

**APPRAISAL OF DIGITAL DISRUPTION IN THE BANKING
SECTOR IN NIGERIA: CREATING A SUSTAINABLE LEGAL
FRAMEWORK**

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Abstract

Technology has always impacted the banking industry, and customers want to stay current. Until the early 2000s, banks required a few days to transfer money across bank accounts in various Nigerian states. Today, most of these banks offer mobile applications through which you can open a fully functional bank account, make investments, and buy things without physically going to a bank or seeing or handling money. Thus, the banking industry has been democratised and transformed by digital disruption. Digital disruption is defined as the development of new markets and value networks that eventually subvert established market leaders and alliances by dislodging current markets and value networks. In light of this, this paper seeks to examine the need to create a sustainable legal framework in the banking sector. In achieving this, a doctrinal methodology was adopted by consulting primary sources of law such as the Bank and Other Financial Institutions Act 2020, Central Bank of Nigeria Act 2007, and other legal instruments, and secondary sources of law such as journal articles, and online sources which were all subject to content analysis. This paper found that the fragmented legal framework cannot effectively address issues of digital disruption in the banking sector. This paper concludes that lawmakers should

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establish a sound regulatory framework in the country to safeguard consumers and corporate entities while using technology to reshape the banking sector.

Keywords: *Digital Banking, Digital Disruption, Fintech, Nigeria Sustainable Framework,*

1.0 Introduction

It's undeniable that what first served as a way for people to communicate across borders, exchange ideas, or find pleasure has expanded its sphere of influence to encompass every aspect of daily life. It started with the World Wide Web (WWW) and has since grown to include social media, mobile apps, virtual reality, robotics, smart devices, information technology, data mining, cloud storage/computing, and fintech Innovations have sprung from the mining and efficient use of technology.²

The constant advancement of technology has resulted in the digital transformation of almost every industry and business. This system is changing how the average person sees how financial activities are carried out due to disruptive Fintech inventions.³ Banking is transitioning from a branch-based (i.e., physical location) model to one that mainly depends on information technology, big data, and highly qualified human resources.⁴

² O Ojo and U Nwaokike, "Disruptive Technology and the Fintech Industry in Nigeria: Imperatives for Legal and Policy Responses" (2018) 9(3) *The Gravitas Review of Business & Property Law* <<https://www.researchgate.net/publication/330255465>> accessed 29 September 2023.

³ Jacques Bughin, Laura LaBerge, and Anette Mellbye, "The Case for Digital Reinvention." *McKinsey Quarterly* (2017) <<https://www.mckinsey.com/~media/McKinsey/Business%20Functions/McKinsey%20Digital/Our%20Insights/The%20case%20for%20digital%20reinvention/The-case-for-digital-reinvention-vF.pdf>> accessed 29 September 2023

⁴ VC Ehiedu, and others, "Innovative banking models and banks fragility in post covid-19 era in Nigeria" (2022) 6(5) *International Journal of Academic Accounting, Finance &*

Financial innovations that are more disruptive to banks core activities, such as, payment and advising services, as well as increased competition from other intermediaries, are both posing a threat to the industry. A shift in the application of financial disruptive innovations in creating new services and business models has been unfolding with the growth of the FinTech industry (short for Financial Technologies).⁵

Traditional financial services have been governed and overseen for many years by a number of established regulatory bodies, both internationally and in Nigeria. Additionally, industrialized nations with significant and developed financial markets like the United States of America, the United Kingdom, and China are feeling the effects of the ongoing digitalization and disruptive technologies in relation to their numerous traditional financial services.⁶

As a result, they are currently putting into place efficient regulatory measures for their respective Fintech industry. In this regard, there is a clarion call for a sustainable legal framework that will regulate these digital disruptions in the banking sector in Nigeria. The urgent need for regulatory action in the Nigerian financial sector is primarily driven by the desire to solve the unusual problems raised by this innovation and to give the sector's various stakeholders regulatory clarity.

