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The impact of the legalization of Bitcoin in the Central African Republic – a legal analysis

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ABSTRACT

Cryptocurrencies have since their inception assumed a controversial role in the worlds financial economy, with advocates outlining the significant benefits and independence from a central institutions, while opponents focusing on the lack of regulation, volatility and usage for illegal activities. Cryptocurrencies have for several years been considered primarily for transactions and speculations with the price of bitcoin fluctuating widely in between. With the significant growth of blockchain technology and the cryptospace, as well as legalization of cryptocurrencies in several jurisdictions, the COVID pandemic and resulting challenges to the financial system has led El Salvador to introduce bitcoin as a legal tender, which was followed by the Central African Republic. The Central African Republic has made bitcoin a legal tender and reserve currency in April 2022 in addition to the CFA Franc. While bitcoin and other cryptocurrencies have been legal in many jurisdictions, they are typically considered as capital assets. In making bitcoin a legal tender, there are several legal risks and opportunities that arise from this. The legal risks encompass issues with the contracts and jurisdiction that are especially relevant in an international legal framework. Given the decentralized nature of bitcoin and its international usage, transaction data are shared across the world which may raise legal issues related to tax implications, data theft and fraud, and intellectual property. We will address in this article the legal challenges and risks of the legalization of bitcoin in the Central African Republic, and the possible opportunities. The analysis of the legalization of cryptocurrencies as a tender and reserve currency leads to a completely new legal environment.

1. Introduction

The legalization of Bitcoin as a legal tender in the Central African Republic has been a major shift in how cryptocurrencies are perceived in the world. After Salvador introduced Bitcoin as a legal tender in the nation, the Central African Republic is now the second economy that aims to utilize cryptocurrencies in order to support the economy and exchange of goods and services.[1]

The Central African Republic had significant time to investigate the experience of El Salvador in its utilization of bitcoin as a legal tender. The Salvadorean government has introduced bitcoin as a legal tender in 2021, creating a government-backed digital wallet that enables anyone in Salvador to use the

[1] AFP. 2022. *Central African Republic adopts bitcoin as legal currency.* April 27. Accessed May 16, 2022. https://www.france24.com/en/africa/20220427-central-african-republic-adopts-bitcoin-as-legal-currency.

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cryptocurrency.[2] The government invested significant amounts into the legalization process, amounting to some 180 million USD and required that any business accept the cryptocurrency for payments. El Salvador legalized bitcoin for several reasons, such as the reduction of the strong reliance on the US Dollar by the economy and the reduction in the cost of transfer. Furthermore, the legalization of a cryptocurrency shall further help attracting foreign investment and boost overall domestic consumption. The US Dollar plays a dominant role in the El Salvadorian economy due to the fact that it became legal tender in 2001.[3] El Salvador utilized a pegged exchange rate mechanism at a rate of 8.75 colon per US Dollar from the period of 1993 until 2000, which led to the implementation of the US Dollar at a time when the macroeconomic fundamentals were strong, inflation was low and stable and the economy was growing.[4] Furthermore, public and external debts were manageable and the country exhibited a solid banking system. The main arguments for the legalization of the US Dollar was the strong connection between the United States and the El Salvadorian society with many Salvadorians living in the United States and sending remittances back to El Salvador. Additionally, the expectation was that the strong link with the US economy will enable the support of foreign investment and trade, subsequently supporting economic growth.[5] Extensive research on the dollarization of an economy have been conducted within the last decades and in general the effects are positive. However, there are several challenges that arise from the implementation of a legal tender of another country. The first challenge is that the monetary policy is entirely dependent on the decisions by the United States and its economic situation. This implies that it is impossible for the Central Bank of El Salvador to conduct its own monetary policy and adapt interest rates to stimulate economic growth.[6] This forces the government to solely utilize fiscal measures in order to adapt to the needs of the economy, while being heavily influenced by the monetary policy decisions of the Federal Reserve. Specifically, if the economy is booming and there exists strong inflationary pressure, such as in 2022, the Federal Reserve will raise interest rates irrespective of the economic condition of the El Salvadorian economy, which may move the El Salvadorian economy into recession territory. Another major challenge the El Salvadorian economy faces is that it is required to purchase US Dollars in order to have sufficient liquidity in the market to support the economy.[7]

Personal remittances play a critical role in the Salvadorian economy, amounting to almost 24 % of the GDP. In comparison with other Latin American countries, this makes El Salvador one of the most remittance reliant economies in the region, putting it in the same category as other countries such as Tajikistan, Samoa and Tonga.[8] This makes the country strongly reliant on the economic performance of the United States and the remittances of Salvadorians to the country. This necessarily creates significant challenges in terms of that if the remittances dry up, the economy would be significantly affected and experience a reduction in the GDP. While the pegging to the US Dollar creates several advantages, such as a stable currency regime and stronger investment guarantees.[9]

