament, although it appears that such introduction was considered till 2021.

- The Ministry of Corporate Affairs by way of a notification dated 24 March 2021 amended Schedule III to the Companies Act, 2013 requiring new disclosures on virtual digital asset by companies in their financial statements. Such disclosures must include details of their trades, profits/losses on transactions involving virtual digital asset, amount of virtual digital asset held and deposits or advances from any person for the purpose of trading or investing in virtual digital asset.[47]

- In May 2021, following reports of certain banks and regulated entities cautioning their customers against dealing in virtual digital asset by referencing the invalid RBI Circular[48], the RBI issued a clarification that the RBI Circular was no longer valid and that customers cannot be cautioned against virtual digital asset transactions by citing it. The RBI also stated that banks and other regulated entities may continue undertaking customer due diligence processes in accordance with AML, KYC, and combating of financing of terrorism (**CFT**) standards, and comply with their obligations under the Prevention of Money Laundering Act, 2002 (**PMLA**) and the Foreign Exchange Management Act, 1999 (**FEMA**).[49]

- On 23 February 2022, the Advertising Standards Council of India (**ASCI**), a self-regulatory body, issued guidelines to regulate the advertising and marketing of virtual digital assets and virtual digital asset platforms and services. As per these guidelines, all advertisements for virtual digital assets, virtual digital asset exchanges or virtual digital asset products should display the following disclaimer: "Crypto products and NFTs are unregulated and can be highly risky. There may be no regulatory recourse for any loss from such transactions", among other guidelines. The ASCI guidelines are voluntary self-regulatory guidelines, except in certain limited contexts such as for advertisements on cable television.

- In March 2022, the Finance Act, 2022, was enacted, amending the Income Tax Act, 1961 (**Income Tax Act**), to include a definition of 'virtual digital assets', a requirement of 1% withholding tax (TDS) on virtual digital asset transactions, and, a flat rate of income tax

[46] https://dea.gov.in/sites/default/files/Approved%20and%20Signed%20Report%20and%20Bill%20of%20IMC%20on%20VCs%2028%20Feb%202019.pdf
[47] https://www.mca.gov.in/Ministry/pdf/ScheduleIIIAmendmentNotification_24032021.pdf
[48] https://www.livemint.com/news/india/leading-indian-banks-warn-investors-against-dealing-in-cryptocurrencies-11622459525028.html
[49] https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12103

(30%) on income from transfer of virtual digital assets, with no offset or carry forward of losses among other things.[50]

- Directions were issued on 28 April 2022, effective from June 2022, by the Indian Computer Emergency Response Team under the Information Technology Act, 2000, which require 'virtual asset service providers', 'virtual asset exchange providers' and 'custodian wallet providers' to undertake KYC verification in the manner prescribed, and maintain all information obtained as part of the KYC process and records of financial transactions for a period of five years.[51]

- In March 2023, the Department of Revenue, Ministry of Finance, Government of India issued a notification[52] which classifies an entity that carries out any of the following activities, on behalf of others in the course of its business, as falling within the ambit of a 'reporting entity':

  (i) Exchange between virtual digital assets and fiat currencies;

  (ii) Exchange between one or more forms of virtual digital assets;

  (iii) Transfer of virtual digital assets;

  (iv) Safekeeping or administration of virtual digital assets or instruments enabling control over virtual digital assets; and

  (v) Participation in and provision of financial services related to an issuer's offer and sale of a virtual digital asset.

  Reporting entities are subject to various obligations under the PMLA, including prescribed KYC norms, appointing designated officers, filing suspicious transaction reports, and tracking virtual digital asset deposits and withdrawals (known as the 'travel rule' in the AML industry), among others. The FIU has published guidelines titled 'AML & CFT Guidelines for Reporting Entities providing services related to Virtual Digital Assets' to implement such requirements.[53] The FIU has also issued circulars for the registration of virtual digital asset service providers as reporting entities[54], and the reporting format for virtual digital asset service providers.[55]

- In December 2023, it was announced that the FIU issued show-cause notices to nine foreign virtual digital asset service providers for alleged non-compliance with the PMLA and requested MeitY to block their URLs.[56]

- As of December 2024, there are reported to be approximately 47 virtual digital asset service providers registered with the Financial Intelligence Unit – India (**FIU**), as shared by Ministry of Finance in answer to a question in Lok Sabha .