Management Research 91-100 < <http://ijeais.org/wp-content/uploads/2022/5/IJAAFMR220509.pdf>> accessed 29 September 2023

⁵ DG Oldenbourg, "Xavier Vives: Competition and Stability in Banking: The Role of Regulation and Competition Policy" (2017) 37(2) *Journal of Economics and Statistics* 147-150 <<https://www.degruyter.com/document/doi/10.1515/jbnst-2017-1001/pdf>> accessed 29 September 2023

⁶ O Ojo and U Nwaokike, "Disruptive Technology and the Fintech Industry in Nigeria: Imperatives for Legal and Policy Responses" (2018) 9(3) *The Gravitas Review of Business & Property Law* <<https://www.researchgate.net/publication/330255465>> accessed 29 September 2023.

1.1 Objectives of the Study

The objectives of the study are to:

1. Explore the concept of digital disruption, Fintech and digital banking
2. Examine the current legal frameworks for Digital Disruptors
3. Ascertain the causes of digital disruption in the banking sector
4. Embark on a voyage to the policy and regulatory approach in the United Kingdom and the United States of America on digital disruption
5. Access the challenges faced in regulating digital disruption
6. Examine the process of creating a sustainable legal framework for the future of banking in Nigeria

2.0 Conceptual Clarification

2.1 Digital Disruption

It is defined as the development of new markets and value networks that eventually subvert established market leaders and alliances by modifying current markets and value networks.⁷ It is an invention that adds more value when it upsets the status quo.⁸ Digital disruption is described as a technology that modifies an existing technology and upends the market or a game-changing product that births a brand-new market. Digital disruption is the term used to describe the change brought about by emerging computerized developments and strategies.⁹ The idea of "Disruptive Innovation" is closely related to that of "Disruptive Technology" and refers

⁷ Olatunji Tolu, "Advancing The Cause Of Fintech In Nigeria Through Regulation" (2020) 11(4) *The Gravitas Review of Business & Property Law* <<https://d1wqtxts1xzle7.cloudfront.net/65259300/>> accessed on 29 September 2023

⁸ N Krstic and others, "Digital Disruption of the Banking Industry- Threat or Opportunity?" (2016) <<https://www.researchgate.net/publication/305629159>> accessed 29 September 2023

⁹ S Ahana, "Impact of Digital Disruption on the Indian Banking Sector" (2022) <<https://www.researchgate.net/publication/349695047>> accessed 29 September 2022

to the process by which a good or service first establishes itself in basic applications at the bottom of a market before ruthlessly moving up the market and eventually replacing established rivals.¹⁰ The banking sector has been threatened by these disruptions and the concurrent disruptive forces are fintech. They have created a financial environment that is ruled and controlled by the internet, continual connectivity, mobility, and quick pleasure, fundamentally altering the nature of the business. Online banking has also been made possible via the internet, allowing clients to get financial services without having to visit banks for them.¹¹

2.2 FINTECH

As the term implies, fintech mainly refers to the integration of finance and technology.¹² FinTech, which Price Waterhouse Coopers defines as "a dynamic segment at the intersection of the financial services and technology sectors where technology-focused startups innovate the products and services currently provided by the traditional financial services industry."¹³ FinTech has democratized and revolutionized the financial services industry. It has allowed new players to carve out a significant piece of the pie for themselves by offering innovative solutions through intuitive apps that upend the traditional customer experience for something simpler and smoother. Without a doubt, traditional financial

¹⁰ Clayton M Christensen and others, "What is Disruptive Innovation" (December 2015) *Harvard Business Review* <<https://hbr.org/2015/12/what-is-disruptive-innovation>> accessed 29 September 2023

¹¹ Lilian Aoko Peters, *Effect of Digital Disruption on the Financial Performance of Commercial Banks in Kenya: A Case of Ecobank Kenya Limited* (MBA Dissertation School of Business, The Catholic University of Eastern Africa 2017)

¹² I Goldstein, W Jiang, GA Karolyi, "To FinTech and Beyond" (2017) 32(5) *The Review of Financial Studies* 123.