[2] Alvarez, F. E., D. Argente, and D. Van Patten. 2022. *Are Cryptocurrencies Currencies? Bitcoin as Legal Tender in El Salvador.* National Bureau of Economic Research.
[3] Oxford Analytica. 2021. *El Salvador bitcoin experiment comes with risks.* Emerald Expert Briefings.
[4] Cáceres, L. R. 2021. "The monetary policy transmission mechanism in a dol-larized economy. The case of El Salvador." *Cuadernos de Economía* 713-746.
[5] Lopez, J. R., and M. A. Seligson. 2019. "Small business development in El Salvador: the impact of remittances." *Migration, Remittances, and Small Business Development* 175-206.
[6] Gorjón Rivas, S. 2021. "The role of cryptoassets as legal tender: the example of El Salvador." *Economic bulletin/Banco de España* 4.
[7] Pérez Caldentey, E., and M. Vernengo. 2020. "The historical evolution of monetary policy in Latin America." *Handbook of the History of Money and Currency* 953-980.
[8] Warnecke-Berger, H. 2020. "Remittances, the rescaling of social conflicts, and the stasis of elite rule in El Salvador." *Latin American Perspectives* 202-220.
[9] Sousa, L., and A. F. García-Suaza. 2018. "Remittances and labor supply in the Northern Triangle." *World Bank Policy Research Working Paper* 8597.

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The introduction of bitcoin as a legal tender was made against the recommendation of the International Monetary Fund with the aim of attracting international investors in the cryptocurrency area. Bitcoin is a highly volatile asset with the price of the cryptocurrency fluctuating widely within limited period of times, which makes the storage of wealth and transactions uncertain and subject to timing. The Salvadorian government introduced the Chivo Wallet that has become a considerable stumbling block given that the app has significant security requirements, which conventional mobile phones may not satisfy, and updates caused considerable problems with individuals even losing access to their funds. Additionally, challenges arise from the irreversibility of the transactions, digital fraud and the complexity of user access codes. The cryptocurrency law required anyone to accept the cryptocurrency where the government introduced an option that allows businesses to automatically convert the cryptocurrencies into US Dollar. Further challenges arise for the economy if taxes are quoted in bitcoin, which may lead to significant exchange risks and may also reduce economy activity and interest. Another major challenge facing users in the Salvador from utilizing bitcoin for transactions is the electronic nature of the currency. While the internet penetration rate in Salvador has reached 55 % in 2020 and has risen sharply in the last several years, this implies that almost every second resident in El Salvador does not have access to the internet and may not utilize bitcoin. This puts smaller businesses that lack internet access at a significant disadvantage and make them more susceptible to violations of the law.[10]

The experience in El Salvador has outlined the challenges faced by the legalization of cryptocurrencies as legal tenders.

2. Bitcoin legalization in the Central African Republic

The Central African Republic has recently announced the legalization of bitcoin as a legal tender in the country. The Central African Republic is after El Salvador the second country that aims to utilize the cryptocurrency for driving economic growth and the establishment of new blockchain associated industries. The main objective was to have an alternative tender to the used Central African CFA franc that has had both positive and negative effects on these economies.[11] The Central African CFA franc is the currency of six African countries in Central Africa, which consist of Cameroon, Central African Republic, Chad, Republic of the Congo, Equatorial Guinea and Gabon. The CFA franc was introduced into the French colonies by 1945, which replaced the French equatorial African Franc and the currency remained in use after their dependence. The currency was initially pegged to the French franc, having been devalued by halve and ever since 1999 been pegged to the Euro. While the CFA franc is an independent currency, the peg requires it to follow the monetary policy of the European central bank.[12] Specifically, this creates a strong link between the economies which limits the ability of the central banks to address different monetary policy goals and support different economic development stages. Furthermore, the multinational nature of the CFA France is both a blessing as well as a challenge as several different nations utilize the same currency but experience different degrees of development. Furthermore, the existing CFA Franc is a physical currency with most transactions in all the utilizing countries being primarily in cash.[13] This is primarily due to the low penetration of cards, limited banking access and low degree of internet access amongst the population.[14]

Specifically, internet access is one of the basic requirements for bitcoin transactions to operate efficiently. While conventional cash is physical, and can be exchanged without any additional infrastructure, digital currencies require an internet connection in

[10] Oxford Analytica 2021.
[11] Kangami, D. N., and O. Akinkugbe. 2021. "Common Currency and Intra-Regional Trade in the Central African Monetary Community (CEMAC)." *Journal of African Trade* 13-22.
[12] Giorgioni, G. 2019. "The CFA Franc Zone: a political re-evaluation twenty years after the advent of the Euro." *Journal of Contemporary African Studies* 379-403.
[13] Wilson, J. 2020. "Losing currency? The shifting landscape of the CFA franc zones." *Third World Quarterly* 736-754.
[14] https://bitcoinist.com/the-actual-text-from-the-car-bitcoin-law/

