

Policy Brief

CRYPTOCURRENCY AND REGULATION IN UGANDA



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Introduction

This Policy brief is premised on an analysis as to the need for regulation of cryptocurrencies in Uganda. In October 2019, the Minister of Finance, Planning and Economic Development issued a public statement to the effect that the Government of Uganda does not recognize any cryptocurrency as legal tender in Uganda.¹ However, as technology continues to reposition itself around societal needs, at a fast pace, more countries around the globe are embracing and creating avenues for the use of cryptocurrencies within their local environments. Uganda should not be caught at the tail end of this drive and neither should it wait out the process of strategically positioning itself in the electronic commerce domain. Although Uganda is still predominantly an Agro-based economy, various stakeholders in the economy are constantly evaluating ways through which socio-economic transactions can be simplified and concluded efficiently. Such stakeholders include banks that facilitate Agro-based accounts; the capital markets industry; those engaged in foreign exchange; as well as Investment Clubs. Various computer-generated platforms are also being utilized as part of the digital space in carrying out transactions. For instance, more transactions are undertaken using mobile money payment systems than the brick-and-mortar banking system of only a few years ago.

Back in 2011, Cyber-related legislation were passed to cater for the emerging digital landscape in Uganda. These include the Computer Misuse Act, No. 2 of 2011; the Electronic Signatures Act, No. 7 of 2011; and the Electronic Transactions Act, No. 8 of 2011. As such, the regulatory landscape shows an appreciation of electronic transactions and utilization of currencies but shies away from directly mentioning cryptocurrencies. This is problematic for users of such digital assets. A regulatory framework requires clarity for the economy to thrive under it. In this regard, other countries have taken bold measures by highlighting their government positions as to whether they are to embrace and regulate cryptocurrencies or not. As is highlighted in this policy brief, the current legal framework

in Uganda does not directly address cryptocurrencies. Nonetheless, the same legal framework encompasses certain aspects under which cryptocurrencies are affected. Nonetheless, the public statements issued by the Ministry of Finance and the Bank of Uganda expressly paint the picture of non-adherence to cryptocurrencies in Uganda. This thus begs the question as to which direction should be taken in a country where we have an ambiguous legal framework about cryptocurrencies – on the one hand – and political rhetoric and misgivings – on the other hand? This policy brief is meant to provoke a direction towards the government of Uganda clearly positioning itself towards the regulation of cryptocurrencies in appreciation of the fact that they exist in practice.

The rationale for this policy brief therefore, is to provide a bird's eye perspective on consideration of cryptocurrency regulation in Uganda. The policy brief is anchored on using the current status to inform the future considerations. This is through using a situational analysis of strengths, weaknesses, opportunities and threats; legislative analysis; as well as case law analysis, to paint a picture of the current status of cryptocurrencies in Uganda. It then dwells on what can be learnt elsewhere, before concluding and presenting a summary of recommendations drawn from the best practices.

The Policy brief proposes clarity on the government position on use of cryptocurrencies; and suggests that Uganda should work with regional and international partners on establishment of an international treaty, as well as international collaborative measures in addressing cryptocurrencies.

The Policy is thus structured on a background which includes a definition of key terms; a situational analysis; concerns over impact on stakeholders; guiding principles on cryptocurrencies as drawn from best practices from key jurisdictions, as well as the International Monetary Fund; and finally, the conclusion and recommendations.




¹ See: <https://www.finance.go.ug/sites/default/files/press/statement%20on%20crypto%20currency.pdf>

Background

Under Objective IX of the 1995 Constitution, the Government of Uganda is mandated to encourage private initiatives and self-reliance in order to achieve development across all sectors. The Government is also mandated under clause (ii) of Objective XI of the 1995 Constitution to stimulate agricultural, industrial, technological and scientific development by adopting appropriate policies and the enactment of enabling legislation.

Putting into place the right legal framework for the regulation of cryptocurrencies is therefore a government obligation that should be followed through as the demands in tech development prompt us to also think of new ways to adapt to such technology. This process, as analyzed in this paper, requires cautious approach in consideration of the impact that such regulation may have in different stakeholders.

2.1 Definition of key terms

Term	Definition and characteristics
Blockchain 	This is where transactions occurring in the same timeframe are compiled into a virtual list of transaction data on the ledger (i.e., a 'block') and validated through consensus (or agreement) by other users. ² Users can store their cryptocurrency in 'wallets' which consist of a public key (similar to an account number) and a private key (like a PIN code) that can be stored, such as on a user's hard drive, external storage media or online. ³
Crypto asset 	This is a digital representation of value or contractual rights that can be transferred, stored or traded electronically, and which may (though not necessarily) utilize cryptography, distributed ledger technology or similar technology. ⁴ Crypto-assets are characterized by high price volatility, which makes them incapable of performing the three functions of money, that is: acting as a store of value; a means of payment; and, a unit of account. ⁵
Cryptocurrencies 	These are peer-to-peer electronic cash systems which allow online payments to be sent directly from one party to another without going through a financial institution. They have no association with any higher authority; have no physical representation and are infinitely divisible. ⁶
Cryptocurrencies Crypto-linked exchange-traded products (ETPs)	These are vehicles or avenues for institutional investors to invest in the crypto world without investing in crypto directly. ⁷
Distributed Ledger Technology (DLT)	DLT, based on a distributed ledger, represents a fintech development that offers potential improvement in financial record keeping. They can be relied upon as an efficient means to create, exchange and track ownership of financial assets on a peer-to-peer basis. ⁸