¹³ IH Chiu, "The Disruptive Implications of Fintech – Policy Themes for Financial Regulators" (Digital Currencies and Finance Conference, Centre for Law, Economics and Society, UCL, Athens, 2016) <<http://discovery.ucl.ac.uk/id/eprint/1528728/1/the%20Disruptive%20implications%20of%20fintech%Rev.pdf>> accessed 30 September 2023

institutions are faced with the reality of either metamorphosing into the digital space or risk extinction.¹⁴

2.3 Digital Banking

Digital banking can be defined as the digitalization of all conventional banking services that historically were offered to clients in person at a bank branch.¹⁵ Digital banks can also be described as fast-growing fintech companies hosted online to provide customers with seamless banking and other financial services, and they include; Opay, Kuda Bank, Rubies, ALAT, Monnie point, Mint App, One Bank¹⁶

3.0 Examination of Current Legal Framework for Digital Disruptors

Although innovative Fintech has received enormous interest and popularity in recent years, no significant success has been achieved in the regulatory landscape. However, a combined reading of various legislation which will be examined shortly, are aimed at regulating these digital disruptors.

3.1 Central Bank of Nigeria Act 2007

In exercise of the powers conferred on the CBN by section 47(2) of the CBN Act 2007, the Regulatory Framework for Mobile Payments Services in Nigeria leading to the Guidelines for Mobile Money Services in Nigeria was established. Also, the regulatory framework for Bank Verification Number (BVN) was also released in an effort to safeguard the security of Nigeria's electronic payment system. In Nigeria, it's possible that there isn't currently any particular regulation governing digital disruptors. The CBN,

¹⁴ T Olatunji, "Advancing The Cause Of Fintech In Nigeria Through Regulation" (2020) 11(4) *The Gravitas Review Of Business & Property Law* 6.

¹⁵ This comprises operations including money transfers, withdrawals, and deposits, as well as management of checking and savings accounts, loans, bill payments, and account services. see I Marshel & K Nkwadochi, "Effect of Digitalization of Banking Services on the Nigeria Economy" (2022) 2(1) *Contemporary Journal of Banking and Finance* 56.

¹⁶ IA Ogbuji, MM Ologundudu, & OO Oluyomi, "Comparative Analysis of Financial Technology and Traditional Bank Performance in Nigeria: The Camel Approach" (2021) 6(1) *UNILAG Journal of Business* 145-168.

however, has taken great initiative to make sure that best practices in the banking industry are followed.

3.2 The Nigeria Data Protection Act 2023

The Act establishes the Nigerian Data Protection Commission¹⁷, and vests it with the power to regulate the deployment of technological and organizational measures to enhance personal data protection.¹⁸

3.3 The Federal Competition and Consumer Protection Act 2018

It demands that service providers refrain from engaging in transactions with customers for the supply of goods or services in ways that are unfair, unreasonable, or unjust.¹⁹

3.4 Cyber Crimes (Prohibition, Prevention, Etc.) Act, 2015

Notably, the Act creates a framework for cyber security, which in turn protects the protection of electronic communications, intellectual property, privacy rights, data and computer programmes, computer systems and networks, and data and computer programmes.²⁰

3.5 Banks and Other Financial Institutions Act 2020

The Act provides that the Bank may make regulations and issue guidelines to banks to address cyber security issues in the delivery of financial or banking services.²¹

¹⁷ Nigeria Data Protection Act 2023, s 4.

¹⁸ Nigeria Data Protection Act 2023, s 5.

¹⁹ Federal Competition and Consumer Protection Act 2018, ss 125,126,127 & 128

²⁰ Cyber Crimes (Prohibition, Prevention, Etc) Act, 2015, Ss 1 & 2. The Cyber Crimes Act is a crucial legislation that acknowledges and governs Nigeria's internet usage for electronic commerce. Although the Act does not specifically include online or digital banking, it does cover all types of electronic transactions.