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order to be able to conduct the transactions. Specifically, the bitcoin network distributes the transactions on the ledgers across thousands of computers on the network. In the case of a lack of internet access, these would stop communicating with each other in case the internet is down. While this would not affect the content of the ledgers in the blockchain, it will stop synchronizing. As soon as the computer is again connected, the copies can be verified for consistency. In case there is an inconsistency, then either the blockchain can be updated or one can opt-out of the network. The challenge still remains that users cannot conduct bitcoin transactions. There are various estimates for the user penetration, ranging from 4 % to 10 %, which is by all means a very low level to support the wide adoption of bitcoin for transactions within the country.[15] Given the fact that both parties will need to have access to the internet in order for the transaction to succeed, this will make bitcoin only relevant to a small group of the population. The legalization of bitcoin brings further regulatory concerns, as merchants without internet access may get fined if they do not accept bitcoin for transactions.

When analyzing the new law, the text promulgates the creation of a new national agency for the regulation of electronic transactions, abbreviated as ANTE. The organization will be responsible for all public ATMs both in terms of controlling and managing. However, the law does not provide details on its further tasks and objectives. Additional questions arise how the responsibilities between banks and the new organization are shared, and how the organization engages with the Bank of Central African States that issues the CFA Franc.[16]

Naturally, the question arises whether other cryptocurrencies may receive also a form of official status. The law explicitly defines that only bitcoin is a legal tender and reserve currency, but the law also covers various cryptocurrencies that may be in operation.

The second article implies that the law applies to individuals and institutions, both private and public, which offer services through blockchain technology. These services lead to the creation of smart contracts to procure goods and services. Naturally, questions arise from this article whether the law is limited to institutions using smart contracts, or if the party utilizes blockchain technology but not smart contracts.[17]

Article four of the law specifies that a cryptocurrency is a digital currency issued by peer to peer without the need of a central bank and is based on blockchain as well as usable through a decentralized network. This puts in questions Central Bank Digital Currencies (CBDC) which are issued by Central Banks and may not utilize a decentralized network approach. The e-CNY would not satisfy the criteria for being considered a cryptocurrency and would need to be addressed within a different context.[18]

Article 6 of the law defines that any electronic transaction may be expressed in cryptocurrencies, and that also tax contributions may be paid in cryptocurrencies. Confusion arises here as the cryptocurrency trades are not subject to tax, but profits resulting from the trading of cryptocurrencies is subject to taxation (article 16). Another question arises whether taxes are denominated in bitcoin or only in CFA Franc.[19]

A critical provision of the law is that bitcoin and CFA franc may be instantaneously converted and the law stipulates that provisions shall be instituted, such as the creation of a trust, that enables this automatic and instantaneous conversion.

A key part of the law is article 21 that exempts businesses and individuals that do not have access to the technology to enable the cryptocurrency transaction. For all others, article 19 stipulates that

[15] Misic, J., V. B. Misic, and X. Chang. 2019. " On ledger inconsistency time in bitcoin's blockchain delivery network." *2019 IEEE Global Communications Conference (GLOBECOM)* . IEEE. 1-6.

[16] President of CAF. 2022. *Regissant la cryptomonnaie en republique centrafricaine.* L'Assemble Nationale - Central African Republic.

[17] Ibid, Article 2.

[18] Ibid, Article 4.

[19] Ibid, Article 6.

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everyone is required to accept bitcoin for transactions. The main question is what qualifies for getting an exemption for not being able to process bitcoin payments.[20]

3. Bitcoin as a legal tender – legal risks and opportunities

The legalization of bitcoin as an official tender bring significant opportunities but also considerable risks.

Contract issues

The first challenge is that contractual issues may arise from the utilization of cryptocurrencies. Smart contracts act as a basis upon which the parties in a transaction fulfill their specific promises. This revolves around the automatic payment when the other party fulfills the contract. This requires that smart contracts have to be dealt with either separately or that contract law has to be adopted in order to take into account the complexity and nature of these smart contracts. This is especially relevant at an international level as well as domestic level where the contract law regulations may vary. While there are provisions related to electronic signatures that make it legal in specified circumstances, there are challenges when it relates to smart contracts where they have to be accepted.

Jurisdictional issues

Another issue revolves around the jurisdictional challenges that may arise. Blockchain technology has at its core the anonymity of the ledger's actual location. This enables greater privacy than transactions on traditional platforms. However, there are jurisdictional challenges that arise from it. First, the nodes of crypto transactions may be located in different jurisdictions, where different conflicting legal frameworks may be in place.