² University College London (UCL): Cryptocurrencies and the future crime, February 2021. See: <https://www.ucl.ac.uk/future-crime/policy-briefs/policy-brief-cryptocurrencies-and-future-crime>

³ Ibid

⁴ UK Regulatory approach to crypto assets and stablecoins: Consultation and call for evidence, January 2021

⁵ Bullmann, Dirk and Klemm, Jonas and Pinna, Andrea, In Search for Stability in Crypto-Assets: Are Stablecoins the Solution? (August, 2019), at p. 7. Available at SSRN: <https://ssrn.com/abstract=3444847> or <http://dx.doi.org/10.2139/ssrn.3444847>

⁶ Shaen Corbet, Brian Lucey, Andrew Urquhart, Larisa Yarovaya, Cryptocurrencies as a Financial Asset: A systematic analysis. *Finana* (2018), doi:10.1016/j.irfa.2018.09.003

⁷ Lee Reiners and Sangita Gazi, Wanted: A Prudential Framework for Crypto-Assets, see: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4327091

⁸ Capital Markets Authority: Regulatory options for Crypto Assets in Uganda. See: <https://cmauganda.co.ug/wp-content/plugins/download-attachments/includes/download.php?id=8073>

Initial Coin Offering (ICO)

An Initial Coin Offering is an unregulated process for raising of capital which is typically used by firms in the cryptocurrency field as a substitute for the controlled funding methods applied by other financial intermediaries.⁹

Payment Tokens

These are used interchangeably with Cryptocurrencies. Payment tokens are intended to be used as a means of payment for acquiring goods or services or as a means of money or value transfer.¹⁰

Payment tokens make it easier to transfer funds between two parties in a transaction; these transfers are facilitated using public and private keys for security purposes.

Security tokens

These are crypto assets that are usually centrally issued, transferable, and meet the definition of a security within respective jurisdictions. Their use cases include tokenized equities, fractionalized non-fungible tokens, and initial coin offerings.¹¹

Utility tokens

These are crypto assets that are usually centrally issued and provide the token holder with access to an existing or prospective product or service. They are usually limited to a single network (the issuer), or a closed network linked to the issuer, and have limited transferability.¹²

⁹ Liebau, Daniel and Liebau, Daniel and Schueffel, Patrick, *Crypto-Currencies and ICOs: Are They Scams? An Empirical Study (January 23, 2019)* at p. 3. Available at SSRN: <https://ssrn.com/abstract=3320884> or <http://dx.doi.org/10.2139/ssrn.3320884>

¹⁰ *ibid*

¹¹ IMF Policy Paper: *Elements of effective policies for Crypto Assets*. See: <https://www.imf.org/en/Publications/Policy-Papers/Issues/2023/02/23/Elements-of-Effective-Policies-for-Crypto-Assets-530092>

¹² *ibid*

Situational analysis

A discussion of the situational analysis related to the Cryptocurrency position in Uganda requires input of a SWOT analysis. In this regard, the situational analysis explains the state of cryptocurrencies in Uganda by bringing out the internal factors that are expected to arise out of utilization of cryptocurrencies, which are the strengths and weaknesses; and the external factors that should be considered as opportunities and threats. These are thus presented as advantages – through the strengths and opportunities, on the one hand; and, disadvantages, presented as threats and weaknesses, on the other hand. The SWOT analysis is thus an effective tool in enabling different persons impacted upon by cryptocurrencies to appreciate the varying merits and demerits in the use of such currencies. Another significance to be derived from the SWOT analysis is that it portrays key areas that need regulation, as it inadvertently brings out the stakeholders that need regulatory guidance, protection or enforcement in the use of cryptocurrencies. Following the SWOT analysis, this section then highlights current Ugandan legislations and case law that are relevant in the utilization and understanding of Ugandan trends in cryptocurrencies.