²¹ Banks and Other Financial Institutions Act 2020, s 68.

3.6 Investments and Securities Act 2007

The Nigerian capital market and securities market are governed by the Security Exchange Commission. One-way FinTech companies might raise funds is through the capital market, however, they must register with the SEC.

4.0 Causes of Digital Disruption in the Banking Sector

1. **Bank Crisis and Recapitalization:** A perfect innovative vacuum was created in banks as a result of the 2008 credit crisis and the strict regulation of financial services that followed.²² Following the credit crisis, regulators imposed numerous new regulations on banks as well as severe fines and penalties for non-compliance. As a result, banks were forced to reduce their risk-taking, which has led to a growing disruptive trend in the banking industry that is challenging traditional, conventional banking in the world of venture capital investments.²³
2. **Increasing Demographic Change:** The faith in the banking sector suffered as a result of the financial crisis. Second, the benefits of physical distribution that banks formerly benefited from are starting to be challenged by the widespread use of mobile devices. Smartphones provide fully individualized consumer services as well as a new payment paradigm. There is now an enormous amount more readily available, globally transparent data available, and the price of processing power has dropped significantly.²⁴

²² Many reports show how the rapid development of African Fintech, which exploded in the years following the 2008 global meltdown, is threatening established players in the mainstream financial services sector. see 'The unstoppable rise of Fintech in Africa' (SunTrust bank, 22 August 2016)

²³ In 2014, the global investment in Fintech ventures tripled to \$12.21 billion from \$4.05 billion. Venture investment growth in Fintech in 2014 was 201 per cent compared to 63 per cent in the global Venture capital Investments See Akinkunmi Akingbade, 'Nigeria launched its first Fintech bank: here's what you need to know' (Ventures Africa, 30 August 2016)

²⁴ Ibid.

3. The Customer-Centric Business Model for Fintech Startups: Fintech businesses have been able to develop business models that do away with the formality of being a bank while still offering customers a more effective way to meet their demands. For instance, marketplace lending, which has participants in the US like Lending Club and Prosper, is a Fintech area where the lack of strict capital requirements on newer companies has given these new upstarts significantly better returns than established banks.
4. The Emergence of the Global Pandemic: the outbreak of the global pandemic COVID 19, gave momentum to digital disruption by providing an alternative to traditional banking service delivery during the period of restriction of movement as well as the need to limit the numbers of customers in the banking halls per time, which have been occasioned by the global pandemic COVID19.²⁵

5.0 Challenges of Regulating Digital Disruption

FinTech dramatically disrupts the current legal and regulatory systems by introducing new financial, technological, and legal realities. Due to the rapid speed of innovation, regulators will certainly experience a rise in workload, necessitating effective and efficient upkeep. FinTech developments scarcely fit into the current regulatory framework and will always make it difficult for the authorities to come up with a suitable response. The appropriateness and promptness of this legal reaction affect not just the sustainability of the FinTech solution but also its potential impact and ability to support constructive social change. But frequently, the regulatory response to financial innovation is vague, contradictory, or

²⁵ O Ajayi, “Digital Banking in Nigeria: The State of Play and Legal Framework” (2021) <<https://www.olaniwunajayi.net/blog/digital-banking-in-nigeria-the-state-of-play-and-legal-framework>> accessed 10 October 2023.

tardy.²⁶ The scope of these FinTech disruptions has altered financial services and is consequently posing regulatory challenges.²⁷

One of the issues of regulating FinTech is the difficulty regulators may have in covering the areas while avoiding the duplication of legal frameworks. FinTech involves the development of new services or the disruption of those that are already available and governed by clear legal and regulatory frameworks. To ensure that the improvement and disruption do not have unfavourable effects, it is also required to intervene legally and within the boundaries of the law as needed.²⁸

