ATTAINING COMMON GROUNDS
CENTRAL BANK OF NIGERIA
CIRCULAR TO DEPOSIT MONEY BANKS,
NON-BANK FINANCIAL INSTITUTIONS AND
OTHER FINANCIAL INSTITUTIONS ON TRANSACTING
IN CRYPTOCURRENCY

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CIRCULATED TO

1. The Presidency
3. Federal Ministry of Communications and Digital Economy
4. Federal Ministry of Finance
5. Nigerian Stock Exchange, NSE
7. Federal Ministry of Science and Technology
8. Central Bank of Nigeria
9. National Judicial Council
10. National Communications Commission, NCC
11. Nigeria Deposit Insurance Corporation (NDIC)
12. Nigeria Inter-Bank Settlement System (NIBSS)
14. Nigeria Export Processing Zone Authority (NEPZA)
15. Nigeria Investment Promotion Council (NIPC)
16. Economic and Financial Crimes Commission (EFCC)
17. The Nigeria Police Force
18. National Security Adviser (NSA)
19. Securities and Exchange Commission, SEC
21. Nigerian Financial Intelligence Unit, NFIU
22. National Insurance Commission, NAICOM
23. National Pension Commission (PENCOM)
MEMBERS OF THE FINTECH ASSOCIATION AND STAKEHOLDERS IN THE CRYPTOCURRENCY INDUSTRY

The Fintech Association of Nigeria ("FintechNGR") has been invited by the Nigerian Senate to deliver a presentation on behalf of the Nigerian Fintech and innovation ecosystem on the issues pertaining to the Circular. Following this, the FintechNGR has invited members of the public to submit their comments on the Circular. These comments were collated and summarised, and are set out below:

1. BACKGROUND

1.1 On the 5th of February 2021, the Central Bank of Nigeria (the “CBN”) issued a circular to Deposit Money Banks (DMBs), Non-Bank Financial Institutions (NBFIs), and Other Financial Institutions (OFIs) (Regulated institutions) on transacting in cryptocurrencies. (the “Circular”).

1.2 The Circular mandates these Regulated Institutions to identify persons and/or entities transacting in or operating cryptocurrency exchanges within their systems and close such accounts with immediate effect.

1.3 In January 2017 the CBN issued a circular to Banks and OFIs on Virtual Currency Operation Nigeria, directing the banks and OFIs to:

(a) ensure that banks and OFIs do not use, hold, trade and/or transact in anyway in virtual currencies;
(b) ensure that existing customers that are virtual currency /exchanges have effective Anti-Money Laundering/Combating the Financing of Terrorism (“AML/CFT”) controls that enable them to comply with customer identification, verification, and transaction monitoring requirements;
(c) discontinue relationships where banks OFIs are not satisfied with controls with the controls put in place by the virtual currency exchanges/customers; and
(d) report any suspicious transactions in these customers should immediately be reported to the Nigerian Financial Intelligence Unit (NFIU).

1.4 In March 2018 (2018 Press Release), the CBN reiterated its statement on virtual currencies warning traders against digital assets which carry the risk of losing their investments as it does not constitute a legal tender.

1.5 The Circular reiterates the position of the CBN that these Regulated Institutions are prohibited from dealing in cryptocurrencies, the Circular also: (a) prohibits the Regulated Institutions from facilitating payments for Cryptocurrency exchanges; and (b) instructs Regulated Institutions to identify persons and/or entities transacting in or operating Cryptocurrency Exchanges within their systems and close such accounts with immediate effect.
1.6 The CBN Press Release titled *Response to Regulatory Directive on Cryptocurrencies* stated the following reasons – (a) the volatility of cryptocurrency and the consequent inability of cryptocurrency to be used as a lasting means of payment; (b) the anonymity associated with cryptocurrency transactions; (c) that “cryptocurrencies are not backed by any real assets or fundamentals” and as a result could crash in value; and (d) promotion of illegal activities such as money laundering, terrorism financing, etc.

1.7 In view of the above, the FintechNGR informally engaged the Central Bank of Nigeria (“CBN”) as well as major stakeholders in the cryptocurrency industry to understand their perspectives on the Circular. Consequently, the Fintech NGR received an invitation from the Nigerian Senate to deliver a presentation on the issues pertaining to the Circular, on Tuesday 23rd February 2020.

