

## **Demonetisation And Move Toward Cashless Economy**

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### **Abstract**

*The Government of India had demonetized banks notes on two prior occasions i.e. ones in 1946 and again in 1978. The main objective was to combat tax evasion by 'Black Money' held outside the formal economic system. Again, on 8<sup>th</sup> November 2016, the Government in India announced the demonetization of all Rs 500 and Rs 1000 banks notes of Mahatma Gandhi series. The Government claimed that the action would curtail the shadow economy and crack down on the use of illicit and counterfeit cash to fund illegal activity and terrorism. The demonetization scheme good result not only in people reviewing. Their need for hoarding cash both for transaction & precautionary purpose but also quicker adoption of the Digital Technology that enables cashless transactions. It will likely result in people adopting virtual wallets such as paytm, Ola money etc. This behaviorable change could be a game changer for our country. While gradual transition towards digitization a cashless economy will definitely help to curb corruption in the long run. The increased transparency and record of transaction will make it considerably difficult to hold back money and carry out under the table deals. The added convenience of using digital payment solutions and virtual wallets can't be ignored either. Prime Minister of India Narendra Modi announced the demonetization in a unscheduled live televised address at 20:00 Indian Standard Time (IST) on 8 November in the announcement, invalid past midnight and announced the issuance of new Rs. 500 and Rs. 5000 Banknotes of the Mahatma Gandhi New Series in exchange for the old banknote. The benefits of demonetization which include remonitization tax reforms, reducing stamp duties & tax rates. Incentives for tax compliance and facilitate the digital economy.*

### **Introduction**

Demonetization is an act of scrapping the legal tender status of a currency note. When new currency is introduced to replace the old one, government demonetizes the old currency. Demonetization is not a new concept to the world, as there have many instance of demonetization in the recent past. In 2015, the Zimbabwe government demonetized the Zimbabwean dollar to control the hyper inflation in the country. Another example is when member nations of European Union adopted Euro in 5002. Governments fixed the rate of exchange for varied national currencies who Euros and demonetized the old currencies.

The Government's decision to demonetize Rs 500 and Rs 1000 currency notes will also push India towards a cashless economy. "This one decision will change the way the people spend and keep their money." asserted Finance Minister Mr. Arun Jaitley India has been trying to push the country's cash dependent economy towards paperless transactions. It published a draft paper of sops and incentives, which may be considered for those opting for online and plastic payments. However, the move has remained nascent at best till now. High-denomination banknotes account for 86% of the 164000 crore rupees of currency in circulation. With inflation raising prices, most people preferred higher denomination notes. However, by now taking steps to discourage high value notes, the

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government could push more people to opt for e-commerce and plastic money. Analysts believe the move to scrap high demonization notes will now force people to use their accounts and financial technology for transactions. Estimate say the mobile commerce market in India will grow from a current \$2 billion to \$19 billion by 2019.

Prime Minister Mr Narendra Modi announced demonetization of the current series of Rs 500 and Rs 1000 notes from midnight of November 8, 2016 . The move is also expected to weed out large caches of black money. "to break the grip of corruption and black money . We have decided that the 500 and 1,000 rupee currency notes presently in use will no longer be legal tender from midnight that is 8 November, 2016". The prime Minister said in a surprise televised address to the nation . "This means that these notes will not be acceptable for transaction from midnight onwards." After a one day shutdown of all banks and ATMs, new 500 and 2,000 rupee denomination notes are being issued from Thursday November 10 , 2016, by the Reserve Bank of India. The prime Minister Mr Modi had promised to combat the menace of black money when he came to power two-and-half years back, pledging to crack down on parallel economy in India which has seen tax to GDP ratio being abnormally low while the Indian economy grew by 30% during 2011 and 2016, the circulation of money in the economy increased by 40 % However circulation of Rs 500 notes increased by 76% and of Rs 1000 notes by an astounding 109% . Which means the demand for high denomination notes grew at a faster rate, causing suspicion that much of this was being hoarded as black money.