Additionally, the residence country of the cryptocurrency is challenging to be determined given the lack of the ledger's physical location. Additionally, the transactional nature of blockchains makes the determination of applicable laws and the correct jurisdiction for blockchain disputes challenging. While even the legalization and sole domestic intended usage may be possible, the technology's cross-border reach may make this challenging to enforce the laws for blockchain based transactions.

Data Theft and Financial Fraud

An additional challenge is data theft or financial fraud that are significant concerns surrounding cryptocurrencies. Anonymity may provide users with a greater opportunity to conduct illegal activities utilizing cryptocurrencies. The first issue is the security of the digital wallet that is used for the transactions. Security flaws in the Ethereum blockchain have led to more than 250 million USD being put at risk of theft. This requires that there are robust data laws that address data theft and financial fraud which may originate from cryptocurrency transactions.

Privacy Concerns

The privacy concerns represent another crucial part related to data theft. While initially the viewpoint is that bitcoin transactions are anonymous, there are providers that may trace a significant majority of transactions. While the digital wallets may be registered, it may enable also transactions outside the digital wallet utilizing bitcoins, which may represent a challenge when it comes to data regulations where parties may be in different jurisdictions. The Central African Republic currently does not provide an official wallet, such as the Chivo Wallet in El Salvador, which makes it reliant on externally provided wallets.[21] However, the Chivo Wallet does not allow to store one's private key, which implies that the government of El Salvador as the owner of the Chivo Wallet has full control over the wallet.

Money Laundering

As previously outlined, cryptocurrencies enable new ways of committing fraud and money laundering, as well as new financial crimes. This viewpoint arises from the fact that dark-market sites have been utilizing cryptocurrencies in order to buy and sell illegal items without the chance of being identified. Over-the-counter

[20] Ibid, Article 21.

[21] Stacker News. 2022. *Full English Translation of the Central African Republic Cryptocurrency Law.* April 29. Accessed May 16, 2022. https://stacker.news/items/23946.

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trading represents a major challenge as this is outside the real of the identification requirements of the digital wallet that is provided by authorities.

Tax Implications

The major question will arise how cryptocurrencies are classified in terms of taxation and based on which value the transaction is taxed at the time of the transaction. This requires from the tax authorities a diligent recording of the price at which the cryptocurrencies are bought and sold. Furthermore, the classification of cryptocurrencies will be critical to determine whether they are classified as capital assets or currencies, and how they are subject to income tax.

Intellectual Property

The growing popularity of cryptocurrencies has led to significant interest when it comes to intellectual property. This includes pharmaceutical, automotive, luxury and consumer goods industries, where traceability and counterfeit goods are a major concern. Cryptocurrencies are utilized in these areas already but lead to the concern of IP ownership and authorship, as well as controlling and tracking the distribution of registered and unregistered IPs. The establishment and enforcement of IP agreements, licenses and the exclusive distribution networks via smart contracts is a crucial challenge. Furthermore, there is uncertainty who owns the blockchain technology and cryptocurrency and verify their ownership.

Legal and Regulatory Concerns for Investors

Another challenge is the legal concerns of cryptocurrencies and whether they are legal to be held is a major challenge, especially when it refers to international transactions. For investors, questions arise also in terms of their backing and how stable the cryptocurrencies are. There is no backing generally, such as gold or silver, and the value depends on what the owners and investors ascribe to the cryptocurrencies. In case there are complications, there are few legal resources that an investor can avail to protect their rights.

4. Conclusion

The legalization of bitcoin as a tender in the Central African Republic has led to growing interest in how bitcoin can support economic growth and function as a legal tender.

While the legalization of bitcoin has been a major event, the two countries El Salvador and Central African Republic are nations in a development stage with low internet penetration. In the case of the Central African Republic, less than 10 % has robust access to the internet, which will reduce significantly the utilization of bitcoin for transaction purposes.

Besides the utilization challenges, there are legal risks that may arise from the utilization of cryptocurrencies, which have to be addressed. Specifically, as bitcoin is decentralized, legal questions surrounding ownership, data privacy and usage in an international framework have to be taken into account. Additionally, the CFA Franc is a multi-country currency and there will be questions to what extent bitcoin and other cryptocurrencies will be permitted by the members of the central banks to be utilized as a reserve currency.

Finally, the legalization of bitcoin as a tender will lead to the gathering of information and experience on how decentralized cryptocurrencies can act as official currencies of nations, and what legal challenges may arise in practice.

Conflict of Interest

The authors have no conflicts of interest to declare. There are two co-authors, and there is no financial interest to report. We certify that the submission is original work and is not under review at any other publication.

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