## 2 COMMENTS ON THE CIRCULAR

### 2.1 Prohibition of Regulated Institutions

2.1.1 The prohibition of the Regulated Institutions from facilitating payments for Cryptocurrency transactions by the CBN would redirect trade revenue to nearby African markets. This will further limit the federal governments drive to diversify revenue earning sources with the gloomy global economy. Also, the prohibition will make a lot of people involved in cryptocurrency transactions to go underground. Rather than this prohibition, the CBN should adjust/adapt its existing regulatory instruments to fit the highly innovative cryptocurrency sector. This adjustment/adaptation should strike a balance between protecting the people from the dangers of cryptocurrencies and harnessing the benefits of these cryptocurrencies.

2.1.2 The CBN or Securities and Exchange Commission (“SEC”) should reach an agreement as regards the regulatory authority that will regulate cryptocurrencies. They should also consider approving cryptocurrencies that have achieved global acceptance like Bitcoin, stablecoins, and other Altcoins.

2.1.3 Consideration should be given to the role of the National Information Technology Development Agency (“NITDA”) with respect to data protection in the cryptocurrency space.

2.1.4 NITDA is charged with the mandate to create a framework for the planning, research, development, standardization, application, monitoring, evaluation, and regulation of Information Technology practices in Nigeria, NITDA views blockchain technology as one of the emerging technologies that Nigeria should leverage for global competitiveness. Pursuant to its mandate, NITDA published
the Nigerian Blockchain Adoption Strategy. The primary objective of the Nigerian Blockchain Adoption Strategy is to identify and utilize the opportunities provided by Blockchain technologies to strengthen the country’s security on cyberspace and stimulate the growth of the economy. The strategy is built on the following initiatives: (i) Establishment of the Nigerian Blockchain Consortium, (ii) strengthening of the regulatory and legal framework, (iii) focus of the provision of the national digital identity, (iv) promotion of blockchain digital literacy and awareness, (v) creation of blockchain business incentive programmes, (vi) establishment of national blockchain sandbox for proof of concepts and pilot implementation. This blockchain adoption strategy aims at and will promote Blockchain technology in Nigeria and help in mitigating the risks regarding its implementation by government agencies, and corporate organizations.

2.1.5 CBN may also consider registering and designating locally and globally renowned cryptocurrency exchanges with proven KYC and compliance capabilities as legitimate places for Nigerians to trade cryptocurrency. This way, entities dealing with cryptocurrency can be known and licensed accordingly.

2.1.6 The CBN should also communicate with stakeholders and highlight specific ways they would like their concerns to be addressed. This will enable both stakeholders to work together to regulate the cryptocurrency market effectively.

2.1.7 The CBN should consider developing and testing of a Central Bank Digital Currency (CBDC). CBDC is a digitally represented version of the country’s sovereign currency, in this case the Naira, issued and backed by the Central Bank. CBDC could impact monetary policy favorably by providing a new tool for the Bank to apply and implement monetary policy with enhanced speed and improved efficiencies. If the Bank determined that CBDC should be interest bearing, this remuneration feature would likely increase the accumulation and use of CBDC for direct payments by and between individuals and retail businesses as the wallet holders of CBDC. Some countries have started experimenting and testing CBDC’s. Please see Schedule II.

2.2 Cryptocurrencies as Speculative Assets

2.2.1 The CBN, by its response following an uproar from the public, has taken a general view that Cryptocurrencies are speculative assets. However, there are some cryptocurrencies like stablecoins that do not fall under the generalisation made by the CBN. The different types of stablecoins include (i) Fiat- backed stablecoins which are backed by a fiat currency, (ii) collateralised stablecoins which are backed by other cryptocurrencies and (iii) Algorithmic Stablecoins which are backed by algorithms.

2.2.2 We note section 13 of the Investment and Securities Act, 2007 that confers powers on the Securities and Exchange Commission (“SEC”) as the apex regulator of the Nigerian capital market to regulate investments and securities business in Nigeria. In line with these powers, the SEC released a statement where it adopted a three-pronged objective to regulate innovation, hinged on
safety, market deepening and providing solution to problems. This will guide its strategy, its regulations and its interaction with innovators seeking legitimacy and relevance. Consequently, the SEC will in line with this statement regulate crypto-token or crypto-coin investments when the character of the investments qualifies as securities transactions. In line with the foregoing, the SEC should regulate Cryptocurrency as an asset while CBN regulates Cryptocurrency that fall within its purview.