According to Expert :

According to experts, in short run there will about 5% to 7% dent in the job market. especially in real estate and allied activities like cement, construction iron etc. However , some businesses which receive direct benefit due to this cashless drive like Fin-tech, digital payment companies have started hiring exponentially to meet the increased demand. Many ecommerce companies have started 'wallet on Delivery' in place of 'cash on Delivery' .some people are criticizing the demonetization move on the point that enough preparation was not done. Even banks did not have any idea about this move as it was top secret project of the government which was known to just few trusted people. However, preparation means involving more people and more involvement might have defeated the very purpose of this move that was to combat black money.

#### **History of Demonetization:**

The Indian government has demonetized currency notes. RBI first demonetized Rs. 1000 and Rs. 10000 banknotes in January 1946. Banknotes for Rs. 1000, Rs. 5000 and Rs. 10000 were reintroduced in 1954. However, Rs. 1000 Rs. 5000 and Rs 10000 were once again demonetized in January 1978 once again. In 1978 the then government said the move was aimed tackling the issue of the black money which had grown to large proportions at the time. The measure was enacted by passing the high denomination bank note (Demonetization) Act, 1978. The law's preamble said that this was an Act to provide in the public interest for the demonetization of certain high denomination bank notes and for matters connected therewith or incidental thereto.

#### **Objectives of Demonetization:**

According to the government, demonetization is intended to combat untaxed black money, rampant corruption, encourage cashless transactions, checkhawala transactions to counter terrorist activities and to bring more accountability in the informal sector of the economy. India's black money, has been estimated by the World Bank in 2010 to be worth about on fifth of the Gross Domestic Product (GDP). In a country where 90% transactions are carried out on cash basis it was a revolutionary move to transform from cash to cashless transactions. The currency notes of Rs. 500

and Rs.1000 which constituted nearly 86% of the whole money circulation in the country, were demonetized on November 8, 2016. The Government gave the option, either to deposit the scrapped currency notes in banks or exchange them against new currency. The main objectives of demonetization are:

- To curb black money (Untaxed liquid assets)/ corruption.
- To discourage cash system.
- To combat inflation.

According to a World Bank Report, bank account penetration in India 2014 was just 53%, out of which only 15% users used their accounts to make or receive payments. In 2014, the NDA government announced Pradhan Mantri Jan Dhan Yojna to increase the financial inclusion of those who never had an account in a bank. Under this scheme, 250 million bank accounts have been opened in two years. As per RBI reports bank branches increased by 5% per year but Automated teller Machine (ATM'S), debit cards and card swiping machine have doubled in four years and online transactions have grown 20 times in sixes years to 2016. All these data shows a gradual shift towards cashless economy. Demonetization has sped up this transition.

#### **Impact of demonetization in India:**

Prime Minister Mr. Narendra Modi announced demonetization of current series of Rs 500 and Rs 1000 notes from Mid night to Nov 8, 2016 The move is also expected to weed out Large catches of black money. "To break the grip of corruption and black money, The Prime Minister Narendra Modi had promised to combat the menace of black money when he came to power two-and-half years back, pledging to crack down on parallel economy in India which has seen tax to GDP ratio being abnormally low. Which means the demand for high denomination notes grew at a faster rate, causing suspicion that much of this was being hoarded as black money?"

This measure was necessary to maintain the financial integrity of our economy. "Said Secretary Economic Affairs Shaktikanta Das Demonitisation is a move which had been suggested by several quarters.

