



<http://www.casestudiesjournal.com/>

Impact Factor: 4.428

## **Cryptocurrency: How Regulators Can Strengthen Digital Currency Regulations within the Current Regulatory Framework in Nigeria**

### **Author's Details:**

**Emem Udoh**-Institute of Corporate Law & Business Development

**Elizabeth C. Ogwo**-Institute of Corporate Law & Business Development

**\*Corresponding Author: Email: ememudoh2001@gmail.com**

### **Abstract:**

*The widespread use of digital currency as an alternative method of payment and an investment tool has led to a growing digital ecosystem over the years. The use of digital currency however has come with perceived threat to the financial sector. Governments around the world are behind the curve, continuing to wrestle with how to develop effective public policy measures to regulate its adoption and use. Thus, this paper will explore the current regulatory framework on digital currency in Nigeria, with major focus on ways these regulations can be strengthened*

**Keywords:** Digital Currency, Cryptocurrency, Regulation

### **1.0 Introduction**

Nigeria raised early concerns surrounding the popularity and appeal of digital currencies, specifically Cryptocurrency. On the 5<sup>th</sup> of February 2021, the CBN released a ruling that orders all financial institutions to stop facilitating crypto transactions and desist from transacting with entities engaging in crypto. The statement also instructed all banks and financial institutions to close accounts of individuals or entities engaging in this type of transaction. The CBN warned in the letter that breaches of the directive will attract severe regulatory sanctions<sup>1</sup>. This ruling was made following a few circulars issued by the Central Bank of Nigeria (CBN) to banks and financial institutions and other pronouncements made by the Securities and Exchange Commission (SEC) and Nigeria Deposit Insurance Corporation (NDIC) within 2017 to 2020<sup>2</sup> on the use of Cryptocurrency.

Despite the ban on Cryptocurrency by the Nigeria government, Cryptocurrency continue to bloom and flourish in the country as Nigeria is said to be one of the largest Cryptocurrency markets in the world, accounting for Cryptocurrency transactions worth US\$566 million in five years<sup>3</sup>. The ban has had little to no effect on Cryptocurrency usage in the country as many have adjusted to the current situation, Cryptocurrency users have found new ways to buy and invest in Bitcoin and other digital currencies in Nigeria.

Consequently, a ban on the use of Cryptocurrency in Nigeria may be futile considering the fact government around the world are adopting Cryptocurrency and other digital currencies, many are considering ways to regulate and adopt same, there is also growing interest among central banks to create a digital version of fiat, or traditional, money. For example, the E-Naira was launched by President Muhammadu Buhari, on Monday 25

<sup>1</sup> "Why Crypto Is Booming in Nigeria despite Govt Ban |" (September 6, 2021) <> accessed November 26, 2021.

<sup>2</sup> "Letter to Banks on Crypto" (PDF). Central Bank of Nigeria(www.cbn.gov.ng) <> accessed November 26, 2021. Also

"Cryptocurrency: We Acted in Nigerians' Best Interest - Emefiele" (Cryptocurrency: We Acted in Nigerians' Best Interest - Emefiele) <> accessed November 26, 2021.

<sup>3</sup> Magdalene Teiko Larnyoh, "Twitter CEO Jack Dorsey Says Nigerians Will Lead Bitcoin Charge despite Cryptocurrency Ban" (Business Insider Africa June 14, 2021) <> accessed November 29, 2021.

October 2021, which is the digital version of the fiat and Africa's first central bank digital currency (CBDC)<sup>4</sup>. It is therefore obvious that the Nigerian government has perceived the futility in its attempt to ban the use of Cryptocurrency, as it has been revealed that The Securities and Exchange Commission (SEC) is working with the Central Bank of Nigeria (CBN) for a better understanding and regulation of Cryptocurrencies in the country<sup>5</sup>.