2.2.3 It is also important for the regulatory authorities like SEC to properly define the various types of cryptocurrencies to be able to decipher which regulatory body has the power to regulate a cryptocurrency based on its definition.

2.3 **Security Risks in the Use of Cryptocurrencies**

2.3.1 Although the CBN highlighted security concerns as well as risks that necessitated the circular such securities concerns are understandable giving that Philippine authorities, in 2018, arrested a couple for allegedly defrauding more than 100 people who poured at least 1 billion Philippine pesos (more than $19 million) into their bitcoin investment scam, it should be noted that the use of cryptocurrency by criminal elements follows an interesting technology pattern where grey market participants are often ahead of the technology adoption curve. In view of this, the CBN can use its supervisory oversight to regulate the cryptocurrency industry in Nigeria to manage the identified risks associated with disruptive technologies like Digital currencies such as Bitcoin. A regulated Nigerian Crypto market will make commerce faster and more secure, mobile smartphone based, create jobs, and bring more revenue to the country.

2.3.2 Although cryptocurrencies have indeed been a conduit for flouting capital controls, proper regulation and partnerships with global exchanges and stable coin issuers offer us a path to growing our foreign reserves and defending the Naira from unscrupulous speculators. The cryptocurrency market, like most markets, is subject to laws. The CBN can convene a forum of stakeholders within the cryptocurrency space to understand what it will take for Nigerian banks to adopt the use of stablecoins as an alternative means of payment emulating the USA, where the Office of the Comptroller of the Currency has approved the use of stablecoins by federally regulated banks for payments and other activities.

2.3.3 Most Cryptocurrency transactions save for some transactions involving privacy coins, are recorded on public ledgers, and can therefore be tracked and traced where KYC protocol is being adhered to. CBN should consider partnering with tech companies that can assist with tracing cryptocurrency transactions.

2.4 **Prospects of Cryptocurrency**

2.4.1 Cryptocurrency will empower Nigerians to quickly scale past the barriers of participating in a global financial system. More importantly, it will enable Nigeria to grow its foreign reserves making the elusive Naira price stability more of a reality. This is currently evident in the cryptocurrency markets as Nigerians have
become very curious about bitcoin lately, going by Google search results. In the last 12 months, most global Google search queries for bitcoin originated in Nigeria. A leading global cryptocurrency trading platform estimated that Nigerians traded over $566 million in Bitcoin on its platform in the last five years, placing Nigeria second behind the United States Bitcoin volume traded.

2.4.2 In view of the above it is plausible that the actual volume of Nigerian cryptocurrency transactions is possibly much greater. Techpoint estimates Nigerian cryptocurrency transactions at US$400 million for 2020. We believe this demand is driven not just by speculation but by the average Nigerian's desire to participate in a technology-driven global economy.

2.4.3 Non-Governmental organisations ("NGOs") have received funds exchanges, with these funds NGOs have been able to achieve their objectives in the society for example for Pencils of Promise ("PoP") works with communities to build schools and create programs that provide educational opportunities for students, no matter where they are born or what resources they have. Funds raised through the #BuiltWithBitcoin initiative will support Pencils of Promise's mission to provide access to quality education to children around the globe. In December 2017, first bitcoin-funded school was completed in December 2017, serving a community of 7,500 people.

2.4.4 Cryptocurrency has made international trade possible for individuals who cannot access banks for foreign exchange, especially in rural areas. It has also helped ease remittances from people in the diaspora to Nigeria.

2.4.5 In the banking industry, blockchain creates decentralization which can make it easier for banks to focus on other activities besides tracking payment transactions. The use of blockchain has changed banking in many ways. It has affected things such as payments, settlement systems, fundraising, securities management, loans, credit, and trade finance. With the decentralization ledger for payments, blockchain can provide faster payments and lower fees than banks. Blockchain affects clearance and settlement systems where distributed ledgers can reduce the costs of operations and bring more real-time transactions between financial institutions.

https://builtwithbitcoin.org/#projects.
NOTABLE JURISDICTIONS
APPROACH TO THE
REGULATION OF
CRYPTOCURRENCY

We have highlighted a few jurisdictions that are especially known for their notable, thoughtful, innovative approaches to creating regulatory frameworks for blockchain.