The Move will also check fake note flows, a bane which has been dogging the Indian financial markets for years. The Reserve Bank said while the Indian currency's security features have not "been breached". the fake notes being pushed by Pakistan's spy agencies were similar to legal tender and were causing confusion in the market. currently there are 16.5 billion legal Rs 500 notes and 6.7 billion Rs 1000 notes. But estimates point to larger numbers of high denomination notes circulation in the market, clearly pointing to fake currency being pushed into India in large numbers. Some Impacts of Demonetization in India are as follows:-

- **Black Money:** Black money stored in the form of Rs 500 and 1000 Rs notes will be taken out of our system. As predicated by ICICI Securities Primary Dealership the government's plan to scrap Rs 500 and Rs 1000 notes will uncover up to Rs 4.6 Lakh crore in black money.
- **Real estate may see significant course correction:** The demonetization decision is expected to have far reaching effects on real estate. Resale transactions in the real estate sector often have a significant cash component as is reduces incidence of capital gains tax. Black money was responsible for sharp appreciation of properties in metros; real estate price may now see a sharp drop.
- **Political parties in crisis ahead of polls:** With nearly five state elections in 2017, demonetization has stunned political parties. Especially, in large states like Punjab and

Uttar Pradesh, cash donations are a huge part of "election management". In one stroke, big parties will find themselves hamstrung as cash hoards are often undeclared money, Parties will have to completely rejig campaign strategies in light of expected cash crunch.

- **Terror funding:** Fake Indian currency Notes (FICN) network will be dismantled by the demonetization measures. Taking out 500 and 1000 rupee notes out of circulation will have a lasting impact in Jammu and Kashmir, North-eastern states and Naxalite hit states.
- **Moving towards digital payments:** Demonetization will likely result in people adopting virtual wallets such as PAYTM, Ola Money etc.; This behavioral change could be a game changer for India.
- **Temporary chaos and confusion** : Public will face minor problem for a few days owing to the scarcity of lower denomination notes in the system.

#### **Effort of Government towards demonetization:**

The Government has announced Lucky GrahakYojana and DigiDhanVyaparYojana to promote digital payments. Chief Executive Officer of NITIAayog Amitabh Kant said, Lucky GrahakYojana is to encourage consumers while DigiDhanVyaparYojana is to encourage merchants for transition to digital payments. Mr. Kant said National Payment Council of India will announce 15000 winners and 1000 rupees each for the next 100 days, starting this Christmas. He said, 7000 weekly awards and maximum award of 50 thousand rupees each for merchants will be given under DigiDhanVyaparYojana. He said, mega awards under the two schemes will be announced on the birthday of Dr. B R Ambedkar on 14<sup>th</sup> April. Prime Minister NarendraModi has described the Lucky GrahakYojana and DigiDhanVyaparYojana as a strategic push towards increased cashless transactions. In a series of tweets, Mr. Modi said, the two schemes will give a big boost to move towards and corruption free India.

The Government and financial institutions could also build a credit history using e-transactions to give consumers easier credit terms and higher credit flows. Tax collections in medium term will increase and bank deposits will also rise. "India cannot afford to live with black money and longer. Honesty, integrity & ethical conduct are requirements of India's development." said the Finance Ministry. The Government will be keeping an eye on all cash deposit of over Rs 2.5 lakh and could if it finds that the deposit does not match tax returns, impose a penalty of 500% on the income deposited besides extracting taxes on it. According to a senior official, "We would be getting reports of all cash deposited during the period of 10<sup>th</sup> November to 30<sup>th</sup> December, 2016 above a threshold of Rs. 2.5 lacs in every account. the department would do matching of this with income returns filed by the depositors. And suitable action may follow." If a huge amount of cash is deposited which does not match with income declared, "this would be treated as the case of tax evasion and the tax amount plus a penalty of 500% of the tax payable would be levied as per the section 270(A) of the income tax Act." Section 270 A of the IT Act provides that in case of under-reporting of income flowing from deliberate misreporting, the penalty which may be imposed can be 500% of the amount under – reporting, but not due to willful mis-reporting then the penalty can be 50% of undeclared income. However, cash deposits of up to Rs. 2.5 lakh will not be scrutinized and ordinary people who make such deposits will not be harassed. People need not worry about such small amount of deposits up to Rs. 1.5 of 2 lacs, since it would be below the taxable income. There will be no harassment by Income Tax Department for such small deposits made.