3.1 SWOT Analysis

Strengths	Opportunities
<ol style="list-style-type: none"> 1. It eliminates the need for middlemen in transactions because of the peer-to-peer networking structure, hence greater transparency, accountability and efficiency in transactions. 2. There is decentralization in the use, i.e., the control is in the hands of the developers using the cryptocurrency or by the entity that develops it before it is released into the market. This guarantees stability and security, unlike fiat currencies which are controlled by the State. 3. Enhanced security and consumer privacy are guaranteed through the encryption techniques employed throughout the distributed ledger and the cryptocurrency transaction processes. 	<ol style="list-style-type: none"> 1. Each transaction is unique, private and executed between two parties, thus creating confidentiality. 2. Gradually, adoption of cryptocurrency utilization can create more job opportunities in the tech world for blockchain developers, cybersecurity experts, smart contract engineers and others. It also opens up for new industries such as cryptocurrency exchanges and blockchain-based payment systems.
Weaknesses	Threats
<ol style="list-style-type: none"> 1. Cryptocurrency exchanges are not as secure as the cryptocurrencies themselves. In the effective operation of user IDs, most exchanges store the wallet data of users. Such data can be stolen by hackers, granting them access to a lot of accounts and the ability to make transfers of funds from those accounts. 2. An erroneous transfer cannot be cancelled or retrieved. If a user mistakenly sends funds to a wrong wallet address, the coin cannot be retrieved by the sender. This weakness can be exploited as an excuse by a user who wants to cheat another. 3. Adoption of crypto assets can erode the effectiveness of capital flow measures, which will in turn limit the county's ability to counteract capital flow volatility. 	<ol style="list-style-type: none"> 1. It is near-impossible for government to monitor and track down illegal activities employed in cryptocurrency transactions since privacy and security are quite high. This can thus attract illegal activities through this channel of transactions. 2. If a user loses the private key to his or her wallet, this locks the user out of a transaction or account, with all the coins inside of it, which results into financial loss for the user. 3. Widespread adoption of crypto assets can threaten the effectiveness of monetary policy, especially where firms and households prefer to save and invest in crypto assets that are not pegged to domestic fiat currency.

3.2 Legislative analysis on Cryptocurrencies in Uganda

Currently, there is no recognized cryptocurrency as legal tender in Uganda, and neither are there any licensed organizations in Uganda to sell or facilitate the trade in cryptocurrencies. To the extent that practices in crypto assets relate to various fields of financial transaction and investment, there are existing regulations in Uganda that are or can be perceived as applicable to them. The impact of these legislations on various stakeholders, is addressed under section 4.0.

a) Capital Market Authority Act, Cap. 84: Crypto currency companies as issuers of securities: Crypto currencies are considered as securities which fall under the mandate and regulation of the Capital Market Authority in accordance with Section 1 of the Capital Markets Authority Act. Section 1(hh)(iii) of the Act defines Securities as inclusive of any right, warrant, option, or futures in respect of any debenture, stocks, shares, bonds, notes or in respect of commodities. Crypto assets can thus fall under the definition of securities in this respect, which covers Security tokens as well.

b) Anti-Money Laundering Act (as amended by the Anti-Money Laundering (Amendment of Second Schedule) Instrument, No. 136 of 2020): The Second Schedule to the Anti-Money Laundering Act, 2013, was amended to include virtual assets service providers (VASPS) among the list of “accountable persons” subject to supervision and monitoring by the Financial Intelligence Authority (FIA). The amendment introduces paragraph 16 to the Schedule, which, in defining VASPS, states as follows:

“16. Virtual asset service providers, that is to say, a natural or legal person who conducts one or more of the following activities for or on behalf of another natural or legal person –

(a) the exchange between virtual assets and fiat currencies;

(b) the transfer of virtual assets;

(c) the safekeeping or administration of virtual assets or instruments enabling control over virtual assets or instruments enabling control over virtual assets; and

(d) the participation in or provision of financial services related to an insurer’s offer or sale of a virtual asset.”

This provision, thus, means that anyone or any company that conducts one or more of the above listed activities, for or on behalf of another person or entity, is required to register with the FIA. The purpose of this provision is to hold crypto service providers accountable in addressing scams and criminal liabilities related to the use of cryptocurrencies. Effectively therefore, the Financial Intelligence Authority can rely on this regulation to supervise or monitor the activities of crypto service providers.

c) The Foreign Exchange Act of 2004: Section 3 defines a foreign exchange as inclusive of “(a) banknotes, coins or electronic units of payment in any currency other than the currency of Uganda which are or have been legal tender outside Uganda. Considering that cryptocurrency, which are electronic units of payment, are recognized as legal tender in some countries outside Uganda, by virtue of this definition, they could also be interpreted as foreign currency under this Act.

d) The Electronic Transactions Act, No. 8 of 2011: This law provides for, among others, the use, security, facilitation and regulation of electronic communications and transactions. The Act, for instance, defines an “automated transaction” to mean “an electronic transaction conducted or performed, in whole or in part, by means of a data message in which the conduct or data messages of one or both parties is not reviewed by a natural person in the ordinary course of the natural person’s business or employment.” Section 4(1) of the Act provides for its objectives. These include: (a) enable and facilitate electronic communication and transactions; (b) remove and eliminate the legal and operational barriers to electronic transactions, and so on. Electronic transactions conducted by virtual of crypto assets, such as payment tokens, are thus adequately covered under these provisions of the Electronic Transactions Act. Ideally, this can be taken to include Crypto-linked exchange-traded products (ETPs).

