

FINTECH UPDATE





Introduction

The Central Bank of Nigeria ("CBN") issued the Guidelines on the Operation of Bank Accounts for Virtual Asset Service Providers ("VASPs") dated 22nd December, 2023 (the "Guidelines") which was published on its website on 2nd January, 2024. The Guidelines apply to all financial institutions ("Fls") regulated by the CBN. The provisions of the Guidelines mark a notable relaxation by the CBN of its prior restrictions imposed on Fls by its circular dated 5th February, 2021 (the "2021 Circular"). The CBN had, in the 2021 Circular, prohibited Nigerian Fls from (a) facilitating the settlement of transactions in virtual assets and from opening and operating bank accounts for virtual assets exchanges; and (b) holding or trading in virtual assets. In this regard, the CBN warned Nigerian Fls against having any transactions in crypto or facilitating payments for crypto exchanges. Owing to the increased activities of VASPs and the need to regulate such activities and the Nigerian government's decision to impose capital gains tax on gains realised from the disposal of digital assets, the CBN has now issued the Guidelines to ease the restriction on Nigerian Fls settling transactions and operating accounts for VASPs.

Under the Guidelines, only eligible stakeholder Fls such as commercial banks, merchant banks, and payment service providers involved in the settlement of transactions for third parties are allowed to operate the relevant accounts. Other stakeholders are VASPs licensed by the Securities and Exchange Commission ("SEC"), digital asset custodians, digital asset offering platforms, digital asset exchanges ("DAX"), DAX operators², and any other entity that may be categorised as such by the CBN from time to time ("Eligible Entities").

Objective of the Guidelines and permissible activities

The primary objectives of the Guidelines are to prescribe the minimum standards for banking relationships with VASPs in Nigeria, monitor Fls providing services to SEC licensed Eligible Entities, offer guidance on Eligible Entities' account operations, and ensure robust risk management practices in the sector.

Permissible Activities

In relation to the operation of accounts for VASPs, the Guidelines extended the permissible activities of the eligible stakeholder Fls to include: (a) opening of designated accounts; (b) providing non-interest-bearing designated settlement accounts and settlement services; (c) acting as channels for foreign exchange flows and trade; and (d) any other activity that may be permitted by the CBN from time to time.

Extent of the Guidelines

The CBN does not intend to regulate the activities of Eligible Entities or peer-to-peer crypto transactions. The aim of the CBN through the Guidelines is to regulate Fls under its regulatory purview facilitating transactions for Eligible Entities, especially in

¹https://www.cbn.gov.ng/Out/2024/FPRD/GUIDELINES%20ON%20OPERATIONS%20OF%20BANK%20ACCOUNTS%20FOR%20VIRTUAL%20Asset%20Providers.pdf

² The Guidelines retain the definitions of VASP, digital asset custodian, digital asset offering platform, DAX, DAX operator, and digital asset used in the SEC Rules on Issuance, Offering Platforms and Custody of Digital Assets 2022.



relation to an Eligible Entity operating an account and having a designated or settlement bank account with the FI. In addition, FIs regulated by the CBN remain prohibited from engaging in the holding, trading, and/or transacting in virtual currencies on their own account.

Requirements for Designated Accounts

The requirements for opening a designated account and designated settlement accounts include the obligations that accrue to the FIs as well as Eligible Entities. The Guidelines stipulate that only Eligible Entities, (a) incorporated in Nigeria; and (b) licensed by the SEC, are authorised to maintain designated accounts with Nigerian FIs. Opening a designated account is subject to obtaining the approval of the FI's senior management³. This means that a senior official from the position of an Assistant General Manager must approve the opening of a designated account for an Eligible DA.

To open a designated account, an Eligible Entity's application to open an account must include: (a) evidence of a valid licence issued by the SEC for the entity to engage in its business of an Eligible Entity; (b) a certified true copy of the entity's memorandum and articles of association; (c) incorporation documents of the entity, (d) verifiable registered address of the entity; (e) copy of the certificate of capital importation (where applicable); (f) valid means of identification, bank verification number and home address of all the directors, principal officers and beneficial owners of the entity; (g) anti-money laundering, combating financing of terrorism and combating proliferation financing policy of the entity; (h) all other requirements of a corporate account in line with the CBN Customer Due Diligence Regulations; and (i) any other requirement that the CBN may prescribe from time to time.

