DIGITIZING THE RUPEE, REWRITING THE LAW: A CRITICAL EXAMINATION OF CBDC'S LEGAL IMPLICATIONS IN INDIA

Yash Nandini Singh, B.B.A. LL.B. (Hons.), National Forensic Sciences University, Delhi

ABSTRACT

The purpose of this paper is to investigate CBDC as an important innovation in the development of money, payments, and monetary management in India. This study does not consider CBDC as a mere instrument of payment transactions but as a form of money that poses significant legal, economic, and policy questions. This paper commences by introducing the CBDC into the context of India's burgeoning digital payments landscape. Thereafter, the paper contrasts the CBDC to private cryptocurrencies through their characteristics as sovereign money that enjoys legal backing and recognition. By reviewing the existing literature, this study finds that most scholars see the possibility of using CBDC to enhance the efficiency of payment processes, cut down the costs of transactions, promote financial inclusion, and assist in monetary policy transmission. However, the literature has also identified several challenges that CBDC poses.

The article then goes on to examine the legal framework underpinning the issuance of CBDC in India, along with the statutory powers of the Reserve Bank of India and the changes in the legislation for issuing digital rupees. It further explains the role played by the design features of CBDC, whether based on accounts or tokens, in influencing the legal aspects of its development. Another section is dedicated to issues related to privacy and anti-money laundering and counter terrorism financing regulations, illustrating the conflict between transaction tracking and individual privacy. CBDC can also pose a risk to commercial bank deposits due to liquidity problems in case of wide-scale adoption, hence necessitating certain safety measures like deposit limits and staged deployment.

On the whole, the paper argues that CBDC has great scope for enhancing the money system of India, but it will require effective legislation, enhanced privacy, liability laws, and prudence in implementation. This paper's recommendations and limitations illustrate that CBDC can prove to be a successful concept if introduced effectively.

Keywords: CBDC, India, Legal Framework.

INTRODUCTION

CBDC, or Central Bank Digital Currency, is one of the most important new ideas in the way money, payment systems, and financial governance are changing today. As digital technologies change the way people and businesses store, move, and use money, central banks around the world are looking more and more at whether a sovereign digital currency can work with or change existing monetary systems. The introduction of the digital rupee in India has also sparked a major legal and policy debate about the future of state-backed money in an economy that is quickly becoming more digital. This development is especially important because CBDC is not just a new way to pay; it is also a sign of a bigger change in institutions that could change the way currency works, the role of central banks, and the balance between innovation and regulation in the financial sector.

This topic is important because CBDC is at the crossroads of law, economics, technology, and public policy. It has a lot of good points on the one hand. It might lower transaction costs, make payments faster and more efficient, make it easier for people to get access to financial services, and be a safer option than private digital currencies. It might also help central banks have more control over monetary policy as the world becomes more digital. On the other hand, the introduction of CBDC raises serious privacy, data protection, cybersecurity, consumer autonomy, and the possible disintermediation of commercial banks. Because the State backs CBDC directly, it also raises questions about how digital money should be regulated, who should have access to the data that powers it, and what legal protections users should have.

In India, these questions are even more important because the country already has a very advanced digital payments system, with UPI being the most well-known example. At the same time, India is also dealing with issues of financial inclusion, digital literacy, and unequal access to technology. So, we can't look at the introduction of CBDC in a vacuum; we need to think about the bigger picture of the law and the economy. It must be evaluated in the context of the Reserve Bank of India's statutory authority, the current payment and settlement framework, constitutional principles, and the policy objectives of efficiency, transparency, and inclusivity.

CBDC raises many unresolved questions. What is its legal status? How does it fit in with existing forms of money? What protections are needed against misuse or exclusion? At the same time, changes to legal or technological frameworks may raise new open questions that will need to be examined. Experts should examine how to tackle these emerging issues.

