



The Securities and Exchange Commission (SEC) Statement on the Classification and Treatment of Digital Assets

Introduction

The Securities and Exchange Commission (SEC) issued an official statement on 14 September 2020 on the classification and treatment of Digital Assets (crypto assets such as crypto currencies and tokens). It communicated its position in a published statement (“the Statement”) stating that crypto assets are securities which fall under the regulation of the Commission.

Section 13 of the Investment and Securities Act (ISA), 2007 conferred powers on the SEC as the apex regulator of the Nigerian Capital Market to regulate investments and securities in Nigeria. Prior to this, digital assets were largely unregulated in Nigeria. In SEC’s statement it has been made clear that digital assets fall under securities¹ and has classified these digital assets in order to regulate them and protect investors.

SEC’s Position

1. Crypto assets are securities and the burden of proving otherwise is on the issuer or sponsor of the said assets.
2. Proving that the digital assets are not securities is to be done by making an initial assessment filing². However, where the finding of the Commission is that the virtual assets are indeed securities, then the issuer or sponsor must register the digital assets.
3. In order to register these crypto assets, an investor or sponsor must do the initial assessment filing to satisfy SEC that it is not a security, and then file for registration if the burden of proof is not satisfied.
4. Digital assets that are exclusively offered through crowdfunding portals or other exempt methods are not deemed securities and as such do not need to be registered.
5. All Digital Assets Token Offering (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 the regulation of SEC. Existing digital asset offerings prior to the implementation of Regulatory Guidelines will have three (3) months to either submit the initial assessment filing or documents for registration.

1 <https://sec.gov.ng/statement-on-digital-assets-and-their-classification-and-treatment/>

2 An initial assessment filing is a Capital Market Fintech Assessment Form filled by business or individuals that plan to launch a digital innovation to enable SEC provide guidance on regulatory requirements.

SEC defined a crypto asset as a digital representation of value that can be digitally traded and functions as:

- a. a medium of exchange; and/or*
- b. a unit of account; and/or*
- c. a store of value, but does not have legal tender status in any jurisdiction.³*

In light of this, SEC has classified digital assets and has expressly stated how they would be treated. Crypto assets are to be treated as commodities if they are traded on a Recognized Investment Exchange or issued as an investment and utility tokens are also to be treated as commodities.

However, spot trading⁴ and transactions in Utility Tokens⁵ will not fall under SEC regulation unless conducted on a Recognized Investment Exchange.

Security tokens⁶ are deemed to be securities pursuant to PART XVIII (315) of Investment and Securities Act (ISA) while Derivatives and Collective Investment Funds of Crypto Assets, Security Tokens and Utility Tokens are to be regulated as Specified Investments under the ISA & SEC Rules and Regulations. Market intermediaries and market operators dealing in such Derivatives and Collective Investment Funds will need to be registered and approved by SEC.

Scope of Application

This Statement applies to any person (individual or corporate) involved in the provision of block-chain related and digital asset services and such persons or institutions must register with SEC and will be subject to regulatory guidelines. It also applies to sponsors and issuers of digital assets. Foreign or non-residential issuers or sponsors may be required to establish a branch office in Nigeria or may be recognized where a reciprocal agreement exists between Nigeria and the country of the foreign issuer or sponsor. Recognition status will also be accorded, where the country of the foreign issuer or sponsor is a member of the International Organization of Securities Commissions (IOSCO).

Conclusion

The regulation of digital assets is long overdue as they are gaining popularity and have become a major method of investing for the public. Admittedly, there are risks involved in these types of investments but regulation of these digital assets is imperative in order to protect the interest of investors as effective regulation will promote transparency, create standards that encourage ethical practices, and encourage the development of a fair and efficient market.

It is expected that robust regulation on digital assets will be developed in the future and that effective implementation will follow.

Disclaimer: The information, materials and opinions contained herein are for general information purposes and are not intended to constitute legal or other professional advice, and should not be relied on or treated as a substitute for specific advice relevant to particular circumstances.

³ <https://sec.gov.ng/statement-on-digital-assets-and-their-classification-and-treatment/>

⁴ Spot trading refers to the purchase or sale of a foreign currency, financial instrument or commodity for instant delivery on a specified spot date

⁵ a digital token of cryptocurrency that can be used to purchase a service offered by the issuer of the cryptocurrency.

⁶ A security token is a portable device that authenticates a person's identity electronically by storing some sort of personal information. The owner plugs the security token into a system to grant access to a network service. Security Token Services (STS) issue security tokens that authenticate the person's identity. <https://www.investopedia.com/terms/s/security-token.asp>