3.1.1 Switzerland:

3.1.1.1 When compared to its European neighbors, Switzerland has taken a pragmatic approach to regulating digital assets and blockchain. Switzerland is also unique in that its approach has been driven almost exclusively by its financial regulator, the Financial Market Supervisory Authority (FINMA). This began in 2014, when FINMA issued a fact sheet stating that purchase and sale of bitcoins on a commercial basis and the operation of trading platforms for digital assets were subject to the country’s AML law. Since then, FINMA has issued regulatory guidance on fintech licenses. However, there are indications that the legislature could get involved, as the Federal Council released a report in December 2018 on the legal framework for blockchain in the financial sector; this report identified problem spots, and the Federal Council in March 2019 published a draft law to address these relatively minor issues.

3.1.1.2 Most recently, Switzerland passed the Blockchain Act, a law intended to create more legal certainty and fewer obstacles for blockchain applications while also minimizing abuse; is expected to come into force February 2021. The law covers the exchange of digital securities and sets standards for exchanges, establishing a “firm legal basis for exchanging digital-only securities and reclaiming digital assets from bankrupt countries.” Switzerland’s regulations and existing financial infrastructure have made it a top destination for innovative firms. Switzerland is also home to Zug, also known as “Crypto Valley,” which has been open to digital assets and blockchain since 2014. With a low corporate tax rate and loose regulations on digital assets, it has been successful in attracting blockchain companies.

3.1.2 Bermuda:

3.1.2.1 Bermuda is a unique jurisdiction in that it has already implemented multiple iterations of its digital asset regulatory framework, which was first introduced in 2018. In May 2018, Parliament passed the Companies and Limited Liability Company (Initial Coin Offering) Amendment Act 2018 (known as the “ICO Act”), which regulated all digital tokens issued through ICOS. The ICO Act gave the Minister of Finance authority to approve or reject ICOS and established disclosure,
audit, and compliance requirements. The following month, Parliament passed the Digital Asset Business Act 2018 (DABA), which established a licensing regime for digital asset businesses, gave the Bermuda Monetary Authority (BMA) jurisdiction over these businesses, and amended existing AML laws to include digital asset businesses.

3.1.2.2 This law requires licensed businesses to prepare annual audited financial statements and notify the BMA prior to accepting a new 10% shareholder. It also establishes a procedure for warnings and civil penalties up to $10 million. Finally, the Parliament of Bermuda passed the Digital Asset Issuance Act 2020, which replaced the ICO Act. The new law replaced the term “initial coin offering” with “digital asset issuance,” and established a more structured application process for issuance, like the process established in DABA. Bermuda has proved successful in attracting innovative companies that may have otherwise gone to different jurisdictions; its replacement of the ICO Act shows an understanding of new fundraising methods beyond the ICO.

3.1.3 **Mauritius:**

3.1.3.1 The Island of Mauritius took steps to proactively construct a regulatory environment aimed at encouraging innovation and development on the island. The adoption of the Economic Development Board Act in the National Assembly on July 19, 2017 formalized a “regulatory sandbox,” a legal framework specifically designed for licensing activities that are not yet regulated. Mauritius issued an open call to innovators to take advantage of its new Regulatory Sandbox License. Applicants must demonstrate that their project is innovative, beneficial to the Mauritian economy, and cannot be accommodated in the innovator’s home jurisdiction due to legal or regulatory gaps. In particular, the Government of Mauritius is seeking to attract fintech start-ups. Specific conditions are attached to the granting of a license under the sandbox regime. The Economic Development Board Act lists four conditions that could lead to the suspension of a license under this regime.

