December 31, 2021

ripple

The Centre for Internet and Society, India
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Email: aman@cis-india.org

Dear Mr. Aman Nair,

Ripple Labs Inc. ("Ripple") welcomes the opportunity to comment on the Report on the Regulation of Private Crypto-assets in India ("Report") published by the Centre for Internet and Society, India ("CIS") on December 15, 2021.[1]

Ripple would like to thank CIS for the for the in-depth and comprehensive analysis that has been undertaken in the Report, and we appreciate the initiative CIS has taken in proactively highlighting the importance of developing a regulatory framework to govern private cryptoassets[2] in India. We also commend CIS for the recommendation to avoid a ban on cryptoassets and support the long-term policy recommendations set out in the Report.

Using blockchain technology, Ripple allows financial institutions to process payments instantly, reliably, cost-effectively, and with end-to-end visibility anywhere in the world. RippleNet, our enterprise software solution which is powered by a standardized application programming interface ("API") and built on the market-leading and open standard Interledger Protocol, enables financial institutions to facilitate faster and less costly cross-border payments, demonstrating that deep interoperability between commercial financial institutions can make payments truly efficient, particularly in eliminating the uncertainty and risk historically involved in moving money across borders using interbank messaging alone.

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[1] *See* https://docs.google.com/document/d/1BDk2Vd4BsOmmnjOXZLCxcKsgsfNC8rpF/edit?usp=sharing&ouid=117432309658394042594&rtpof=true&sd=true, CIS Report on the Regulation of Private Crypto-assets in India.

[2] The terms digital asset, virtual currency, cryptocurrency, cryptoasset and others are used interchangeably in the marketplace. For the purposes of this letter, Ripple adopts the terminology and related definitions used by CIS in the Report.

Some customers, in addition to deploying RippleNet, choose to leverage XRP - the cryptoasset native to the XRP Ledger, a distributed ledger platform - as a bridge between fiat currencies, further reducing the friction and costs for commercial financial institutions to transact across multiple global markets.

Although Ripple utilizes XRP and the XRP Ledger in its product offerings, XRP is independent of Ripple.[3] The XRP Ledger is decentralized, open-source, and based on cryptography. While there are well over a hundred known use cases for XRP and the XRP Ledger, Ripple leverages XRP for use in its product suite because of XRP's suitability for cross-border payments. Key characteristics of XRP include speed, scalability, energy efficiency, and cost - all of which benefits the consumer and helps reduce friction in the market for cross border payments, thereby removing barriers to India's growth as a technology and finance centre.

We would also like to highlight that on June 18, 2020, Ripple published a policy paper offering an overview of the global cryptoassets landscape, and proposing measures policymakers and regulators may wish to consider implementing to support a comprehensive and competitive digital asset policy in India ("Policy Paper").[4] These include adopting a taxonomy consistent with global best practices, enacting a facilitative legal framework for service providers, and implementing a conducive regulatory framework by amending certain financial sector legislation.

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With this overview, and in line with the recommendations of the Report, Ripple respectfully submits feedback on use cases for how blockchain applications and cryptoassets can benefit consumers in India, as well as policy recommendations for consideration in the attached Appendix.

Ripple appreciates the opportunity to provide feedback and we would encourage and support further dialogue with all stakeholders. Please do not hesitate to contact Rahul Advani (Policy Director, APAC) at radvani@ripple.com regarding any of the points raised in this letter or the Policy Paper.

Sincerely,

Ripple Labs Inc.

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[3] *See* Report, page 33. While the Report refers to "Ripple's XRP", we would like to note that XRP is independent of Ripple.
[4] *See* https://ripple.com/wp-content/uploads/2020/06/Ripple-Perspective-The-Path-Forward-For-Digital-Asset-Adoption-In-India-June2020.pdf, Ripple Policy Paper: The Path Forward for Digital Assets Adoption in India.

APPENDIX

1. Use cases for how blockchain applications and cryptoassets can benefit consumers in India

As outlined in the Report and Policy Paper, blockchain technology and cryptoassets represent a promising breakthrough, showing the potential to transform many sectors of the Indian economy. However, for any technology, success is based on its use cases as well as its ability to solve real-world problems and provide benefits to consumers and end-users. A variety of use cases have emerged as blockchain and digital assets technologies have matured, and we have highlighted two main use cases relevant to India. More details on these use cases are also outlined in the Policy Paper.[5]

a. Minimize friction & promote competition in cross-border payments

As highlighted in chapter 6.1 of the Report, easier cross-border transactions are a key benefit of blockchain technology and cryptoassets.[6] One such use case is in remittances.