e) The Electronic Signatures Act, No. 7 of 2011: This law makes provision for the use of electronic signatures and related matters. It holds various provisions which can be utilized in the recognition and enforcement of the rights of electronic transaction users, inclusive of cryptocurrency. Section 2, for instance, provides an interpretation as to what it means to “rightfully hold a private key”. The Section stipulates that this means – “to be able to utilize a private key – (a) which the holder or the holder’s agents have not disclosed to any person in contravention of this Act; and (b) which the holder has not obtained through theft, deceit, eavesdropping or other unlawful means.” This law thus recognizes the use of electronic signatures in payment tokens.

f) The Computer Misuse Act, No. 2 of 2011: This law provides for, among others, the safety and security of electronic transactions and information systems; as well as the prevention of unlawful access, abuse or misuse of information systems including computers. Section 5, for instance, provides that what amounts to ‘authorized access’, covers access by a person to any program or data held in a computer, by virtual of entitlement or consent. The legal risks involved in the use of crypto assets include unauthorized access by persons who are not part of the peer network within a block chain. In such respects, addressing such unauthorized access, can fall within the provisions of this Act.

g) The National Payment Systems Act, 15 of 2020: This law serves the purpose of regulating the payment systems; providing for the safety and efficiency of payment systems; and, among others, to regulate the issuance of electronic money. Under Section 4(1) of the Act, the Central Bank is mandated to regulate, supervise and oversee the operations of payment systems in order to ensure their safety and efficiency. The Bank is also mandated to issue directives, standards, guidelines, orders and circulars regulating the manner in which the objectives of the Act may be achieved. It is premised on these provisions, that the Central Bank has been empowered to issue circulars and guidelines against the practice of facilitating cryptocurrency transactions in Uganda.

3.3 Case law analysis

At the time of developing this Policy Brief, only one case involving the legality of crypto assets, had been brought before the Courts of Judicature in Uganda. This is analyzed below:

Silver Kayondo versus Bank of Uganda, Miscellaneous Cause No. 109 of 2022

This was an application for judicial review seeking orders, among others, for a declaration that: Crypto assets and Cryptocurrencies are legitimate digital assets tradable in the digital economy and can be liquidated/cashed out via mobile money and other payment systems in settlement for Uganda Shillings, at the prevailing free-floating exchange rates established by the global and national market forces of demand and supply. The Applicant also sought a declaration from court to the effect that the Central Bank (Respondent in this case), did not have the mandate to issue circulars barring all entities licensed under the National Payment Systems Act 2020 from facilitating cryptocurrency transactions without consultation of the industry players/licensees.

Hon. Justice Ssekaana Musa, in dismissing the application, ruled to the effect that cryptocurrencies, under the current National Payment System Act, are illegal or unlawful and are not accepted as a general payment instrument; and that the Bank of Uganda had the mandate to issue directives to the licensees under the National Payment System. Court pointed out further that any person who claims to be an affected party in the area of cryptocurrencies cannot claim to be lawfully operating a system which is not recognized by our legal system.

“The Respondent has a duty to warn the public about the attendant risks associated with cryptocurrencies or crypto assets before the public fall prey [to such] [sic] schemes disguised as digital economy where there is anonymity of the real players, money-laundering or other illegal activities thrive. . . .

The Honourable Judge Ssekaana went on to state that: “The Respondent has a duty to warn the public about the attendant risks associated with cryptocurrencies or crypto assets before the public fall prey [to such] [sic] schemes disguised as digital economy where there is anonymity of the real players, money-laundering or other illegal activities thrive. . . . The current regulatory framework was not designed with cryptocurrencies in mind and the respondent was only advising the public generally without any specific stakeholders in mind who may be operating in Uganda illegally. The respondent could not give recognition to the applicant and other stakeholders whose trade is quite unclear to the legal and economic system of the country through consultation. . . . The respondent did not ban cryptocurrency but rather directed licensees under the National Payment System Act to desist from liquidating cryptocurrency. . . This was merely a regulatory directive to avoid legalizing the undefined system as a payment instrument in Uganda.”

This ruling can be interpreted as providing clarity on the Ugandan government position in as far as regulation and licensing of cryptocurrencies in Uganda is concerned. It clearly portrays the position that cryptocurrencies are not a recognized or regulated currency in Uganda. As stipulated in the ruling, any institutions in Uganda that are utilizing crypto assets as part of their operations, are doing so illegally since such system is “not recognized by our legal system”.

In the legislative analysis, as presented under section 3.2 above, there are particularly regulatory provisions that can be interpreted as applicable to crypto assets and yet Ssekaana J., points out that the current regulatory framework was not designed with cryptocurrencies in mind. This essentially means that if any person or entity were to rely on the legislations aforementioned, in trying to administer, supervise or enforce a crypto asset transaction in Uganda, such action can be overruled by a party relying on the ruling in the Silver Kayondo case.