3.1.3.2 This suspension may occur, for example, if the project is viewed as a threat to the reputation of the island. As part of its plan to create a fintech hub “in and for” Africa, Mauritius has become “the first jurisdiction in the world to offer a regulated environment for digital asset custody,” according to the Mauritius Financial Services Commission. On March 1, 2019, a regulation came into force that requires any person carrying out custody services for digital assets to apply for a custodian services license. To receive a license, applicants must meet certain governance, minimum capital, cybersecurity, and AML requirements.
3.1.4 United States of America:

3.1.4.1 The United States' web of federal and state laws and regulations has led to a complicated regulatory landscape for digital assets. This is perhaps most evident in the differing rulings of state regulators on whether certain digital asset businesses need to obtain a money transmitter license, as well as differing definitions of blockchain, distributed ledger technology, virtual currency, digital assets, and more. In 2015, New York established the BitLicense regulation, which requires virtual currency businesses to apply for a license from the Department of Financial Services (DFS). Since then, states like Vermont and Wyoming have taken more open approaches to virtual currency and blockchain, with Vermont passing a law to create Blockchain-Based Limited Liability Companies. Also, the Office of the Comptroller of the Currency announced earlier in January that Federally regulated banks can make use of stablecoins to conduct payments and other activities.

3.1.4.2 At the federal level, the Securities and Exchange Commission (SEC) has regulatory authority over securities and has taken the position that certain tokens should be deemed securities, while the Commodity Futures Trading Commission (CFTC) has authority over tokens deemed to be commodities, which includes bitcoin and ether.

3.1.5 Malta:

3.1.5.1 Malta classifies cryptocurrencies into 3 categories which are payment tokens, asset tokens and utility tokens. Malta is the only country in the world that has promulgated legislation that regulates cryptocurrencies. The legislations are: (a) Malta Digital Innovation Authority Act (MDIA); (b) the innovative technology arrangements and services Act (ITAS); and (c) the Virtual Financial Assets Act (VFAA).

3.1.5.2 The purpose of the MDIA is to establish the Malta Digital Innovation Authority whose main function is to exercise regulatory functions regarding innovative technology arrangements. The ITAS provides the procedure for the certification of technology arrangements and the registration of technology service providers. It also defines “Innovative technology arrangements” as software and architectures which are used in designing and delivering Distributed Ledger Technology (“DLT”), smart contracts and related applications, and any other innovative technology arrangement which may be designated by the Minister from time to time. The VFAA seeks to establish a regulatory regime governing Initial coin Offerings (“ICOs”), white papers, cryptocurrency exchanges, wallet provider it also Introduces a new class of intermediaries called Virtual Financial Asset Agents (VFAA) and they are tasked with performing regulatory checks on Prospective ICO’s and Cryptocurrency exchanges.
4.1 Framework I

4.1.1 CBN should establish a framework for an International Finance Centre like the Dubai International Finance Centre. The proposed Nigerian International Finance Centre will be the gateway for Nigeria and Nigerians to participate in the global economy through modern instruments, including but not limited to the regulated use of cryptocurrency and the blockchain. We believe this can grow our banks into truly global institutions with hundreds of billions of dollars under their management while creating hundreds of thousands of jobs for our financially savvy young people and generating hundreds of millions of dollars in potential tax revenues from the country.

4.1.2 The Guidelines to Bank Operations in Free Trade Zones first published in 2016 and then ratified in the Banking and Other Financial Institutions Act signed into law in 2020. The framework allows the CBN to license offshore banks that can operate in Nigeria's free trade zones. In restricting international finance activity to free trade zones, CBN can protect the general populace from the adverse effects of unrestrained trade in financial products within the country's customs area.

4.1.3 The proposed Nigerian International Finance Centre should have branches in all of Nigeria’s approved Free Trade Zones, the NEPZA Act, the BOFIA Act 2020, and the CBN's guidelines on banking operations in free trade zones will regulate the activities of the Nigerian International Finance Centre. The CBN and the SEC can, thereafter, direct that any crypto exchanges who buy or sell stable coins like USDT, USDC, and NGNT to Nigerians (who will be identified by compulsory KYC) must lodge fiat dollars backing these coins in Nigerian offshore banks. By so doing, the CBN will primarily accomplish three things.

(a) First, it will give the cryptocurrency exchanges and issuers of the stable coins the confidence to move their dollars back and forth without contending with capital controls as they would in mainland Nigeria.