Inward remittances into India accounted for approximately USD 83 billion in 2020,[7] which makes India the world's top receiver of remittances with a share of more than 12.8% of global remittances in 2020.[8] Even so, international remittances to India are costly, full of friction, and slow. Data from the World Bank indicates that the average cost of remittances globally is around 6.5%.[9]

The majority of banks currently use correspondent relationships - a network of bilateral accounts-based relationships - spread across the world to process payments originating from their corporate and retail clients. The market structure of correspondent banking injects significant friction, delay and costs in processing payments for the respondent banks due to the fragmented and bilateral nature of correspondent banking relationships,[10] which can materially affect recipients of remittances and small businesses in consequential ways. For example, evidence shows that remittances increase the disposable income of recipients, and in most

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[5] *See* Policy Paper, page 14.
[6] *See* Report, page 82.
[7] Based on World Bank data. *See*
https://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT?locations=IN
[8] Based on World Bank data. *See*
https://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT?most_recent_value_desc=true
[9] *See*
https://remittanceprices.worldbank.org/sites/default/files/rpw_main_report_and_annex_q42020.pdf,
Remittance Prices Worldwide Quarterly Report, December 2020.
[10] *See* https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf, BIS Quarterly Review March 2020, page 31.

cases remittance inflows represent an additional source of income. Furthermore, surveys show that remittance receiving households have a relatively higher propensity to save than households that do not receive remittances.[11] However, these remittance corridors are sometimes too small to warrant adequate attention from correspondent banking and therefore cannot reach the economies of scale needed in order to reduce costs, which acts as a barrier to financial inclusion.

Cryptoassets issued on blockchains that serve the same end-use as the incumbent correspondent banking model can offer a compelling alternative for consumers in India, while still being compliant with global KYC and AML/CFT requirements. Global multilateral bodies have also recognized the potential digital assets and blockchain technology have in facilitating faster cross-border payments.[12]

b. Micropayments

An additional benefit of blockchain technology and cryptoassets that has not been covered in the Report lies in their ability to support micropayments. A micropayment is a transaction involving low value payments (i.e., payments made for very small amounts). Traditional payment rails have high transaction costs, which means that payments below a certain level are not viable to process. Account-based payment systems incur substantial costs for the reconciliation of two ledgers, meaning they can only operate at a given scale and typically cannot support micropayments as a use case.

However, cryptoassets embedded in blockchains can be used as neutral bridge assets[13] to support frictionless value movement between fiat currencies that can be used to settle transactions on-chain.[14] Since there is no need for reconciliation across centralized ledgers, the settlement is virtually instantaneous, eliminating almost all settlement risk. As a consequence, the cost of transferring value is negligible. These structural features mean that certain cryptoassets (such as XRP) are well suited to support micropayments. While these payments are very small in value, the low cost and fast settlement time means that they are still viable to process.

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[11] *See* https://www.gpfi.org/sites/gpfi/files/documents/11-The%20Use%20of%20Remittances%20and%20Financial%20Inclusion.pdf, G20 Global Partnership for Financial Inclusion report on the use of remittances and financial inclusion, page 19.
[12] *See* https://blogs.worldbank.org/psd/paying-across-borders-can-distributed-ledgers-bring-us-closer-together, World Bank blog.
[13] XRP is an example of a neutral bridge asset. Party A deposits a fiat currency with the Sending Bank, who then converts that fiat currency into an equivalent amount of XRP on RippleNet and sends it to the Receiving Bank. The XRP is then converted back into another fiat currency by the Receiving Bank, before being collected by Party B. In other words, the presence of a native digital asset like XRP makes the blockchain a token-based system, relative to the account-based system of traditional finance.
[14] On-chain transactions are transactions that occur on a blockchain that are reflected on the distributed ledger. On-chain transactions are those that have been validated or authenticated and lead to an update to the overall blockchain network.