As such, this ruling does not help matters but instead stirs up a confusion in the sense that the Ugandan regulatory landscape that has a reach on cryptocurrencies due to its technological neutrality, is still not perceived to cover cryptocurrencies in as far as the Ugandan courts of law are concerned. It should, nonetheless, be pointed out that the Kayondo case only made reference to the National Payment Systems Act, 15 of 2020 as there was no argument brought before the Court to interpret any of the other legislation analyzed in this policy brief. It goes without saying that perhaps the direction of the ruling would have been different.

Even then, a counter position to the ruling in the Kayondo case is that the legislation does not necessarily have to directly mention the term “cryptocurrency” so as to show that it was designed in Uganda with the consideration of such assets. It can be argued that it is enough for such legislation to provide for different characteristics that relate to cryptocurrencies, which is the current case. By way of example, it can be considered sufficient for the Electronic Transactions Act to broadly provide for ‘electronic communications and transactions’ as opposed to specifically mentioning ‘cryptocurrencies’.

On the flip side, if the Court had agreed with the Applicant and issued a declaration to the effect that crypto assets and cryptocurrencies are legitimate digital assets in Uganda, this would have strengthened reliance on the aforementioned legislation under section 3.2 of this policy brief and legitimized the use of crypto assets and cryptocurrencies in Uganda.

The Kayondo case has thus strengthened the Central Bank’s position to continue exercising its mandate under the National Payment System Act in, amongst other things, warning the public against dealing in cryptocurrencies. However, the further legal ambiguity created by placing this ruling alongside the legislation analyzed above (see 3.2 above) further lays emphasis on the need for the government of Uganda to come up with a clear regulatory position on the utilization of cryptocurrencies as digital assets in Uganda.

Impact of Cryptocurrencies on stakeholders:

Key concerns (why should we care?)

a) The anonymity aspect:

Due to the anonymity of cryptocurrency users, this can encourage criminal activity but also presents a problem over erosion of the tax base for the government. In the past, the Uganda Revenue Authority (URA) and the Financial Intelligence Authority (FIA), have been collaborating with the banking industry to present information about account holders so as to curb criminal activity such as money laundering, protect the tax base, as well as oversee domestic resource mobilization. Balances kept in cryptocurrencies are essentially untaxed considering that the Uganda Revenue Authority does not have specific guidance on the regulation of electronic transactions that rely on cryptocurrencies. As such, where cryptocurrency accounts are anonymous, the benefit for Uganda, derived from the collaborative enforcement measures exercised by URA and FIA, will not be felt. Ultimately, the anonymity aspect in the operation of cryptocurrencies, can pose a negative effect to the economy through money laundering and tax avoidance activities that go through undetected.

b) Difficulty in monitoring capital flow:

The Bank of Uganda monitors and manages capital flow in Uganda. However, the decentralized, borderless and pseudonymous nature of cryptocurrencies can be of concern and a challenge for the effective monitoring and control of capital. The absence of a mechanism to monitor capital flow through crypto assets means that such transactions cannot be controlled and are not predictable. This would thus make it difficult for the Bank of Uganda and other government sectors such as the Ministry of Finance, Planning and Economic Development, to effectively plan the country's economy, including controlling inflation.

c) Legal risks:

Various challenges arise in attempting to apply existing rules to cryptocurrencies, which cannot be easily classified under the current legal regime. This can lead to uncertainty and potential legal risks. Multiple regulation should be avoided as this can create legal conflict and naturally increases the cost of operation and enforcement of the law. Furthermore, due to the opaque nature through which crypto assets operate, those who wish to invest in such businesses, would not have a track record to rely on, in the same way that someone buying shares in an ordinary business can easily read through its portfolio or Initial Public Offering (IPO). The absence of a record to rely upon, increases the legal risks involved.

d) Consumer Protection:

Risks upon consumers are likely to arise where consumers and investors do not have a full comprehension of the risks associated with cryptocurrencies, due to inadequate governance mechanisms, opaque decision-making processes and inadequate enforcement where defaults arise. The impact in consumer protection is thus likely to be felt across the board for various stakeholders such as the Cybercrimes Unit of the Uganda Police Force which will require capacity building so as to understand how to combat irregularities in the use of cryptocurrencies; Internet Service Providers that will have to employ self-regulatory mechanisms in monitoring and reporting or striking down irregular activities through their platforms without denting legitimate usage; Government regulators such as the Uganda Communications Commission and the Financial Intelligence Authority having to devise ways in which they can enforce or ensure that online service providers have tools in place that guarantee consumer protection for those that use their digital services.

e) Employment issues:

The SWOT analysis highlighted in section 3.1 above, shows that cryptocurrencies can, to an extent, eliminate the need for middlemen in financial transactions. Ideally, this means that a certain level of employees in the banking industry are rendered irrelevant. Although it is arguable that this would not be a massive impact on the employment sector of a least developed economy like Uganda, the effect can grow in the long term with the growth of the economy. This is thus a negative impact where cryptocurrencies are a disruptive technology on the labour market. However, on the flip side, the SWOT analysis also reveals that more job opportunities are made available in the tech world to facilitate digital transactions.

f) Capacity gaps in technology growth

Cryptocurrency is a complicated and disruptive technology with limited comprehension by many entities that are considered to be impacted by it. Human capacity development in this sector is therefore crucial. This will necessitate engaging the services of Civil Society Organisations, academic entities and other key players with a thorough understanding as to how virtual assets operate and thus engage in trainings and advocacy workshops to disseminate information relating to this area of technological growth. Organizations such as the Uganda Water Project, have realized the benefits that come with obtaining funding through cryptocurrencies and are thus looking into training and advocacy programmes for cryptocurrencies.¹³ The Law Development Centre (LDC) which is a government academic Institution with various academic programmes such as the Diploma in Law and Diploma in Legal Practice, is working on revising its curricula to include courses on cryptocurrencies.