The Central Bank Digital Currency (CBDC) is potentially an important form of money in the future. It can act as a secure, efficient and inclusive instrument of payment. Its introduction comes with the assessment of various CBDC aspects which include its design, objectives, legal and financial system and its impact on the existing legal framework in the country, if any. CBDC can be enabled with smart contracts which will revolutionise the banking and payment system in the country. The data privacy and security, operational stability, trust, policies of Central Bank and supervision are also some of the key issues with respect to the financial system which CBDC will need to address for its successful adoption. Adopting CBDC will take India another step forward in the direction of the future of money. It will enable to integrate digital sovereign currency into the financial system. The research paper predominantly evaluates the potential implications of CBDC in the legal and financial system of India and its effect on the existing legal framework.

LITERATURE REVIEW

The concept of Central Bank Digital Currency should be seen as more than just another payment method; rather, it needs to be seen as a transformation of the way money works within the country's economic system. As shown in the current literature, the idea behind the implementation of CBDC is the fusion of the security associated with sovereign currencies and the speed provided by digital payments, which, however, will highly depend on the design, legal framework, and overall financial context. In India, where there exists an established payment system, the issue here should not be about the functionality of CBDC, but rather how it fits in without causing any harm to the monetary system.[1]

The second important theme for researchers includes financial stability and how this innovation may affect banks. According to scholarly articles, CBDC can provide benefits to central banks by improving money management and efficiency of the payment process, but it may create problems for banks due to the potential withdrawal of deposits. This is why research papers tend to consider the issue of central bank digital currencies as an instrument that may be advantageous for the monetary system, but only in case of careful approach, which will prevent banks from experiencing any risks related to money management, lending practices, and provision of credit facilities. Finally, as it was already mentioned, all the effects associated with

[1] Bhavesh H. Bharad & Komal B. Sharma, *Legal Challenges in Adopting Central Bank Digital Currency: A Case Study of an Emerging Nation India*, 1 Int'l J. Mgmt., Econ. & Com. 138 (2024)

using central bank digital currencies depend on its availability, remuneration, and regulations of ownership.

The third discussion topic relates to privacy and data management. Most CBDCs will have to identify the participants in order to adhere to policies aimed at prevention of money laundering and terrorism financing; however, identification of users raises a number of privacy issues. The studies done in India show that the issue of privacy in India is not merely related to policies but is also an intrinsic aspect of the Indian Constitution, which implies that CBDCs should be designed according to the principle of privacy through the use of data minimization and proportionality.[2]

Overall, the discussion in the literature shows that CBDC is promising but incomplete. It may modernize money, improve payment efficiency, and reinforce the role of sovereign currency, but its success depends on carefully balancing legal authority, financial stability, privacy, and inclusion. The Indian case demonstrates that CBDC is not only a question of technology, but of institutional design and regulatory judgment.

RESEARCH OBJECTIVE AND METHEDOLOGY

The paper aims to examine the implications of Central Bank Digital Currency on the legal, economic and policy strata of India, with particular emphasis of its impact on monetary sovereignty, banking stability, privacy and financial inclusions. In addition, it also seeks the check whether the existing framework is adequate for CBDC implementation.

The methodology is doctrinal and analytical in nature. It is based ona review of primary legal sources, policy documents and relevant academic literature. The study compares different scholarly views and evaluates their findings in the Indian context.

ANALYSIS AND DISCUSSION

This section looks at India's Central Bank Digital Currency, or CBDC, from a legal and policy point of view. It focuses on matters like what legal basis CBDC has, the privacy issues and rules it brings up, how it affects financial stability, and the wider concerns about protecting consumers and figuring out who is responsible. Since CBDC isn't just a new technology but

[2] Reserve Bank of India, Concept Note on Central Bank Digital Currency (2022)

actually changes how a country's money works, we need to pay close attention to both its legal structure and what happens in the real world.