2. Policy recommendations

Ripple is supportive of the Report's position against a ban on cryptoasset activities,[15] and believes a ban would likely result in outcomes opposite of what is intended. As highlighted in the Report, a blanket ban on cryptoasset activities could have the unintended consequence of such activities going underground. Additionally, any benefits of innovations in such technology will be lost, ultimately affecting the end-user and consumer in India.

However, as is often the case with any disruptive technology, under-regulation can be equally as risky as over-regulation. Left unregulated, the cryptoasset industry is vulnerable to fraud, and therefore regulators and policymakers in India have the monumental challenge of striking a delicate balance between fostering innovation while ensuring sufficient safeguards.

Ripple firmly believes that these policy goals can be achieved through a clear regulatory framework for cryptoassets. To start with, any framework implemented should be technology-agnostic. In practical terms, this means that financial services using digital assets as a solution should not be treated differently from those that choose to leverage traditional architectures instead. It should also be principles-based, guiding market participants to regulatory and policy goals without imposing an overly prescriptive process. Finally, an ideal framework would use a risk-based approach that calibrates regulations according to the specific risks posed.

Ripple respectfully outlines some potential policy recommendations that can help achieve a clear regulatory framework. We believe that each of the policy proposals below – whether implemented separately or together – can succeed in achieving the policy goal of fostering innovation while ensuring sufficient safeguards.

a. Adopt a digital asset taxonomy aligned with global best practices

As noted in chapter 1.2 of the Report, there is significant diversity among cryptoassets.[16] It is also important to note that there is no single or generally recognised definition of cryptoassets at present. Chapter 8.2.2 of the Report recommends adopting clear definitions,[17] and Ripple is supportive of this proposal.

Ripple respectfully submits such assets should not be solely defined relative to a specific technology (e.g., cryptography), but, for the purposes of regulation, should instead fall under a broader heading such as "digital assets", and subsequently classified depending on the particular economic function and purpose they serve. Such an approach is consistent with that taken by other jurisdictions like the United

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[15] *See* Report, page 124.
[16] *See* Report, page 13.
[17] *See* Report, page 126.

Kingdom ("UK") and Singapore, which have issued classifications that do not depend on whether a business model uses distributed ledger technology or not.

The Report has provided a comprehensive comparison of these jurisdictions, along with other international jurisdictions, in chapter 7.[18] We have summarised the taxonomies for the UK and Singapore respectively in Table 1 & Table 2 below.

Regulated Tokens

a. Security tokens: These are tokens that amount to a 'Specified Investment' under the Regulated Activities Order, excluding e-money. These may provide rights such as ownership, repayment of a specific sum of money, or entitlement to a share in future profits. They may also be transferable securities or other financial instrument under the EU's Markets in Financial Instruments Directive II. These tokens are likely to be inside the FCA's regulatory perimeter.

b. E-money tokens: These are tokens that meet the definition of e-money under the Electronic Money Regulations. These tokens fall within regulation.

Unregulated Tokens

Any tokens that are not security tokens or e-money tokens are unregulated tokens. This category includes utility tokens which can be redeemed for access to a specific product or service that is typically provided using a blockchain platform.

The category also includes tokens such as Bitcoin, Litecoin and equivalents, and often referred to as 'cryptocurrencies', 'cryptocoins' or 'payment tokens'. These tokens are usually decentralised and designed to be used primarily as a medium of exchange. We sometimes refer to them as exchange tokens and they do not provide the types of rights or access provided by security or utility tokens, but are used as a means of exchange or for investment.

Table 1: Summary of the UK Financial Conduct Authority taxonomy for digital asset

Digital Payment Tokens

Refers to "any digital representation of value that is expressed as a unit; is not denominated in any currency, and is not pegged by its issuer to any currency; is, or is intended to be, a medium of exchange accepted by the public, or a section of the public, as payment for goods or services or for the discharge of a debt; and can be transferred, stored or traded electronically".

Digital tokens which constitute capital markets products

MAS will examine the structure and characteristics of, including the rights attached to, a digital token in determining if the digital token is a type of capital markets products under the Securities and Futures Act. This includes, but is not limited to a share, a debenture, a unit in a business trust, a securities-based derivatives contract, or a unit in a collective investment scheme, as defined under the Securities and Futures Act.