(b) Second, it will allow Nigeria to claim the dollars backing these stable coins as part of its foreign reserves bringing back in an orderly fashion with supply coming from remittances and exports to supply import and trade demands; and

(c) Finally, and most importantly, it will reduce the pressure on the Nigerian government to waste its precious foreign exchange on consumption rather than dedicate those resources to pursuing our nation's industrial policy objectives.
4.2  **Framework II**

4.2.1  The proposed regulation will apply to Merchants, Scheme Operators, Exchanges, Virtual Currency Brokers, Processing Service Providers, Wallet Providers/Custodians, Inventors, Technical Service Providers, Information Providers, and Miners that are involved in the operation of virtual currencies on a distributed ledger technology.

4.2.2  It is recommended that Virtual Asset/Currency Brokers, Virtual Asset/Currency Exchanges, Wallet Operators be required to obtain licenses in two stages namely Approval-in-principle (AIP) and Final license (FL). To obtain both, an application must be made to the Director General of SEC and subsequently, Governor of the CBN with the necessary documents e.g., a certificate of incorporation, financial projection, organizational structure etc. Upon obtaining an AIP the entity seeking approval shall not commence business unless the FL has been obtained.

4.2.3  Under the proposed regulations, the operations of licensed operators shall be guided by the following: (a) disclosure of the source of funds where the sale of virtual currencies is above US$10,000; (b) transactions shall be on a spot basis and forward transactions are not allowed; (c) the maximum amount per transaction shall be determined by the CBN; (d) the rates shall be displayed (e) the licensed entity shall maintain a database of all its transactions; (f) CBN shall advise licensed entities regarding any blacklisted virtual currency; and (g) every licensed entity have an internal audit/compliance unit.

4.2.4  Licensed entities should be made to ensure the following: (a) that currency conversion is facilitated through approved digital exchanges on the ledger; (b) that the regulator can monitor transactions as may be required and in the specified format; and (c) that the funds are deposited automatically to the beneficiary account or made available post-validation of digital identity profile.

4.2.5  Dispute resolution clauses shall be clearly spelt out. Also, the terms and conditions and risks of a licensed entity shall be disclosed to the public to foster consumer protection. It is recommended that the regulation comes with a risk matrix which licensed entities can identify with and mitigate against.

4.2.6  The CBN shall make a list of non-permissible activities that licensed entities shall not engage in.

4.2.7  The CBN can work closely with cryptocurrency providers to formalise their KYC, combating the financing of terrorism ("CFT"), and AML processes. This can include the use of Bank Verification Numbers ("BVN") and National Identity Numbers ("NIN").
5.1 That the National Assembly should prevail on the CBN to allow investors / traders/exchanges to liquidate their accounts within a period of six (6) months. The prayer is on the basis that the exchanges have funds belonging to Nigerians who have invested in the cryptocurrency trading business. The Stakeholders recommend that the exchanges during this period will not engage in any cryptocurrency transactions, i.e., the exchanges will not receive any deposits but only pay out to subscribers. India recently banned exchanges but allowed a six (6) month period to wind down. The Central Bank should also consider a CBDC for Nigeria to position Nigeria as an International Finance Center.

5.2 That the National Assembly convene a forum to discuss the issues/comments set forth above with critical stakeholders, including:
(a) The Securities and Exchange Commission
(b) Representatives of Global Cryptocurrency Exchanges
(c) Representatives of Local Cryptocurrency Exchanges
(d) Representatives of Global Stablecoin Issuers
(e) CEO of Banks
(f) Central Bank Officials
(g) President of Fintech Association of Nigeria and Representatives of the Nigerian Fintech ecosystem
(h) Senate & House Committees on Banking, Insurance and Other Financial Institutions.
(i) The Presidency
(j) Managing Directors of NEPZA and OGFZA
(k) Representatives of the Association of Bureau De Change Operators

5.3 Expected outcomes of this forum will include:
(a) The implementation of the recommended regulations; and
(b) The reversal of the CBN circular prohibiting banks from facilitating cryptocurrency transactions.

5.4 The CBN should consider the merits and characteristics of the different types of crypto assets/cryptocurrencies, and the risks they pose to the integrity of the financial system while in the process of creating their regulatory framework. Hence, a one size fits all will not be an effective approach and likened to throwing out the “baby with the bath water”, and would result in Nigeria not gaining the enormous benefits of digital and crypto assets.
APPENDIX

SCHEDULE I
Definition of terms

“Altcoin” means a general term used to refer to any cryptocurrency that is not Bitcoin.