[50] Section 194S and 115BBH of Finance Act, 2022.
[51] https://www.cert-in.org.in/PDF/CERT-In_Directions_70B_28.04.2022.pdf
[52] https://egazette.gov.in/WriteReadData/2023/244184.pdf
[53] https://www.fiuindia.gov.in/pdfs/AML_legislation/AMLCFTguidelines10032023.pdf
[54] https://fiuindia.gov.in/pdfs/downloads/VDASP04072023.pdf
[55] https://www.fiuindia.gov.in/pdfs/quicklinks/User_Manual_VASP.pdf
[56] https://pib.gov.in/PressReleasePage.aspx?PRID=1991372

- In February 2025, the Finance Bill, 2025, proposed inclusion of Section 285BAA which makes it mandatory for reporting entities to furnish transaction statements of VDAs to the prescribed income tax authority. Provided such a requirement, this may mean that undisclosed VDA may attract a tax of 60% under Section 158BA.[57]
- In February 2025, the Finance Bill, 2025, the definition of VDA was proposed to be amended to include the following "(d) any crypto-asset being a digital representation of value that relies on a cryptographically secured distributed ledger or a similar technology to validate and secure transactions, whether or not such asset is included in sub-clause (a) or sub-clause (b) or sub-clause (c)".[58]

4. Global Regulatory Approaches

Countries around the world have recognized both the benefits and risks of virtual digital assets. Globally, a consensus has emerged among multilateral bodies and leading economies that effective and targeted regulatory measures can help mitigate the risks while promoting the benefits of the technology. This would also align with India's objectives of promoting the digital economy and protecting constitutional freedoms.

G20

During the G20 Summit in 2023, which India presided over, India advocated for harmonising regulatory norms for virtual digital assets and a collaborative approach to virtual digital asset regulation on a global level to address their cross-border nature and for mitigating the associated macroeconomic implications. India's Presidency Note[59] also outlined certain recommendations to act as an input for the IMF-FSB Paper, for acting as minimum standards to guide global crypto regulation. The Presidency Note's recommendations include the implementation of FSB's high-level recommendations (discussed below), development of a framework which takes macro financial risks and implications into account, generation of awareness among various jurisdictions in relation to virtual digital assets, facilitation of cross-border information sharing and consumer protection, and effective implementation of AML and CFT standards, following a risk-based approach as set out by the FATF.

In a recent interview from May 2024, Finance Minister Nirmala Sitharaman reiterated the need for a global regulatory framework for crypto-assets, similar to the approach taken during the G20 summit.[60]

In July 2024, the finance ministers and central bank governors of the G20 reiterated the need for the regulation of crypto-assets by way of implementing the recommendations of international organisations such as the IMF, FSB and FATF. They also recognised upcoming steps in crypto-asset regulation such as assessing the implications of tokenisation of assets in the context of money and other assets and developing a tokenised environment that has incorporated the best attributes of the current monetary and financial system.[61]

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[57] https://www.indiabudget.gov.in/doc/Finance_Bill.pdf
[58] https://www.indiabudget.gov.in/doc/Finance_Bill.pdf
[59] https://www.g20.in/content/dam/gtwenty/gtwenty_new/document/Presidency_note_on_Framework_for_Crypto_Assets.pdf
[60] https://www-thehindubusinessline-com.cdn.ampproject.org/c/s/www.thehindubusinessline.com/news/nobody-has-the-right-to-curb-entrepreneurship-says-fm-nirmala-sitharaman/article68194358.ece/amp/
[61] https://www.g20.org/en/documents/documents-resulting-from-the-3rd-g20-finance-ministers-and-central-bank-governors-meeting-rio-de-janeiro-25th-and-26th-of-july-2024/2-3rd-fmcbg-communique.pdf/@@download/file

It is worth noting that in 2023, the Organisation for Economic Cooperation and Development (**OECD**) had issued the Crypto Asset Reporting Framework (**CARF**), which provides for the automatic exchange of tax relevant information on crypto-assets between jurisdictions.[62] In a G20 ministerial declaration on international tax cooperation in July 2024, the finance ministers of the G20 recognised the work of the OECD on the CARF, calling for its swift implementation, and recognised that the exchange of relevant information regarding crypto-assets, including beneficial ownership information, is a challenge which requires enhanced international tax cooperation.[63] The ministers also stated that they look forward to the recommendations of the OECD on advancing tax transparency, further to the OECD's recommendations made during the Indian G20 presidency.

Financial Stability Board

In July 2023, the FSB finalised its 'Global Regulatory Framework for Crypto-Asset Activities'[64] and made two sets of recommendations for the regulation, supervision and oversight of (i) crypto-asset activities and markets;[65] and (ii) "global stablecoin" arrangements[66]. The FSB has upheld its position that crypto-asset activities must be subject to regulation and oversight that is effective and commensurate with the risks they may pose, while facilitating innovation. Recommendations issued by the FSB aim to promote comprehensiveness and higher levels of consistency in regulatory and supervisory approaches globally to crypto asset activities and markets, including crypto-asset issuers and service providers.

