

Bitcoin-based pyramid schemes flourishing in regulatory vacuum

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According to data available with Tracxn, a website that provides financial information on start-ups, there are about 20 bitcoin firms in India now from just four in 2013. Photo: Bloomberg

Mumbai: Some small-time traders are taking advantage of the absence of rules governing crypto-currencies in India by creating multi-level marketing (MLM) or pyramid-like schemes with bitcoin as the base product.

The issue of multi-level marketing schemes is a global problem; however, these are now gaining traction in India owing to a lack of governing guidelines and the rapid rise in value of the crypto-currency, according to Digital Assets and Blockchain Foundation of India (DABFI), a self regulatory organization for bitcoin and blockchain companies.

“People form companies that promise lucrative returns and indeed give them for the first few months. This is in exchange for bringing in more members under them who will buy bitcoins and bring in newer members. This goes on till it explodes and the people lose all their money,” said Saurabh Agrawal, co-founder and chief executive officer, Zebpay, an app-enabled bitcoin exchange.

Typically, a small group of people come together to develop a code that will automatically transfer a certain percentage to users if someone in their network purchases bitcoin and brings in new

members. Once the code is established, it becomes difficult to find out the source of this whole operation as each user plays the victim when it collapses.

Since December 2016, the value of bitcoin has risen from around Rs57,000 to over Rs89,000 now, touching a high of Rs98,602 on 4 March, according to data available on the Zebpay website.

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A crypto-currency is a digital currency created through encryption techniques. Bitcoin is the most famous. Some others are: litecoin, peercoin, namecoin, ether and primecoin. In India, most companies are associated with bitcoin. No monetary authority in the world backs crypto-currency and most are trying to find ways to regulate the market. The Reserve Bank of India (RBI) has released a white paper on crypto-currencies and blockchain to understand them better.

DABFI—formed by the representatives of four bitcoin firms: Zebpay, SearchTrade, Unocoin and Coinsecure—is currently working on creating awareness among investors and firms against such programmes that lead to problematic transactions and mistrust around crypto-currencies.

Sathvik Vishwanath, CEO and co-founder of Bengaluru-based Unocoin, another platform to buy, sell and store bitcoin, says the idea behind a self-regulatory organization is to draft a firm policy to curb the misuse of blockchain technology and crypto-currencies.

“We thought that in the absence of any formal guidelines from the government, we can form some of our own regulatory policies and ensure some basic standard in the way bitcoin firms operate. This way, investors can be aware that companies not certified by us are probably not worth investing in,” Vishwanath said.

DABFI has appointed Nishith Desai Associates for legal support, it said in a statement last month. The law firm has already drafted a white paper on bitcoin, its industry application and legal perspectives.

“The fact is that the Indian crypto-currency market is not big enough for the government or regulators to get involved right now. They are watching how this space develops and are in constant conversation with some of us about what is going on. Once it reaches critical mass, then

formal guidelines should follow," said Vishal Gupta, CEO, SearchTrade, a search engine that pays its users in bitcoin for using it to search for something.

The government does not have any formal guidelines governing the crypto-currency trade happening in India. RBI does not recognize bitcoin or any crypto-currency as a legitimate form of currency.

In February, the central bank put out a cautionary note warning the public of the same and said anyone indulging in purchase or trade of crypto-currencies shall be doing so at their own risk.

"Globally, regulators are grappling with the need to stay lock-step with the developments, and initiatives such as DABFI will go a long way in ensuring that. Standardization will also mitigate the risk of fraud in the crypto-currency space that by definition operates on the fringes of regulation," said Mandar Kagade, a financial sector policy analyst.