Restrictions on Designated Accounts

The Guidelines impose certain restrictions on the operations of designated accounts that are essential for ensuring compliance with the Guidelines and maintaining effective oversight over designated accounts. Some of the restrictions include:

- (a) Usage Restriction: Designated accounts are strictly for transactions involving virtual and digital assets and are not permitted to be utilised for other purposes.
- (b) Withdrawal Limitations: Withdrawals from designated accounts are permitted only through a Manager's Cheque or transfer to another account. Exceptions are, however, made for the settlement of virtual or digital assets transactions which can be done through a transfer to another designated account.
- (c) Transaction Limits: Fls are mandated to establish transaction limits on designated accounts. In setting these limits, Fls are required to take into consideration the volume of cash movement and the risk profile associated with the account holder's conduct and nature of business.
- (d) Concession Agreements and Transaction Charges: Fls are restricted from entering into concession agreements or arrangements with the holder of a

³ Senior management include any officer of a bank from the rank of Assistant General Manager and above.



designated account. In addition, the relevant maximum transaction band provided for in the CBN Guide to Charges for Banks and Other Financial Institutions shall be applicable to designated accounts at all times.

(e) **Dormancy Conditions**: The Guidelines stipulate that any account devoid of customer-induced transactions for three consecutive months will be classified as dormant. Subsequently, accounts falling under this category will be closed and the account holders will be duly notified of the closure.

Designated Settlement Accounts

The Guidelines provide for the opening of settlement accounts for Eligible Entities subject to obtaining the approval of the CBN. The conditions applicable to a designated settlement account include: (a) the designated settlement account must be utilised for settling all the obligations from transactions generated from the Eligible Entity's platform; (b) the account will hold the Naira balances of individuals associated with the Eligible Entities; (c) funds deposited in the account will be utilised to finance the Naira positions of persons on the Eligible Entity's platform; (d) withdrawals from the account will only be paid into the specific account that was used to fund the position of persons using the Eligible Entity's platform; and (d) the details of the transactions on a VASP platform leading to settlement on the account shall be accessible online to Fls on a real-time basis at all times

In addition to the above, the Guidelines further require that: (i) the transactions on the Eligible Entity's platform must be in Naira and the designated settlement account shall not be used to facilitate the foreign exchange positions of persons on the Eligible Entity's platform or used by the FI to facilitate the transfer from the foreign exchange positions of such persons to a foreign account; (ii) the FIs shall ensure that Eligible Entities always maintain a minimum collateral equal to 150% of the highest debit net position into the designated settlement account (over the past ten days); (iii) designated settlement accounts are not permitted to be used as security for credit; (iv) the settlement cycle for transactions shall be T+3, and value will only be given after settlement has occurred; and (v) transfers from the Naira positions of individuals on a VASP Platform to their bank account are restricted to two transactions in a quarter.

Eligible Entities will need to take these restrictions into consideration when seeking to be licensed in Nigeria and as product implementation is carried out for its Nigerian users.

Obligations of FIs and Risk Mitigation for AML/CFT Compliance

The Guidelines impose some compliance obligations on FIs including risk mitigation for anti-money laundering, combating the financing of terrorism and counter-proliferation financing ("AML/CFT"). Some of these obligations include:

Risk Mitigation: Fls must establish and uphold effective risk management systems. These systems aid in identifying instances where a designated account, opened in compliance with the Guidelines, is currently in use, has been used, or may potentially be used for activities related to money laundering, terrorism financing, or proliferation financing. In addition, Fls are



required to undertake steps to determine the beneficial ownership, source of wealth, and funds in designated accounts. Fls are also to ensure that there are appropriate customer protection systems against the risk of fraud, established complaints redress mechanisms and a channel for communication of customer complaints against designated account holders.