The FSB's recommendations require authorities to be adequately empowered to regulate and enforce relevant laws in relation to crypto-asset activities. The regulatory framework applied must be proportional to the nature of the crypto-asset activity and the financial stability risk it poses, including those cases where a crypto asset service provider is engaged in multiple functions. Authorities of different jurisdictions must have cross-border cooperation, coordination and information sharing. Crypto-asset issuers and service providers must fulfil certain responsibilities and have systems in place for (i) risk management; and (ii) data collection, recording and reporting; (iii) making disclosures to users and other relevant stakeholders. Authorities must also take into account the financial stability risk arising due to interconnectedness, such as between the crypto-asset ecosystem and the wider financial system.

International Organisation of Securities Commissions

In May 2023, the International Organisation of Securities Commissions published its report making recommendations to address market integrity and investor protection issues in the

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62 https://www.oecd.org/en/publications/international-standards-for-automatic-exchange-of-information-in-tax-matters_896d79d1-en.html

63 https://globalgovernanceprogram.org/g20/2024/240726-1)-G20-Ministerial-Declaration-International-Taxation-Cooperation.pdf

64 https://www.fsb.org/2023/07/fsb-finalises-global-regulatory-framework-for-crypto-asset-activities/
65 https://www.fsb.org/wp-content/uploads/P170723-2.pdf
66 https://www.fsb.org/wp-content/uploads/P170723-3.pdf

virtual digital asset markets.[67] The recommendations encourage regulators to analyse the applicability and adequacy of their regulatory frameworks applicable to traditional financial instruments and activities in relation to virtual digital asset activities, and to engage in cross-border cooperation. The report also makes recommendations for virtual digital asset service providers on (i) governance and disclosure of conflicts; (ii) order handling and trade disclosures; (iii) listing of virtual digital assets and primary market activities; (iv) custody of client monies and assets; (v) operational and technological risks; and (vi) retail distribution.

Financial Action Task Force

The FATF is an inter-governmental body which sets global standards on AML and CFT.[68] In October 2018, the FATF amended Recommendation 15 of the International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation[69] (**FATF Standards**) to clarify their application to financial activities involving virtual assets and defined the terms "virtual asset" (**VAs**) and "virtual asset service provider" (**VASPs**). Recommendation 15 requires VASPs to be regulated for AML and CFT purposes, be licensed or registered, and be subject to effective systems monitoring or supervision.[70] The FATF also issued an interpretative note on the implementation of Recommendation 15.[71] In October 2021, the FATF provided updated Guidance for a Risk Based Approach to VAs and VASPs, which focuses on areas such as (i) clarification on the definition of VAs and VASPs; (ii) guidance on how FATF Standards apply to stablecoins; (iii) additional guidance on the risks and the tools available to countries to address the money laundering and terrorist financing risks for peer-to-peer transactions; and (iv) updated guidance on the licensing and registration of VASPs.[72]

Recommendation 16 provides for the implementation of FATF's wire transfer requirements (**Travel Rule**) in the context of VAs. The Travel Rule requires VASPs obtain, hold, and transmit specific originator and beneficiary information immediately and securely when transferring VAs.[73]

Organisation for Economic Cooperation and Development

The Organisation for Economic Cooperation and Development (**OECD**) issued the Crypto Asset Reporting Framework and Amendments to the Common Reporting Standard (**CARF**) in October 2022.[74] The OECD issued CARF to amend the Common Reporting Standard to provide for a new tax transparency and reporting framework for transactions involving virtual digital assets in a standardised manner. The CARF provides for rules that can be transposed into national law to obtain information from crypto asset service providers. The rules are related to (i) the scope of virtual digital assets to be covered; (ii) the individuals and entities

[67] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD747.pdf
[68] https://dea.gov.in/pressrelease/indias-membership-financial-action-task-force
[69] https://www.fatf-gafi.org/content/dam/fatf-gafi/recommendations/FATF%20Recommendations%202012.pdf.coredownload.inline.pdf
[70] https://www.fatf-gafi.org/content/dam/fatf-gafi/guidance/RBA-VA-VASPs.pdf
[71] https://www.fatf-gafi.org/en/publications/Fatfrecommendations/Public-statement-virtual-assets.html
[72] https://www.fatf-gafi.org/content/dam/fatf-gafi/guidance/Updated-Guidance-VA-VASP.pdf.coredownload.inline.pdf
[73] https://www.fatf-gafi.org/content/dam/fatf-gafi/guidance/June2023-Targeted-Update-VA-VASP.pdf.coredownload.inline.pdf
[74] https://www.oecd.org/tax/exchange-of-tax-information/crypto-asset-reporting-framework-and-amendments-to-the-common-reporting-standard.pdf

who will be subjected to data collection and reporting requirements; (iii) the types of transactions to be reported and the information to be reported in relation to such transactions; and (iv) due diligence procedures to identify users and to determine the relevant tax jurisdictions for reporting and exchange purposes.