“AML” means Anti-Money Laundering.

“Cryptocurrency” means a digital or virtual currency that is secured by cryptography, which makes it nearly impossible to counterfeit or double-spend.

“Cryptocurrency exchange” means an online platform where a person can exchange one type of cryptocurrency for another cryptocurrency.

“Cryptography” means the mathematical and computational practice of encoding and decoding data.

“Distributed ledger technology” means the technological infrastructure and protocols that allows simultaneous access, validation, and record updating in an immutable manner across a network spread across multiple entities or locations.

“KYC” Know Your Customer.

“Miner” means an individual or entity involved in Virtual currency mining. Miners are central to the smooth functioning of Virtual Assets. Their activity consists of participating, with the help of powerful computers, in the complex decentralized process of discovering and maintaining blocks of transaction records.

“Stablecoins” means cryptocurrencies that mimic the value of fiat currencies and are backed by either Fiat currencies, Cryptocurrencies or Algorithm.

SCHEDULE II

A Digital Cash Infrastructure: The Case for a Central Bank Digital Cash (CBDC)

In search of effective tools to ensure financial stability and efficient payments, The CBN should move forward with the discovery and testing of a Central Bank Digital Currency (CBDC). Research and experimentations from The Bank of England to The Central Bank of Bahamas have demonstrated real value of CBDCs ranging from modernizing the form of central bank money in the economy, financial inclusion to drastically easing cross border trade payments.

Central Bank Digital Currency is a digitally represented version of the country’s sovereign currency, in this case the Naira, issued and backed by the Central Bank. The industry has defined Wholesale and Retail CBDC models that can be seen in the BIS and IMF Reports on CBDC. Most central banks around the world have begun research and testing.

https://www.arabnews.com/node/1283721/world
https://builtwithbitcoin.org/#projects.
Private-Public partnership can support the safe and thoughtful approach to such efforts. Questions such as is a CBDC needed in Nigeria? What is the primary use case? How should it be designed (with blockchain? Cryptography for security? Align with KYC). How should the CBDC be issued and distributed? And how will FinTechs, banks and individuals interact with a CBDC? What is the AML/KYC framework?

Those questions will be best addressed in a collaborative and agile way. It is true that Blockchain technology is not needed for CBDC however, the need for compatibility to tokenized assets and ever more popular cryptocurrencies is a critical consideration as well. The nature of Bitcoin is a threat to central banks only in the case of a non-compatible sovereign currency that citizens trust. CBDC designs and incorporates essential controls with innovations to assist the central bank in executing their prudential responsibilities. Design innovation consider privacy; data and consumer protection; cybersecurity risks as well as efficiency of payment exchange.

Given local dynamics on need for financial inclusion and the risk mitigation of general cryptocurrencies, the primary use case we recommend the CBN to start testing with is a Digital Cash version of the Naira – Retail CBDC. As paper cash is today, Digital Naira as “digital cash” can help target **Key Areas of Impact:**

- **Financial Inclusion**
  - Paper cash has no KYC and used in person;
  - Digital cash can provide embedded risk-based KYC and AML Rules; and
  - As in paper cash, everyone can get a digital cash wallet.
- **MSMEs Trade and Payments**
  - Direct cash distribution to trade payments; and
  - Faster liquidity in real time settlement of payments.
- **Strong and automated AML Mechanisms**
  - Embedded AML flags even with cryptography; and
  - Embedded supervision capabilities.
- **Decline reliance of Foreign Reserves (Local Production, AFCTA)**
  - Targeted stimulus in areas to focus on local markets; and
  - Fund key programs via mobile wallets to diversify exports.
**Distribution Model:**
The CBN should consider an Open Banking Architecture where PSPs, Banks and other non-banks can access the Digital Naira Network via strong integrations (APIs, Wallets, Smart Contracts, etc..) all of which provide visibility and traceability mechanisms and reduces market risks.

Ideally, a CBDC model that begins from centralized issuance, but leverages a regulated, distributed, and inclusive ecosystem will foster a resilient infrastructure for every citizen. Here is a representation of the relationship for legal claim of the CBDC in various scenarios of such a distribution models.

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**Hybrid CBDC architectures allow for public-private partnership in payments**

![Diagram](image.png)