## 2.0 An Overview of Digital Currency and Cryptocurrency

Digital currency is any currency, money, or money-like asset that is primarily managed, stored or exchanged on digital computer systems, especially over the internet<sup>6</sup>. A major type of digital currency is Cryptocurrency, others include virtual currency and central bank digital currency (e.g E-naira). Digital currencies exhibit properties similar to traditional currencies, but generally do not have a physical form, unlike currencies with printed banknotes or minted coins. This lack of physical form allows nearly instantaneous transactions over the internet and removes the cost associated with distributing notes and coins, thus enabling ownership transfer across governmental borders<sup>7</sup>. Digital currency can either be centralized or decentralized. Where there is a central point of control over the money supply (e.g. a bank) it is said to be centralized and a typical example of this is the Central Bank Digital Currency. Where the control over the money supply is predetermined or agreed upon democratically, it is decentralized and a popular example of a decentralized digital currency is Cryptocurrency.

Cryptocurrency is a digital asset designed to work as a medium of exchange wherein individual coin ownership records are stored in a ledger typically known as a Blockchain existing in a form of computerized database using strong cryptography to secure transaction records, to control the creation of additional coins, and to verify the transfer of coin ownership<sup>8</sup>. Units of Cryptocurrency are created through a process called mining, which involves using computer power to solve complicated math problems that generate coins. Users can also buy the currencies from brokers, then store or spend them using cryptographic wallets.

Cryptocurrency does not exist in physical form (like paper money) and is not issued by a central authority. Their prices are generally determined by several factors, including demand and supply, competition, news development and its regulation. The most common Cryptocurrencies are Bitcoin, Ethereum, Ripple, Litecoin, Dodge among others<sup>9</sup>.

Cryptocurrency and other digital currencies gained an increasing popularity due to its uses. They are used for online trading, to make payments online, to privately carryout cross border transactions, among others. Most Nigerian users use digital currencies such as Bitcoin to carryout foreign transactions due to the strict foreign exchange laws, taking advantage of the decentralized nature of the currency. The ban by the Central Bank of Nigeria does not affect this use of Cryptocurrency for inter-border transfer as it is not facilitated by a financial institution. Digital currencies are also used as investment tools and a store of wealth<sup>10</sup>. For example, they are used to hedge against inflation as naira continues to lose its value. Despite the positive uses of Cryptocurrency and other digital currencies, they have been used as tool to facilitate cybercrime such as money laundering and are susceptible to theft and fraud as there are a lot of investment schemes surrounding these currencies. Also, due to the fact that Cryptocurrency is a decentralized, peer-to-peer payment network that allows individuals to share information with one another without the need for a middleman, Cryptocurrency circumvents the control

<sup>4</sup> "Enaira Launched by the Nigeria - Google Search" (www.google.com) <> accessed November 26, 2021.

<sup>5</sup> "CBN, SEC Working on Regulatory Guideline for Cryptocurrency Trading - Nairametrics" (April 16, 2021) <> accessed November 26, 2021.

<sup>6</sup> Wikipedia Contributors, "Digital Currency" (WikipediaNovember 8, 2019) <> accessed November 26, 2021.

<sup>7</sup> ibid

<sup>8</sup> Andy Greenberg (20 April 2011). "Crypto Currency". Forbes. At Wikipedia Contributors, "Cryptocurrency" (WikipediaFebruary 15, 2019) <>. , accessed November 26, 2021.

<sup>9</sup> Andrew Bloomenthal, "What Determines the Price of 1 Bitcoin?" (Investopedia2019) <> accessed November 26, 2021.

<sup>10</sup> "Brave New Coin" (bravenewcoin.com) <> accessed November 26, 2021.

central banks have over money supply. Powered by Blockchain technology, no single third party is in control of the transactions and data stored on the distributed ledger. As such, the use of Cryptocurrency as a means of payment has the potential to undermine the ability of the state to track currency movement, thereby propelling the Nigerian government to curtail Cryptocurrencies, in some cases referring to them as a direct threat to national security and the stability of the global financial system. It is clear that the emergence of digital currencies has revolutionized the way transactions are carried out over the internet, however it comes with inherent risks hence the need to regulate its adoption and use.

### 3.0 The Current Regulatory Framework on Digital Currency in Nigeria

There is currently no harmonized legal and regulatory framework regarding the status and treatment of digital currencies and assets in Nigeria. The Central Bank of Nigeria (CBN) and the Securities and Exchange Commission, Nigeria (SEC) assert overlapping jurisdictions for market participants transacting in digital currencies or other digital assets<sup>11</sup>.