- 2. **Returns**: Fls are required to file periodic returns to the CBN between the end of a month and the 10th day of the following month. The returns are required to include (a) the number of the designated accounts opened within the reporting period, (b) the value and volume of transactions conducted in each account within the reporting period, and (c) details of the counterparty(ies) to the transactions, incidents of fraud or theft and number of customer complaints and remedial measures taken.
- 3. Customer Due Diligence and Know Your Customer: In relation to the conduct of customer due diligence, the Guidelines set out a non-exhaustive list of circumstances when such customer due diligence must be conducted. Some of these circumstances include when (i) onboarding a VASP; (ii) a transaction of significant value takes place; (iii) a customer's information or documentation changes substantially; or (iv) there is a material change in the way that a designated account is managed.

In addition to conducting customer due diligence, FIs are also required to independently validate the address and documentation provided by VASPs. Where such address or documentation is found to be invalid or incorrect, the relevant FI is required to place such account on Post-No-Debit. On a related note, FIs also have an obligation to initiate appropriate know-your-customer ("KYC") procedures, identify all individuals and entities offering the VASP services in their books, and ensure that they comply with the provisions of the Guidelines.

4. Suspicious Transaction Reporting and Monitoring: As part of their AML/CFT obligations, Fls are mandated to: (i) implement robust KYC procedures to promptly identify all individuals/entities offering services covered by the Guidelines and ensure immediate compliance; (ii) monitor and supervise all activities within designated accounts and be accountable for any misapplication of these accounts; (iii) maintain transaction volume and value record for each designated account and ensure adherence to set limits; (iv) ensure strict adherence to guidelines and laws by taking measures such as onsite visits to confirm proper account operation; (v) pay close attention to complex or unusually large transactions lacking visible economic or lawful purpose; (vi) investigate suspicious transactions and promptly report findings to the Nigeria Financial Intelligence Unit ("NFIU") and comply with relevant laws and regulations; and (vii) maintain records of investigations into reviewed unusual transactions not reported to the NFIU.



Consumer Protection Measures

As part of their customer protection obligations, FIs are mandated to ensure that appropriate consumer protection systems against risks of fraud are established and to provide a channel for communication of customer complaints against designated account holders. In addition, FIs shall establish a complaints redress mechanism and ensure proper communication of this mechanism to the general public and ensure strict adherence to the provisions of the Circular issued by the CBN (Referenced CPD/DIR/GEN/CIR/01/001) on the Deployment of the Consumer Complaints Management System (CCMS).

Sanctions

In addition to its sanctioning powers under the Banks and Other Financial Institutions Act 2020 and the remedial measures in the Guidelines, the CBN may impose financial and administrative sanctions on an FI, its board of directors, officers, or staff for non-compliance with the Guidelines. These sanctions include prohibiting the opening of additional designated accounts, imposing monetary penalties not less than NGN2 million for any violation, suspending the operating license of the FI and/or removal of directors or other officials from office.

Effects of the Guidelines and Conclusion

The Guidelines allow Fls to facilitate the settlement of cryptocurrency transactions carried out on VASPs/exchanges in Naira. Fls can now open and operate Naira accounts for Eligible Entities and VASPs in Nigeria. The previous restriction, which was a barrier to the implementation of the SEC's issuance of licences to virtual and digital asset operators under the SEC Rules on Issuance, Offering Platforms, and Custody of Digital Assets (the "Rules") dated 11th May, 2022, has now been removed. Now that the restriction has been lifted, we believe that the SEC will now start taking steps to commence the licensing of Eligible Entities and enforce the implementation of the Rules. In addition, we expect participants in the digital and virtual assets space to start taking steps to incorporate entities in Nigeria and/or apply to the SEC to obtain the relevant licence to enable them to open a designated bank account and designated settlement account with Nigerian banks for their operations in Nigeria. This strategic shift is likely to contribute to the broader adoption and usage of virtual and digital assets in Nigeria. Fls are, however, still not permitted to trade or hold virtual assets in their proprietary account.

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