As such, service providers in the financial sector, FinTech and other companies, as well as other private sector entities that engage in online payment systems and/or virtual assets, would fall under regulatory supervision by government departments and agencies such as the Financial Intelligence Authority (FIA). Where such stakeholders in the finance sector are called upon by government agencies, such as the FIA, to fulfill certain regulatory measures in order to operate freely, this may ultimately push up their costs of operation. For instance, most financial technology companies (FinTech) rely on Initial Coin Offerings (ICO) to raise funds for their operations. The ICO acts as a Share Certificate for anyone who wants to invest in the company. Where regulatory measures such as becoming accountable to the FIA are introduced, this may discourage Fintech companies from being established in Uganda or for others to continue in operation due to such accountability requirements.

¹³ See: <https://ugandanwaterproject.com/2020/08/why-we-believe-in-cryptocurrency/>

Guiding principles on Cryptocurrencies

5.1 Country best practices

a) Kenya

In the case of Wiseman Talent Ventures vs. Capital Markets Authority of Kenya (2019) eKair, Justice M.W. Mungai opined on the issue as to whether cryptocurrencies were regulated in Kenya. He stated that: "... the absence of a specific regime does not ouster jurisdiction of the general regime of law as exemplified by the cited provisions of the Capital Markets Act and the application of the Howey test¹⁴ outlined above. The interpretation of cryptocurrency as a security is because it is a scheme that involves an investment of money in a common enterprise with profits to come solely from efforts of others as illustrated by the Howey test....therefore, cryptocurrency is either outlawed or regulated in some form in various countries. The Defendant has residual jurisdiction as per Section 2 & 11 of Capital Markets Act to regulate crypto currencies as securities."

This case thus highlights the Kenyan position of choosing to regulate cryptocurrencies as securities under the Capital Markets Act. Other regulatory frameworks that apply to cryptocurrencies in Kenya include the National Payment Systems Act (NPSA) and the Kenya Information and Communication Act (KICA). Just like in Uganda, the NPSA of Kenya authorizes the Central Bank of Kenya to oversee and regulate payment systems and payment service providers within Kenya. Although the Central Bank of Kenya has issued warnings to the public to refrain from trading in cryptocurrencies, such trading is not prohibited.¹⁵

Furthermore, under the Central Bank of Kenya's Money Remittance Regulations of 2013,¹⁶ cryptocurrency companies can only legally operate after acquiring a license from Kenyan authorities to offer transmission services within Kenya.

b) South Africa

South Africa does not currently have any specific legislation for cryptocurrencies although in October 2022, crypto assets were declared as "a digital representation of value" by the Financial Sector Conduct Authority, thus paving the way for regulation.¹⁷ The Financial Sector Conduct Authority, which is South Africa's financial watch dog, also stated that the government plans to start licensing crypto trading companies. The overall objective of introducing regulatory measures over crypto assets in South Africa, is to prevent theft, money laundering and undermining of the monetary policy.¹⁸

Placing the decisive action of the South African government within the context of the impacts that crypto assets have on various stakeholders, as outlined in section 4 of this policy brief, Uganda can consider taking on similar measures so as to prepare itself against anticipated challenges in the utilization of crypto assets.

¹⁴ The Howey Test is drawn from the United States Supreme Court case of Securities Exchange Commission vs. W.J. Howey Co. 328 US 293 (1946) where the Court determined if an investment is a security and therefore subject to regulation by the Securities Exchange Commission (SEC). The Court relied on substance rather than form; that is, not whether the item was referred to as stock, bond or share but its economic reality. The 'Howey' test has been applied to determine if crypto assets are securities in the U.S and there are four ingredients to consider:

- a) Is there an investment for money;
- b) Is there an expectation of profits from the investment;
- c) Is the investment of money in a common enterprise;
- d) Are there profits that come from the efforts of a Promoter or 3rd Party.