IMF-FSB Synthesis Paper

During the term of the Indian G20 presidency, the International Monetary Fund and the FSB released the IMF-FSB Paper outlining a framework that synthesised their respective approaches to the regulation of crypto-assets.[75] Importantly, this paper provides a policy implementation roadmap for a comprehensive policy framework for crypto-assets. The IMF-FSB Paper was released on 7 September 2023.

The implementation roadmap includes (i) the implementation of policy frameworks; (ii) outreach beyond G20 jurisdictions; (iii) global coordination, cooperation and information sharing; and (iv) addressing data gaps. The implementation roadmap provides a varying timeline of 8 – 12 months i.e., May – July 2024 and end-2025 for the assessment of compliance with these initiatives.

G7

The G7 member countries' deliberations in May 2024 included discussions on virtual digital asset regulations. The G7 reiterated the importance of intensifying global efforts against money laundering and terrorist financing, and the implementation of FATF standards globally. The G7 also reaffirmed its support for the G20 roadmap on crypto-assets. They also welcomed the effective implementation of CARF in relevant jurisdictions, with the aim of commencing first exchanges by 2027 or 2028 at the latest. In June 2024, the G7 reaffirmed its commitment to implementing effective regulatory and supervisory frameworks for crypto-assets. They reiterated the importance of international efforts to combat money laundering and terrorist and proliferation financing and supported the FATF's initiatives in relation to the same. They also reiterated their support for the effective implementation of CARF.[76] India has been part of the outreach sessions of the G7's meetings and deliberations this year.[77]

Jurisdictional approaches

Globally, democratic jurisdictions have generally chosen to regulate rather than prohibit virtual digital asset activities. The regulatory approaches adopted by such jurisdictions can be broadly categorized into (i) applying existing regulatory frameworks, with suitable amendments or modifications, to virtual digital assets; and (ii) developing new regulatory frameworks dealing with virtual digital assets exclusively.

Certain countries such as Singapore and Japan have amended existing legislation to cover virtual digital assets, while other jurisdictions have implemented comprehensive legislation, such as the EU's enactment of MiCA and the United Arab Emirates' enactment of the statute setting up the VARA and related regulations. However, even in those jurisdictions which have

[75] https://www.fsb.org/wp-content/uploads/R070923-1.pdf
[76] https://www.g7italy.it/wp-content/uploads/Apulia-G7-Leaders-Communique.pdf
[77] https://pib.gov.in/PressReleasePage.aspx?PRID=2032987#:~:text=Shri%20Piyush%20Goyal%2C%20Commerce%20and,the%20G7%20Trade%20Ministers'%20Meeting.

enacted new frameworks, certain types of virtual digital assets or virtual digital asset activities in certain designated areas are covered by existing legislation.

The recently published Commonwealth Model Law on Virtual Assets by the Commonwealth Secretariat (**Commonwealth Model Law**) recognizes that countries can introduce new regulatory provisions for virtual digital assets either through a new legislation or by incorporating the relevant provisions suitably into existing legislations.[78] The FSB too has recognized that both approaches are valid and vary by jurisdiction.[79]

[78] https://production-new-commonwealth-files.s3.eu-west-2.amazonaws.com/s3fs-public/2024-07/commonwealth-model-law-on-virtual-assets_d19821.pdf

[79] https://fsb.org/wp-content/uploads/P111022-3.pdf

BHARAT WEB3 ASSOCIATION

BWA is India's leading industry body comprising 40+ members from India's Web3 and VDA ecosystem. Our membership includes several Virtual Asset Service Providers (VASPs), Layer 1/Layer 2 Blockchain Infrastructure Providers, NFT players and other Web3-associated service providers.

At BWA, we are committed to raising awareness, conducting research, establishing industry standards, nurturing the Indian talent pool, protecting consumers' interests, and encouraging stakeholder dialogue to build a strong and compliant Web3 and VDA ecosystem in India. Our vision and mission is to position India as a leader in this next wave of technological innovation.

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https://bwaind.in/

E-MAIL:
secretariat@bharatweb3association.com