**Moving towards cashless Economy:**

Well before the November 9 demonetization of high denomination notes, banks in sync with the Reserve Bank of India has been working on development of different technology – based solutions for electronic transfer of money. There were already systems available in the banks through which one could transfer funds from one bank of branch to the order, in a matter of a few hours. That itself was a good facility replacing quite fast the age-old money transfer through cheques which had to be, first received in the beneficiary, then deposited in the branch, sent for clearing before the funds get transferred in the designated account. It is not that the cheques have gone altogether; but their usage is dropping rapidly.

At these measures were underway even before November 9, but the sense of urgency was a missing link. Besides, different payment networks did not seem to be in perfect coordination while electronic payments for the sale of merchandise and services were restricted to credit or debit cards used either through laptops or the limited point of sale (POS) machines available with the traders or the service providers. There was no sense of urgency, because there was no tearing necessity.

After the launch of BHIM – App, the latest is Bharat QR Code which works on the model of Paytm wherein the customers scans the QR Code of the merchandise and then transfers the money from his/her wallet. The only difference with Bharat QR Code is that just a BHIM, the customers at the merchandise point does not have to create and then draw money from the wallet. The funds are directly transferred from the customer's account and transferred instantly to that of the merchant or service provider. Unlike credit or debit cards used at the points of sales, there are no charges involved. There is an ease of using App with no cost. As far as the integrity and safety of the system is concerned, the RBI is giving assurance about it. "Our systems are not only comparable to any system anywhere in the world, our systems also do set standards and good practices for the world to follow. We remain vigilant for ensuring safety and soundness of the payment systems and are committed to customer safety and convenience." according to Mr. R Gandhi, Deputy Governor of the RBI.

In a cashless economy, where major transactions are done through cards or digital payments, the physical usage of currency remains low, which lowers down the chances of unaccountable transactions. India remains to be a very cash reliant economy than any other country in the world. even many multinational e-commerce companies like Amazon, Uber etc. accept cash in India, the only the country in the world where the option of cash on delivery (COD) is still prevalent, where even till date 70% online transactions are via COD. By adopting the policy of demonetization, the government has put the cash economy out of gear in the people could be brought into the cashless economy. the Gradual transition towards digitization and a cashless economy will definitely help curb corruption in the long run. The increased transparency and record of transactions will make it considerably difficult to hold black money and carry out under the table deals. The added convenience of using digital payment solutions and virtual wallets can't be ignored either. while virtual wallet firms like Paytm are going the extra mile to make things easy for everyday consumers and small vendors, solutions like Happay are working their way towards making business transactions go cashless. Automated expense reporting solutions, coupled with their Visa and Master Card integrated credit cards, have gained significant traction over the past few days for their complete food, travel, medical and ad-hoc, cash free solutions. A cashless economy will give the following positive effects on the economy.

- It will increase the taxation base. India's informal economy contributes 45% in GDP and 80% in employment. It means transactions of millions remain unaccounted and untaxed. Currently only 1% of India's population pays income tax as per Income Tax Department. In the long run, with this system most of this sector will be compelled to function in formal

framework. It will also reduce the instance of tax avoidance.