The Banking sector is primarily regulated by CBN<sup>12</sup>. The CBN, in its circular issued on the 12<sup>th</sup> of January 2017 (the CBN Circular), stated that in the absence of substantive regulation or a decision by the CBN, all banks and other financial institutions in Nigeria should ensure that they do not use, hold, trade or transact in any way in digital currencies<sup>13</sup>. Also stating that digital currency is not a legal tender in Nigeria, the CBN further indicated that the use in Nigeria of digital currencies issued by unregulated and unlicensed entities is contrary to its mandate as the statutory issuer of legal tender in Nigeria<sup>14</sup>. While defining Cryptocurrencies as 'digital or virtual currencies issued by largely anonymous entities and secured by cryptography', and defining cryptography as 'a method of encrypting and hiding codes that prevent oversight, accountability and regulation, the CBN in a press release dated 7<sup>th</sup> February 2021, declared that the use of Cryptocurrencies in Nigeria is a direct contravention of existing law<sup>15</sup>, it further directed the closure of all accounts owned by individuals or entities transacting in or operating Cryptocurrency exchanges in Nigeria<sup>16</sup>.

On the contrary, the Securities and Exchange Commission (SEC) in its 'Statement On Digital Assets And Their Classification And Treatment' (the Statement)<sup>17</sup>, issued on the 14<sup>th</sup> of September 2020, the SEC stated that digital cryptoassets are securities that fall within the SEC's regulatory purview and it reiterated this stance in a press release dated 11<sup>th</sup> February 2021<sup>18</sup>. Furthermore, according to the SEC, all digital asset token offerings (DATOs), initial coin offerings (ICOs), security token ICOs and other blockchain-based offers of digital assets within Nigeria or by Nigerian issuers or sponsors, or foreign issuers targeting Nigerian investors, shall be subject to regulation by the SEC. It should be noted however that in line with the CBN's stated position on Cryptocurrencies<sup>19</sup>, the SEC has suspended the admission to its Regulatory Incubation (RI) programme<sup>20</sup> of all

<sup>11</sup> Chukwudi Ofili and others, "The Law Reviews - the Virtual Currency Regulation Review" (thelawreviews.co.ukSeptember 2, 2021) <> accessed November 26, 2021.

<sup>12</sup> Section 2 of the Central Bank of Nigeria Act 2007 establishes the objectives of the CBN, which include issuing legal tender currency in Nigeria and promotion of a sound financial system

<sup>13</sup> CBN, 'Circular to Banks and Other Financial Institutions on Virtual Currency Operations in Nigeria' (circular, 12 January 2017), <https://www.cbn.gov.ng/out/2017/fprd/aml%20january%202017%20circular%20to%20fis%20on%20virtual%20currency.pdf>

<sup>14</sup> Central Bank of Nigeria Act 2007 S2(b)

<sup>15</sup> Central Bank of Nigeria (CBN), 'Response to Regulatory Directive on Cryptocurrencies' (press release, 7 February 2021), <https://www.cbn.gov.ng/Out/2021/CCD/CBN%20Press%20Release%20Crypto%2007022021.pdf> accessed November 26, 2021

<sup>16</sup> CBN, 'Letter to all Deposit Money Banks, Non-Bank Financial Institutions and Other Financial Institutions' (circular, 5 February 2021), <https://www.cbn.gov.ng/Out/2021/CCD/Letter%20on%20Crypto.pdf> accessed November 26, 2021

<sup>17</sup> Securities and Exchange Commission, Nigeria (SEC), 'Statement On Digital Assets And Their Classification And Treatment' (circular, 14 September 2020), <https://sec.gov.ng/statement-on-digital-assets-and-their-classification-and-treatment> <> accessed November 26, 2021.

<sup>18</sup> SEC, 'Press Release on Cryptocurrencies' (press release, 11 February 2021), <https://sec.gov.ng/press-release-on-cryptocurrencies>. <> accessed November 26, 2021.

<sup>19</sup> *ibid*

persons affected by the CBN directive until they are able to operate bank accounts within the Nigerian banking and financial system.

