

Legal Implications

Of Blockchain and Cryptocurrency

BY

Faith Obafemi

Lex Futurus



Scope

Today's class is limited to Nigerian Laws.

Foreign jurisdictions might be referenced.



Introduction

With our minds on bitcoin shooting to the moon or making our millions, we conveniently prefer to ignore the elephant in the room.

Prevention they say, is better than cure. Now that you've been told all the amazing things that blockchain (and crypto) can do for you and your business, it's time to address the legal implications.

First things first, blockchain and cryptocurrency are not illegal in Nigeria. This does not however imply that it's a free for all. Several extant laws apply.



Applicable Extant Laws

- Companies and Allied Matters Act – general corporate issues like structuring of the business during incorporation.
- Investment and Securities Act (ISA) – running a business where you offer investment advice? ISA requires you to have first obtained a license from SEC as a capital markets specialist.
- Evidence Act – Admissibility of electronic evidence.
- EFCC Act
- Cybercrimes (Prevention and Prohibition) Act 2015
- Constitution of the Federal Republic of Nigeria (As Amended) 1999 (CFRN)



Regulators

- Securities and Exchange Commission (SEC)
- Central Bank of Nigeria (CBN)
- Corporate Affairs Commission (CAC)
- Economic and Financial Crimes Commission (EFCC)
- National Information Technology Development Agency (NITDA)
- Ministry of Finance



- What is blockchain?
-
- How does it work?
 - What can it be used for?



Legal Implications

Blockchain

- Data
- Privacy
- Tokenization
- Smart Contracts



Data

The basic definition of blockchain is that it is a digital record. To record what? Data.

- How that data is imported, stored and exported
- Ownership of data – private keys
- Accuracy of data and right of correction and alteration. Remember blockchain is immutable
- Retention of data and the right to be forgotten
- Identity of data controller



Privacy

Privacy does not mean secrecy.

This is where we distinguish between private and public blockchain. Private blockchain is permissioned (needs permission to access), while public blockchain is permissionless (does not need permission to access).

Public: Everyone can participate, everyone has access, no single location has control over data.

Private: Control over who can participate, control over access and use, Terms of Use must first be accepted before access is granted, control over data location.



Tokenization

Digital representation of physical and digital assets.

Virtually anything and everything can be tokenized.

Legal issues that arise here include determination of ownership, valuation of tokens.



Smart Contracts

I know programmers will not like to hear this, but “smart contracts” are not smart, neither are they contracts in the strict sense of the word. They are simply codes written to represent a mutual agreement. A simplified way to imagine the way it works is using the IF-THEN premise. IF you pay your rent, THEN your house will be unlocked. With smart contracts, once they start running, there is literally no stopping them. Meaning changes to the “terms” of agreement are impossible. How dumb is that?

Fortunately, platforms like EOS allow for resetting of already launched smart contracts.



Smart Contracts *contd*

Legal implications in smart contracts include:

- Validity of contracts
- Proof of relationship/contract
- Liabilities for default or non-execution
- Dispute resolution

It's possible to address the first two, where both parties are corporate entities. The difficulty lies in where humans are parties. For instance, how does a bounty hunter who has been promised airdrops prove that the smart contract for the airdrop is between xyz.io and him?



Legal Implications

Crypto and ICO

- Classifications of cryptos
- Classifications of tokens
- KYC/AML/CFT
- Cybersecurity and Hacks



Classifications of Crypto

There is an ongoing debate on what should be the appropriate classification of cryptocurrency. As commodity or currency?

If commodity, then cryptos will be seen as rice and beans that are sold in the market.

If currency, then it is a valid means of exchange. Federal legislature and CBN will have the power to regulate.

Whichever way, whether as commodity or currency, there are tax issues involved. Where crypto is classified as commodity, tax is paid from profit.



Current Legal Position

As I mentioned earlier, cryptos are not illegal in Nigeria.

CBN and SEC, towards the end of 2017 and early 2018 released some warnings and policies about cryptocurrencies.

In summary, these warnings and policies did not prohibit cryptocurrency in Nigeria, at least for private businesses. However, Banks and Financial Institutions are prohibited from investing in cryptocurrencies or running a virtual currency exchange.

Private businesses other than BFIs, can run virtual exchanges or even launch an ICO.



Current Legal Position *contd*

Earlier this year, a member of the House of Reps called on CBN and NDIC to create a regulatory framework for the innovative technology through a bill titled ‘Need to regulate blockchain applications and internet technology.’

We can expect this to be the beginning of development of a friendly legal framework for Nigeria.



Classification of Tokens

Depending on the characteristics of a token, it could be a security, equity or utility. And there are hybrid tokens which possess all three characteristics.

A utility token is used for accessing or payment for the products and services of a platform. It is simply a means for transfer of value, there is no claim whatsoever on the issuer.

A security token is one representing an investment. In the US, the Howey test is usually applied as a litmus test to determine whether a token is a security or not. The Howey test comprises of four pillars, all of which must be present. It is an investment of money in a common purpose with the expectation of profit from the efforts of others.



Classification of Tokens *contd*

Equity tokens are tokens representing assets, whether digital or physical assets, including debts or equity claims. For instance, if the value of a house is represented with a token, that token is an equity token. Equity tokens, also known as asset tokens are usually treated as securities.



KYC/AML/CFT

Businesses operating virtual exchanges in Nigeria, must comply with the above requirements.

Know Your Customer

Anti Money Laundering

Combating the Financing of Terrorism



Cybersecurity and Hacks

Who is responsible for keeping your cryptos safe?

Whoever is in possession of the private keys is responsible for keeping cryptos safe.

Cybersecurity and Hacks *contd*

Who is liable in event of an hack?

Did the exchange promise to keep your cryptos safe?

In law, there is such a thing as negligence and failure to discharge duty.

Coin exchanges have a duty of care to keep the cryptos of their customers safe.

Who is liable when an ICO fails?

Founders, co-founders and the developer team carry the full-stack responsibility for a failed ICO.

THANK YOU!



LEX FUTURUS

Boutique international law firm with lawyers from four continents in the following countries: Nigeria, Malaysia, Singapore, Russia and England.

Our law practice areas are solely in the blockchain and crypto space.

LexFuturus.io



**CRYPTO &
BLOCKCHAIN
LAWYERS**



QUESTIONS ?