1. **Legal basis of CBDC in India**: In India, the legal framework for CBDC is backed by the *Reserve Bank of India (RBI*), which is empowered to issue currency and regulate monetary systems in general via the RBI Act, 1934[3]. This meant careful reading of both the statutory powers of the RBI and legal meaning attached with "bank note" and legal tender in order to introduce digital rupee. CBDC, while important in that it carries the notion of sovereign currency to a digital medium, questions whether the broad definition of monetary law was well drafted enough within existing monetary policy. The legal framework should therefore clarify issuance, recognition and enforceability as well as the relationship of CBDC to existing forms of money.[4]

2. **Privacy and data protection concerns**: The reason that CBDC is a potentially serious privacy issue is due to the fact that inclusive of all the various different types of digital currency, their transaction contents and history could reflect deeply intimate and consequential details about those individuals' day-to-day lives. For example, whereas cash offers extreme anonymity, CBDC could be used to track payments and spending habits, by identity. Although this would assist with transparency and fraud protection, it raises issues of surveillance and abuse of personal information. In a country like India, where privacy finds constitutional recognition[5], utmost care should be taken over structuring CBDC in manner so as to retain end-user confidence but also allowing de jure regulatory oversight. The challenge involves balancing traceability and confidentiality.

3. **AML/CFT issues**: CBDC could be helpful for compliance with regulations against money laundering and terrorist financing since it provides enhanced transaction tracking and monitoring capabilities. Such a possibility can contribute to effective detection of suspicious transactions and protection from abuse and corruption. At the same time, characteristics that can be beneficial for enforcement can become an impediment when there are no limits on their use.[6] It is necessary to have a proper regulatory framework defining the responsibilities of

[3] Reserve Bank of India Act, No. 2 of 1934, India Code (1934).
[4] Neha K. Chawla, *Implications of Central Bank Digital Currency in India: A Critical Analysis*, 4 DME J.L. 22 (2023)
[5] Justice K.S. Puttaswamy (Retd.) v. Union of India, (2019) 1 SCC 1
[6] FinTech Dep't, Reserve Bank of India, *Concept Note on Central Bank Digital Currency* (2022)

entities involved in customer due diligence, transaction recording, and monitoring.

4. **Financial stability and bank disintermediation**: The main worry in literature is that CBDC could attract deposits from commercial banks. In case people find it better to have sovereign money than commercial bank deposits, banks would have less liquidity and hence lower lending abilities. It could also interfere with financial intermediation processes, and in worse situations, pose a risk to stability during times of crisis. That explains why some designs like limit on holdings, no remuneration, and phased rollout are very crucial in ensuring that CBDC supports banks.[7]

5. **Consumer protection and liability:** The other perspective that has to be considered in regard to CBDCs is that of consumer protection. Consumers should have a clear understanding about how things would proceed in case of any issues such as technical glitches, scams, accidental transactions, and even cyberattacks. Digital currency system nee an explicit redressal framework because unclear accountability weakens trust and adoption.[8] Consumer remedies play a very crucial role when it comes to a successful digital currency system since one needs a clear allocation of liability for resolving grievances.[9]

6. **Comparative insights:** Comparative experience demonstrates that the design of CBDC varies among states. While some states have been keen on implementing the retail version of CBDCs, there are other states which favor the limited and pilot versions.[10] In view of the foregoing observations, it can be suggested that India should take a more prudent approach to implementing CBDCs. The reason why comparative studies are important in this case is that CBDCs are not one-size-fits-all solutions.[11]

LIMITATIONS AND SUGGESTIONS

Central Bank Digital Currency is a valuable and promising innovation in today's world, where spped, safety aand efficiency are the primary concerns of the masses. At the same time, it is

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[7] Priyadarshini D. & Sabyasachi Kar, *Assessing the Viability of an Indian Central Bank Digital Currency (CBDC)*, 3 Indian Pub. Pol'y Rev. 45 (2022)
[8] Parthabi Kanungo & Dr. Priti Saxena, *Regulatory Framework of Central Bank Digital Currency (CBDC) in India: A Comparative Study with Other Jurisdictions*, SSRN (Apr. 6, 2024)
[9] Chawla, *supra* note 2
[10] David Altig et al., *The Macroeconomic Implications of CBDC: A Review of the Literature*, Fin. & Econ. Discussion Series 2022-076 (2022)
[11] Tobias Adrian & Tommaso Mancini-Griffoli, *The Rise of Digital Money*, IMF FinTech Note No. 19/001 (2019)

accompanied with certain limitations that need attention. This section outlines practical suggestions and the main challenges that affect implementation.