Also, the law in Nigeria (including the Investment and Securities Act and the SEC Rules) does not provide for the regulation of digital currencies in Nigeria. The SEC, via the Statement<sup>21</sup> maintains its position that it will be taking a three-pronged approach to regulate innovation in the Cryptocurrency sector; this approach includes safety, market deepening, and providing solutions to problems that will guide its regulations, strategy and interactions with innovators seeking legitimacy and relevance in this emerging industry. In the same Statement, the SEC indicated that it will regulate virtual assets when the character of the investment qualifies as securities. It is the position of the SEC that, unless proven otherwise by the issuer or sponsor, digital cryptoassets are securities. Further in the Statement, any person (individual or corporate) whose activities involve any aspect of blockchain-related and virtual digital assets services, including but not limited to reception, transmission and execution of orders on behalf of other persons, dealers on their own account, portfolio management, investment advice, custodian or nominee services, must be registered with the SEC<sup>22</sup>.

Finally, one of the argument against the adoption of digital currencies is that it is a tool to facilitate money laundering. The main legislation governing money laundering in Nigeria is the Money Laundering (Prohibition) Act 2011 (as amended) (MLPA). In addition to this legislation, the CBN released the CBN (Anti-money Laundering and Combating the Financing of Terrorism in Banks and Other Financial Institutions in Nigeria) Regulations 2013 (the CBN AML/CFT Regulations) to regulate financial institutions under its regulatory purview and the SEC also released the SEC (Capital Market Operators Anti-Money Laundering and Combating the Financing of Terrorism) Regulations 2013 (the SEC AML/CFT Regulations). The MLPA, the CBN AML/CFT Regulations and the SEC AML/CFT Regulations neither envisage nor treat directly the use of digital currencies for money laundering activities.

#### **4.0 Recommendations on How Regulators can Strengthen Digital Currency Regulations.**

Following from the statement issued by the Securities and Exchange Commission (SEC) on the 14<sup>th</sup> of September 2020<sup>23</sup> which stated that digital cryptoassets are securities that fall within the SEC's regulatory purview, which stance was further reiterated in a press release dated 11th February 2021, it is therefore within the jurisdiction of SEC to effectively regulate digital cryptoassets which could be done in collaboration with the CBN and other regulatory bodies. Below are some recommendations on how the adoption and use of digital currencies can be effectively regulated thereby strengthening the current regulatory framework of digital currencies in Nigeria.

- i. The Securities and Exchange Commission (SEC) should consider amending the Investment and Securities Act and the Regulations with a view to extending their scope to cover the regulation of the hitherto unregulated digital currencies and Crypto Assets Market. For example, Estonia amended its Money Laundering Act and Terrorism Financing Prevention Act, respectively, to bring Crypto Wallets and Exchanges under its regulatory regime.
- ii. SEC may also seek the enactment of bespoke legislation that will target specifically, all aspects of the Crypto Assets Market, and digital currencies generally thereby providing for a comprehensive regime of regulation able to address the peculiarities of the market. For example, Malta took this approach when it enacted the Virtual Financial Assets Act<sup>24</sup>. It is therefore recommended that SEC

<sup>20</sup> The Regulatory Incubation programme sets out basic requirements for fintech firms to operate under prescribed, but limited, provisions for a specified period

<sup>21</sup> SEC, 'Statement On Digital Assets And Their Classification And Treatment'. Supra footnote 14

<sup>22</sup> *ibid*

<sup>23</sup> Securities and Exchange Commission (SEC) 'Statement On Digital Assets And Their Classification And Treatment' (the Statement) of 14th September 2020

<sup>24</sup> "The Malta Virtual Financial Assets Act" (Grant Thornton Malta) <> accessed November 28, 2021.

should as a matter of urgency enact new regulations for digital currencies and Crypto Assets Market under its existing powers in Sections 13 and 313 of the ISA.

- iii. It is paramount that the regulating body classifies crypto assets. This is fundamental to the regulation of the Crypto Assets Market as whatever regulations SEC enacts must define the type of crypto assets that will fall within its regulatory ambit. Global best practices tend to classify crypto assets into 3 functional models, i.e. assets that are investment tools (Security Tokens), assets that operate as a medium of exchange (Payment Tokens) and assets that give a right to participate in digital resources (Utility Tokens). In terms of SEC's statutory jurisdiction, by virtue of Sections 13 (a) and 315 of the ISA that Security Tokens could fall within the definition of Collective Investment Schemes and Securities (i.e. under subsection (d)). With regards to Payment Tokens and Utility Tokens, there is no aspect of them that can be deemed to be an investment tool or a security, then they should not fall under the regulatory jurisdiction of SEC.
- iv. It is also important for the body(s) regulating digital assets in Nigeria to have a consensus with the authorities of other countries in order to provide a proper regulatory regime. This is important for the harmonization of the law as digital transactions cut across different jurisdictions. The consensus should be aimed towards making rules that would solve jurisdictional problems in digital transactions and these rules should be of general application.