- Clean and more transparent business transactions and money transfers.
- Improved financial inclusion and credit access through the linkage of all welfare activities with bank accounts. It will not only increase welfare for the people but would assist in creating a sense of belonging and faith in the banking system.
- Reduced money laundering due to easy traceability of transactions.
- Control on the issuance of fake currency and counterfeiting. As per official reports, an estimated 250 out of every million Indian Bank notes were fake.
- It will curb the parallel shadow economy (black economy) which runs majority on cash basis. Cashless transactions are track able and more transparent.
- Efficiency in welfare programs as money can be easily transferred to the accounts of the recipients. It will eliminate the role of intermediaries who usurp the share of welfare money spent on people. This cashless regime represents transparency and people will get all the benefits directly in their account without paying any bribe to any one.
- Improved climate for foreign investments.
- Good Governance.
- In the year 2015, RBI spent Rs. 27 billion on currency issuance and management. Cashless economy will reduce such costs.
- Nobel laureate Kailash Satyarthi and other working to fight human trafficking said that the note ban had led to a huge fall in sex trafficking. Satyarthi said the demonetization would be effective in combating exploitation of children as well as corruption and would be a great obstacle to traffickers. However, 2 months later he expressed his disappointing on Rs5000 notes being pushed into human trafficking in absence of concrete steps.
- The demonetization has badly hit Maoist and Naxalites as well. The surrender rate has reached its highest since the demonetization is announced. It is said that the money these organizations have collected over the years have left with no value and it has caused them to reach to this decision. The move also reportedly crippled communist guerrilla groups ( Naxalites) financing through money laundering.
- As of November 2016, Indian Railways did not have the option to make payment with cards at the counters. After the demonetization move, the government announced to make card payment options available at railway counters in the country. The railways placed an order for 10000 card reader machines in January 2017.

Cashless economy cannot be achieved in few days or months, it is a long process. People have to be prepared to adapt this change. Question arises why cash is no much important? In a country like India where poverty, illiteracy and unemployment are the major issues, cash in hand symbolized safety, security and respect. Government should assure the basic necessities and focus on developing infrastructure specially in rural areas. Special drives through schools, colleges, panchayats etc. Can help create awareness about cashless/ banking transactions. Financial literacy is a must for bringing more and more people to digital platform. Digital payment or payment through banks eg. paying expenses and salary of staff through bank accounts instead of paying cash should be encouraged.

**Conclusion :**

The withdrawal of Rs. 500 and Rs. 1000 notes, accounting for 85 per cent of the currency value in circulation brought in a sheer necessity for an effective and urgent alternative to cash. The

present Govt. India made a commitment about making Indian society less cash dependent in his drive to clean up the economy from the scourge of black money and corruption, put the entire regulatory, operational and policy- making machinery into top gear with the result that within four months, not one but several e-payment options have been developed, tested and launched. They can all be used through the low cost smart phones. The best thing about these Apps is that they are targeted largely at the excluded strata and would be catalytic in the world's biggest financial inclusion programme. After the launch of BHIM- App, the latest is Bharat QR Code which works on the model of Paytm where in the customer scans the QR code of the merchandise and then transfers the money form his/her wallet. The only difference with Bharat QR Code is that Just as BHIM, the customers at the merchandise point does not have to create and then draw money form the wallet. The funds are directly transferred from the customer's account and transferred instantly to that the merchant or service provider. Unlike credit or debit cards used at the points of sales, there are no changes involved. There is an ease of using App with no cost. As far as the integrity and safety of the system is concerned, the RBI is giving assurance about it. " Our systems are not only comparable to any system anywhere in the world, our systems also do set standards and good practices for the world to follow. We remain vigilant for ensuring safety and soundness of the payment systems and are committed to customer safety and convenience." according to Mr. R Gandhi, Deputy Governor of the RBI.

The government has constituted a committee under the Chairmanship of Mr. Ratan Watal, Principal Advisor, NITI Ayog, to suggest measures for encouraging digital payments. Having examined the regulatory and legislative framework, the Watal Committee recommended that the payment and settlement systems Act 5007 be amended for a better regulatory governance, competition and innovation, consumer protection, open access, data protection and security, and penalties for offences. Accepting these recommendations, the legislative changes have been brought in the Finance Bill of 2017. The demonetization scheme would result not only in people reviewing their need for hoarding cash- both for transaction and precautionary purpose – but also in quicker adoption of the digital technology that enables cash-less transactions.

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