1. CBCD should only be introduced after the implementation of a clear policy. The IMF also suggests that countries should, prior to introducing digital currency identify their objectives and quantify risks.[12]

2. India should opt for a phased method for introduction, since researched repeatedly indicated that pilot testing, limited access and gradual implementation reduce operational uncertainty. [13]

3. Limits or tiered system should be considered since according to the IMF and EDPS, limiting, capping or tiering of deposits will help decrease migration of deposits and mitigate risks.[14]

4. The design of CBDC must sustain intermediation by banks, as warned by the BIS report stating that CBDC might not necessarily enhance the transmission of monetary policy.[15]

5. It is essential to incorporate measures for privacy into the system, as CBDC technology could lead to huge exposure of data and potential conflict between traceability and legality.[16]

6. The balance between monitoring for AML/CFT purposes and confidentiality needs to be struck, as CBDC would make it easier to monitor transactions, but over-monitoring could jeopardize confidence.[17]

7. Digital literacy and infrastructure continue to be significant constraints, as per several studies done in India, which show varying levels of access, integration problems, and the prevalence of other payment systems in the marketplace.[18]

8. The most common limitation in terms of literature is the lack of longitudinal evidence, considering the majority of recent studies focus either on concept papers or pilots of CBDCs rather than implementation evidence.

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[12] Int'l Monetary Fund, Central Bank Digital Currency Virtual Handbook (2023)
[13] Priyadarshini, *supra* note 5
[14] Eur. Data Prot. Supervisor, TechDispatch 1/2023: Central Bank Digital Currencies (2023)
[15] Comm. on Payments & Mkt. Infrastructures & Mkts. Comm., Central Bank Digital Currencies (2018)
[16] Aman Patanjali, *Examining the Policy and Legal Consideration of a Digital Rupee*, Vidhi Ctr. for Legal Pol'y: Blog (Dec. 3, 2021
[17] Priyadarshini, *supra* note 5
[18] PwC India, *Future of Digital Currency in India*, PwC: Research and Insights Hub (2022)

9. The limitation related to the results from India could be that CBDC success depends significantly on banking architecture and payment systems of the countries involved.[19]

On the whole, the introduction of CBDC provides an interesting route towards efficiency in the financial system, but success would hinge upon proper recognition of its drawbacks. By having an equilibrium legal structure, adequate privacy protections, and gradual implementation along with consumer protection measures, CBDC can indeed prove to be an important tool for the future of the Indian monetary system. However, the recommendations provided above clearly indicate caution and inclusiveness in the adoption of this technology.

CONCLUSION

Overall, CBDC is a major step in the history of money and payments, particularly for developing economies such as India which are heading towards a much more digital economy. As highlighted by the literature reviewed, CBDC holds great promise for making transactions efficient, decreasing costs of settlements, enhancing financial inclusion, and ensuring the dominance of sovereign money in a digitally oriented world. On the other hand, as seen from the studies examined, CBDC cannot be considered an improvement in technology alone. Indeed, there are some key issues of law, regulation, and policy that should be addressed beforehand.

Most pressing considerations that arise based on the literature review include privacy, security and data protection, financial stability, disintermediation of banks by means of the system, and consumer protection. As CBDC may produce a set of records of each transaction performed, it is important to make sure that this information does not violate users' privacy, yet it could still be accessed by regulators if needed. In addition, since the usage of CBDC may lead to the movement of assets outside commercial banks, it should not undermine the banking industry in general and the stability of the economy in particular.

Thus, legal aspects that should be elaborated upon before introducing CBDC to India include issues such as issuing CBDC, liability and grievance redressal. It appears that CBDC should be considered a promising mechanism of the future that can contribute to the improvement of the monetary system in India provided that it is designed and implemented properly. If all

[19] Vidhu Shekhar & Sanjogita Ramesh, *Central Bank Digital Currency in India: Perspectives on Design Choices and Implications of e-Rupee*, 33 Fin. Servs. Rev. 61 (2025)

necessary precautions are taken, CBDC has a high potential for success.