## 5.0 Conclusion

Governments around the world are adopting digital currencies, with these changing global financial trend, Nigeria's financial regulatory agencies should take the lead in building a solid financial system and regulation that would accept the contemporary technology. Despite the potential for abuse connected with the use of digital currency, it should not be rejected in its entirety; rather, rigorous regulations should be put in place to limit its misuse. Responsively, there are ongoing efforts by the CBN, the SEC and other regulators to establish a unified regulatory framework for virtual currencies in Nigeria<sup>25</sup>. Following the engagement of the regulators, it is expected that a harmonized regulatory framework for the treatment and use of the digital currencies in Nigeria will be issued.

## REFERENCES

- i. Bloomenthal A, "What Determines the Price of 1 Bitcoin?" (Investopedia2019) <<https://www.investopedia.com/tech/what-determines-value-1-bitcoin/>> accessed November 26, 2021
- ii. "Brave New Coin" (bravenewcoin.com) <<https://bravenewcoin.com/insights/10-awesome-uses-of-cryptocurrency>> accessed November 26, 2021
- iii. "CBN, SEC Working on Regulatory Guideline for Cryptocurrency Trading - Nairametrics" (April 16, 2021) <<https://nairametrics.com/2021/04/16/cbn-sec-working-on-regulatory-guideline-for-cryptocurrency-trading/>> accessed November 26, 2021
- iv. "Cryptocurrency Ban: SEC, CBN to Provide Level Field for Investments" (February 21, 2021) <<https://www.premiumtimesng.com/news/more-news/444329-cryptocurrency-ban-sec-cbn-to-provide-level-field-for-investments.html>> accessed November 28, 2021
- v. "Cryptocurrency: We Acted in Nigerians' Best Interest - Emefiele" (Cryptocurrency: We Acted in Nigerians' Best Interest - Emefiele) <<https://www.proshareng.com/news/%20BlockChain%20&%20Cryptos/Cryptocurrency--We-Acted-in-Nigerians--Best-Interest---Emefiele/55945>> accessed November 26, 2021
- vi. Larnyoh MT, "Twitter CEO Jack Dorsey Says Nigerians Will Lead Bitcoin Charge despite Cryptocurrency Ban" (Business Insider Africa June 14, 2021)

<sup>25</sup> "Cryptocurrency Ban: SEC, CBN to Provide Level Field for Investments" (February 21, 2021) <> accessed November 28, 2021.

- <<https://africa.businessinsider.com/local/markets/twitter-ceo-jack-dorsey-says-nigerians-will-lead-bitcoin-charge-despite/607c13m>> accessed November 29, 2021
- vii. Mesele O, “FRAMEWORK for the REGULATION of the NIGERIAN CRYPTO ASSETS MARKET” (Law Allianz April 27, 2020) <<https://www.lawallianz.com/articles/framework-for-the-regulation-of-the-nigerian-crypto-assets-market/>> accessed November 28, 2021
- viii. Ofili C and others, “The Law Reviews - the Virtual Currency Regulation Review” (thelawreviews.co.uk September 2, 2021) <<https://thelawreviews.co.uk/title/the-virtual-currency-regulation-review/nigeria>> accessed November 26, 2021
- ix. “The Malta Virtual Financial Assets Act” (Grant Thornton Malta) <<https://www.grantthornton.com.mt/industry/fintech-and-innovation/The-Malta-Virtual-Financial-Asset-Act/>> accessed November 28, 2021
- x. “Why Crypto Is Booming in Nigeria despite Govt Ban |” (September 6, 2021) <<https://www.premiumtimesng.com/promoted/483386-why-crypto-is-booming-in-nigeria-despite-govt-ban.html>> accessed November 26, 2021
- xi. Wikipedia Contributors, “Cryptocurrency” (Wikipedia February 15, 2019) <https://en.wikipedia.org/wiki/Cryptocurrency>