¹⁵ See: https://www.centralbank.go.ke/images/docs/media/Public_Notice_on_virtual_currencies_such_as_Bitcoin.pdf (Last accessed June 12, 2023)

¹⁶ See: <https://www.centralbank.go.ke/wp-content/uploads/2016/08/The-Money-Remittance-Regulations-2013.pdf> (accessed June 12, 2023)

¹⁷ See: <https://www.reuters.com/technology/south-africa-moves-regulate-crypto-assets-2022-10-19/> (accessed June 21, 2023)

¹⁸ Ibid

c) Central African Republic (CAR)

The CAR became the first African Country to designate Bitcoin and other cryptocurrencies as legal tender by virtue of an April 2022 Statute.¹⁹ However, this legislation brought about a conflict with Partner States in the region under the Economic and Monetary Community of Central Africa (CEMAC). This includes Cameroon, the Central African Republic, Chad, Equatorial Guinea, Gabon and the Republic of the Congo. The Bank of the Central African States (BEAC) serves the CEMAC member-States. The purpose of the BEAC is to manage the monetary policy, issue currency, manage the foreign reserves of the member States, and facilitate payments and settlement systems.²⁰

The BEAC does not have a specific policy on cryptocurrency although in 2011, it created a legal framework for electronic money.²¹ The passing of the April 2022 Statute in CAR placed the country at odds with BEAC, because this action meant that CAR was violating the CEMAC Treaty. BEAC had banned the use of cryptocurrencies for financial transactions in the CEMAC region, hence CAR's action created a conflict with the regional position.²² As a result, in March 2023, the Central African Republic's parliament repealed the law that had given bitcoin and other cryptocurrencies legal tender status in CAR.²³ In reversing the recognition of cryptocurrencies in CAR, the new law effectively meant that crypto assets were no longer given legal recognition in CAR.

The Central African Republic experience in rushing to regulate its own crypto asset amid having a regional financial body that oversees the monetary activities within the region, provides lessons for countries like Uganda. Uganda falls within the East African Community (EAC) under which it strives to fulfill its obligations for financial integration within the EAC. This includes creation of a common market, customs union, and monetary union. If Uganda is to consider regulating crypto assets, it must be done in harmony with the general interests of the EAC so as not to jeopardize its EAC position. However, the current position of the EAC Member States, is that they have taken a common stance against digital currencies.²⁴

d) The United States of America

In the U.S, individuals and businesses that store or exchange any kind of crypto currency, fall under the category of an "MSB", or 'Money Services Business'. All MSBs are subject to the Bank Secrecy Act (BSA) and the first step in obtaining a cryptocurrency license in the USA, requires one to register a business entity with the FinCEN as a Money Service Business.²⁵ The BSA requires businesses to keep records and file reports that are determined to have a high degree of usefulness in criminal, tax and regulatory matters. As such, cryptocurrency transactions are only regulated if such a transaction is perceived as a sale of a security under State of Federal law or if the sale is considered a money transmission under State law, making the person a money services business (MSB) under Federal law.²⁶

¹⁹ <https://cointelegraph.com/news/bitcoin-sango-coin-and-the-central-african-republic> (Accessed June 12, 2023)

²⁰ See: <https://freemanlaw.com/cryptocurrency/central-african-states/> (accessed June 13, 2023)

²¹ *Id.*

²² See: Moki Edwin Kindzeka: Bank of Central AFRICAN States urges CAR to annul Bitcoin as Currency, <https://www.voanews.com/a/bank-of-central-african-states-urges-car-to-annul-bitcoin-as-currency/6567064.html#:~:text=18%2C%202021.,of%20Bitcoin%20as%20legal%20tender.&text=The%20Cameroon%20headquartered%20Bank%20of,the%20cryptocurrency%20Bitco in%20legal%20tender.> (accessed June 12, 2023)

²³ See: <https://www.centralbanking.com/central-banks/currency/digital-currencies/7956294/car-to-drop-crypto-as-legal-tender> (accessed June 12, 2023)

²⁴ <https://www.theeastafrican.co.ke/tea/business/tough-stance-on-cryptocurrency-despite-fast-rising-popularity-1379238>

²⁵ <https://enterslice.com/us/cryptocurrency-license-in-usa>

²⁶ Muskaan Aggarwal, Cryptocurrency regulation in the US in 2023, See: <https://legamart.com/articles/cryptocurrency-regulation-in-the-us-in-2023/> (accessed June 21, 2023)

The bodies responsible for making and overseeing regulation of cryptocurrencies in the U.S are the following: The Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), the Federal Trade Commission (FTC), the Treasury Department, through the Internal Revenue Service (IRS), the Office of the Comptroller of the Currency (OCC), and the Financial Crimes Enforcement Network (FinCEN). Nonetheless, no formal regulation has come about yet.²⁷

The Security and Exchange Commission regulates stocks and other securities in the US. It is also accepted as a regulatory base for cryptocurrencies which fall within the realm of securities under the Howey test explained under section 5.1 (a) of this Policy brief. This resonates with what has been covered in this policy brief regarding regulation of cryptocurrencies as securities in Kenya, as well as in Uganda. It should however be recognized that not all cryptocurrencies are securities and therefore Securities regulation would not apply across the board.

e) El Salvador

On September 7th 2021, El Salvador's legislation on Bitcoin went into effect, making it the first country in the world to formally make Bitcoin legal tender.²⁸ Salvadorans may now access bitcoin through a Government Exchanger and may choose whether to manage their bitcoins via custodian or non-custodian wallet. No commission is to be charged to merchants and the Development Bank of El Salvador will facilitate automatic convertibility which means that businesses that get paid in bitcoin can also opt to receive US Dollars.