Table 2: Summary of the Monetary Authority of Singapore taxonomy for digital assets

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[18] *See* Report, page 93.

Taking into account the taxonomies of the UK and Singapore discussed above and in line with the Report,[19] we strongly support the recommendation that regulators and policymakers in India consider adopting a digital asset taxonomy consistent with such global practices, thereby providing clarity to the legal character of digital assets in India.

In line with global practices, we recommend that there be a clear distinction between payment tokens, utility tokens, and security tokens, as outlined below:

- **Payments or Exchange tokens**: to describe non-fiat native digital assets that are used as means of exchange and have no rights that may be enforced against any issuer;

- **Utility tokens**: to describe those digital assets that create access rights for availing service or a network, usually offered through a blockchain platform; and

- **Security tokens**: to describe tokens that create rights mirroring those associated with traditional securities like shares, debentures, security-based derivatives, and collective investment schemes.

b. Implement a risk-sensitive regulatory framework for digital assets

As highlighted in chapter 8.2.1 of the Report, applying existing Indian regulatory frameworks to cryptoassets is not practical given their unique nature and characteristics. Therefore, a separate regulatory framework for cryptoassets is needed for India.[20]

Taking into account the regulatory frameworks of the UK and Singapore discussed above and in the Report,[21] we request that regulators and policymakers in India also consider adopting a digital asset regulatory framework consistent with these global practices, in order to provide legal certainty and encourage innovation in the blockchain and cryptoassets sector in India.

We recommend that such a regulatory framework should align with the following principles outlined below:

- The regulatory framework should be technology-agnostic, and should not explicitly or otherwise endorse any particular technology. In practical terms, this means that financial services using digital assets as a solution should not be treated differently from financial services embedding legacy architectures, and there should be parity in the treatment of all technology;

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[19] *See* Report, page 127.
[20] *See* Report, page 126.
[21] *See* Report, page 93.

- Given the dynamic nature of digital assets, prescriptive regulation risks obsolescence. Prescriptive regulation could also have the unintended consequence of hindering innovation. Therefore, we recommend considering a principles-based regulatory framework, which will guide market participants to regulatory and policy goals, without imposing an overly prescriptive and onerous process in doing so; and

- The regulatory framework should use a risk-based approach to identify cryptoasset services that pose sufficient risk to warrant regulation, and where such risks are crucial to address. This is in order to build a simple, secure, and accessible cryptoassets ecosystem that will encourage innovation while mitigating any potential risks.

The recommended regulatory framework, as proposed above, should be forward-looking and flexible while providing regulatory certainty and consumer safeguards, and at the same time meet the policy goals of encouraging innovation in India with the principle of 'same risk, same activity, same treatment'.

c. Innovation sandboxes should be fostered and encouraged

An innovation sandbox is a formal regulatory program for market participants to test new and innovative products, services and business models with end-users in a controlled environment, while being subject to regulatory oversight.

However, the Reserve Bank of India ("RBI") currently does not offer any opportunity for cryptoassets in a sandbox environment, as the RBI's Enabling Framework for Regulatory Sandbox ("RBI Regulatory Sandbox Framework") includes cryptoassets in the negative list.[22]

In order to incentivize innovation and inform the development of a clear and consistent regulatory framework for digital assets, we believe innovation sandboxes should be encouraged, at the very least for specific use cases such as cross-border payments, as highlighted in this paper.

Therefore, we respectfully recommend amending paragraph 6.3 of the RBI Regulatory Sandbox Framework to remove "cryptocurrency / crypto asset services" from the negative list,[23] thereby offering service providers an opportunity to test the value proposition of this new technology in the Indian context.

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[22] *See* https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/ENABLING79D8EBD31FED47A0BE21158C337123BF.PDF, Enabling Framework for Regulatory Sandbox.
[23] *See* RBI Regulatory Sandbox Framework, page 6.

d. Public-private collaboration is essential

Finally, any policy framework intended to regulate cryptoassets should promote an active dialogue between regulators and market participants. Such public-private collaboration will lead to more appropriate and effective policy outcomes for the industry and consumers alike.

A collaborative forum that brings regulators and industry stakeholders together to build a rational and holistic framework for blockchain and cryptoassets would represent a substantial step forward toward achieving regulatory clarity in India, and we would support the formation of, and participation in, such a forum.