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CENTRAL BANK DIGITAL CURRENCY (CBDC) AND DIGITAL RUPEE

AUTHOR - UDAYVEER SINGH, STUDENT AT AMITY LAW SCHOOL, NOIDA

What is CBDC?

The traditional banking and financial system have been on a rapid evolving curve owing to the effects of the Covid -19 pandemic, changes in international trade, aggressive technological advancements, and globalization. CBDC is just another outcome of this revolution. The CBDC forms a part of the digital matrix of virtual currencies, however unlike cryptocurrencies, and other virtual assets CBDCs are not a commodity or a virtual asset. CBCDs are more like fiat currency like paper notes and coins, except for the fact it's not physical and instead stored in a e-wallet. Just like physical cash CBDCs hold true to features such as trust, safety, transaction, and finality of settlements. Its framework is backed by the robust foundation of technological advancements such as the blockchain technology which depends on the encryption and decryption of digital ledger to safeguards transactions over the digital network.

Why are Central Banks and Governments interested in CBDC?

CBDC is being seen as a transformative catalyst in the domain of money and finance, which aims to revolutionize financial inclusion, safety, and affordability of financial avenues to help

individuals engage in economic transaction. Unlike cryptocurrencies these are backed and regulated by the Central Banks and thus are stable and facilitate security and trust amongst the people. It's unique features such as its offline capability of transaction using technologies such as Bluetooth and NFC, its mobility, and no requirement for bank accounts will lead to empowerment of the marginalized or the unbanked population by giving them access to the mainstream financial system which will increase their propensity to save and is destined to change their social, economic, and political lives. The broader adoption of CBDCs will reduce the economic and digital divide within the urban and rural areas. The global adoption of CBDCs with a common structure or framework would also ease cross border transactions and smoother funds transfer across the globe and avoid high fees owing to issues such as time zones, foreign exchange, and interest rates.

The Digital Rupee

In the Union Budget 2022-23, Finance Minister Nirmala Sitharaman announced the introduction of CBDC and proposed various necessary amends to the RBI Act 1934 to incorporate the concept of CBDC in the legal framework. With these developments in December 2022, India launched the pilot for its own retail CBCD called the digital rupee (e-₹). With this India joined the list of 105 nations which are developing their own CBDCs. The digital rupee also called RBI's accepted version of cryptocurrency, but unlike cryptocurrencies the digital rupee is a legal tender which is regulated and backed by the RBI. It represents the Indian Rupee (₹) in a digitalized token form. In India the CBDC framework can be classified into Wholesale CBDC(CBDC-W) and Retail CBDC(CBDC-R), the CBDC-W would be issued to banks and financial intermediaries and will be used for interbank settlements, government bond transactions and other capital market transactions, whereas the CBDC-R is meant to be used by the general population the same way as physical cash.

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Owing to its digital nature, RBI will also save on the printing and management cost, for instance in FY 2021-22 the cost of printing a 10 Rupee note was 96 paise and the overall management cost of every 100 Rupee note was around 15-17% including the cost for print, distribution, and return. Further its technological features such as real time tracking, and ledger maintenance will help with the cash placement and tracking issue which used to be a major challenge in case of physical cash. If the CBDC experiment turns out to be fruitful it will eventually lead to better control, oversight, and the stability of the financial system.

Legal Implications of Digital Rupee

Digital Rupee just like cryptocurrencies exist on a virtual network over the internet and acts act as a virtual currency. In theory the two might share many similarities however in its implication it will be of no similarity to the cryptocurrencies like bitcoin, Ethereum or Tether.

Since the digital rupee is backed by the RBI which is the central bank of the country and would use a government permitted private network to regulate the same, thus the digital rupee can be tracked unlike the other cryptocurrencies. Further the addition of section 22A along with other amendments through the Finance Act, 2022, in the RBI Act,1934 makes certain provisions applicable on bank notes to be inapplicable on digital form of currency. Thus the digital rupee would act as a medium of transactions just like the bank notes issued by the RBI and not as a digital asset. And the economy would be able to reap out the benefit of ease of doing transactions by means of a legal and regulated tender.

The way forward

Payments and money supply are the backbone of any financial system, and it has become imperative for the central banks across the globe to develop and provide for frameworks and mechanisms which aims to provide the users with the new world functionalities. The future of CBDCs can be envisioned as the digital counter part of cash while services like UPI will act as a portal connecting different banks and intermediaries.

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