It is however unclear as to the impact the move will have on the valuation of El Salvador's currency reserves and how this could affect its credit in the Capital Markets.

5.2 International Monetary Fund Best practice

On February 8, 2023, the Executive Board of the International Monetary Fund (IMF) discussed a board paper on Elements of Effective Policies for Crypto Assets that provides guidance to IMF member countries (including Uganda) on key elements of an appropriate policy response to crypto assets.²⁹ The Board paper presents nine elements that can help members develop a comprehensive, consistent, and coordinated policy response. Bearing in mind that these elements are still new, there is no indication that they have been applied in Uganda as yet. They are as follows:

1. Safeguard monetary sovereignty and stability by strengthening monetary policy frameworks and do not grant crypto assets official currency or legal tender status.
 2. Guard against excessive capital flow volatility and maintain effectiveness of capital flow management measures.
 3. Analyze and disclose fiscal risks and adopt unambiguous tax treatment of crypto assets.
 4. Establish legal certainty of crypto assets and address legal risks.
 5. Develop and enforce prudential, conduct and oversight requirements to all crypto market actors.
 6. Establish a joint monitoring framework across different domestic agencies and authorities.
 7. Establish international collaborative arrangements to enhance supervision and enforcement of crypto asset regulations.
 8. Monitor the impact of crypto assets on the stability of the international monetary system.
 9. Strengthen global cooperation to develop digital infrastructures and alternative solutions for cross-border payments and finance.
- These nine elements can thus be considered as foundational principles or guidelines to be relied upon by any country that wishes to develop a regulatory framework for cryptocurrencies.

²⁷ *Id.*

²⁸ See: *El Salvador passes law on cryptocurrency transfers*, <https://www.aljazeera.com/news/2023/1/12/el-salvador-passes-law-on-cryptocurrency-transfers#:~:text=El%20salvador%2C%20which%20became%20the,the%20state%20and%20private%20entities>. (accessed June 13, 2023). This is the Bitcoin Law of June 8, 2021.

²⁹ See: <https://www.imf.org/en/Publications/Policy-Papers/Issues/2023/02/23/Elements-of-Effective-Policies-for-Crypto-Assets-530092> (accessed June 14, 2023)

Conclusion and Considerations for Future Adoption

Conclusion

Cryptocurrencies are portrayed in this policy brief as facilitating digital technologies and improving efficiency in trade as they bypass middlemen and all the inconveniences that go with financial transactions in the ordinary business sense. As more countries begin to embrace the prospects of regulating Cryptocurrencies, it is inevitable that rather than completely disregarding them, the considered approach is to study all the risks involved and find ways of mitigating them so as to enjoy the benefits that come from using cryptocurrencies. As such, Uganda should exploit this approach as well, with the consideration of the recommendations highlighted below.

Recommendations

a) Government MDAs, particularly Bank of Uganda, Ministry of Finance, Planning and Economic Development, Uganda Revenue Authority and Finance Intelligence Authority, should clearly define the legal status of cryptocurrencies and avoid the ambiguity under the current regulations for e-transactions so as to be able to enforce them on all inflows and outflows in business and personal accounts. This includes redesigning capital controls to include flows channeled through cryptocurrencies. In the same vein, well-structured regulation on cryptocurrencies would remove uncertainties for other stakeholders in the private sector and thus encourage their engagement in digital transactions involving crypto assets.

b) The regulatory regime can never be able to effectively catch up or be at the same pace as the technical evolution of cryptocurrencies. As such, Uganda should work with regional and international partners in the establishment and implementation of a global or regional cryptocurrency regulatory treaty that considers the needs and challenges of developing countries. This includes, among others, technological transfer and capacity development; addressing the risks involved in cross border cryptocurrency transactions inclusive of money laundering and jurisdictional issues.

c) Apart from embracing a regional or international treaty, regional or international economic corporation or collaboration is also necessary due to the cross-border nature in the operation of cryptocurrencies. Uganda and partner States should engage in the sharing of a comprehensive system of information on cryptocurrency development and trading systems. Such information sharing would be beneficial for capacity development, strengthening joint enforcement measures as well as address evasion of capital controls and enforcement of taxes.

(d) As opposed to the general perception that crypto assets fall under the interpretation of securities under the Capital Markets Authority Act, so as to warrant their regulation under that law, clarity is required in this regard. The Capital Markets Authority should develop guiding principles as to how security tokens can be utilized to mitigate any risks due to a confusion in this regard.³⁰

³⁰ *Ibid*, fn 8 *supra*



Collaboration on International ICT Policy for East and Southern Africa (CIPESA)

📍 Plot 6 Semawata Place (Off Semawata Road) Ntinda, Kampala

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