Similarly, it can be challenging, if not impossible, to regulate some of the innovations in financial services like virtual currencies. These inventions are nevertheless here to stay, and the regulators will be forced to adapt as much as they can. The primary regulatory responsibilities of systemic stability and consumer protection must be balanced with encouragement for innovation.²⁹

6.0 Comparative Analysis of the Regulatory Approach of Digital Disruption in the Banking Sector in the United Kingdom and United States of America

It is pertinent at this juncture to take a voyage to other jurisdictions to consider the regulatory approach to digital disruption in the banking sector

²⁶ J Kidd, “Fintech: Antidote to Rent-Seeking?” (2018) 93(1) *Chicago-Kent Law Review* <<https://scholarship.kentlaw.itt.edu/cklawreview/vol93/issi/6>> accessed 10 October 2023.

²⁷ Ibid.

²⁸ A Didenko, “Regulating FinTech: Lessons from Africa” (2018) 19(2) *San Diego International Law Journal* <<https://digital.sandiego.edu/ilj/v19/iss2/5>> accessed 10 October 2023.

²⁹ DW Arner and others, “FinTech and RegTech: Enabling Innovation While Preserving Financial Stability” (2017) 18(3) *Georgetown Journal of International Affairs* <<https://dx.doi.org/10.2139/ssrn.3211708>> accessed 10 October 2023.

to draw useful and invaluable lessons for the development of a viable legal, regulatory, and policy environment in Nigeria.³⁰

6.1 United Kingdom

The situation in the UK's Fintech sector has grown alarming and unexpected. In order to encourage the inclusive expansion of the Fintech industry in the region, the regulatory authorities in the UK have been very aggressive and pragmatic in creating a favourable regulatory and legal environment. This is because the regulator, Federal Conduct Authority (FCA)³¹ has provided the right policy and regulatory framework for Fintech to thrive and develop on health grounds.

The FCA is a body in charge of financial regulation in the UK, this body is established by the Financial Services Act 2011, and however, it is independent of the national government and is funded by fees imposed on those who work in the financial services sector. It protects the integrity of the UK financial markets and regulates financial companies offering services to consumers. It focuses on the oversight of both wholesale and retail financial services companies' behaviour. The Enabling Act grants the Authority certain supervisory powers, and it is tasked with supervising banks to ensure that they treat consumers fairly, promote innovation and healthy competition, and assist the FCA in identifying possible hazards early so that they can take steps to mitigate the risks.

³⁰ OV Ojo and U Nwaokike, "Disruptive Technology and the Fintech Industry in Nigeria: Imperatives for Legal and Policy Responses" (2018) 9(3) *The Gravitas Review of Business & Property Law* <<https://www.researchgate.net/publication/330255465>> accessed 29 September 2023.

³¹ Financial Conduct Authority <https://en.m.wikipedia.org/wiki/Financial_Conduct_Authority> accessed 30 September 2023

6.2 United States of America

The regulation of fintech firms appears to mainly be done at the state level. According to recent reports, Arizona became the first state in the US to adopt and implement a regulatory sandbox to guide the growth of new emergent industries like Fintech, blockchain, and cryptocurrencies.³² Similar to its UK counterpart, it offers Fintech companies a venue to introduce and test innovative products in a way that relaxes some regulatory limitations while maintaining consumer safety.³³

7.0 Creating a Sustainable Legal Framework for the Future of Banking in Nigeria

Creating a sustainable framework involves striking a balance between leveraging digital innovations while maintaining stability and security in the banking sector. Any financial regulatory system's objective should be to reduce the likelihood and severity of economic harm and to contain that harm to those who consciously and actively participate in the sector.³⁴

Similarly, three fundamental goals, according to Bummer and Yesha's theory, typically guide rulemaking in the FinTech setting and are relevant to regulatory authorities.³⁵ The three objectives are:

Market Integrity: Regulators are responsible for preventing fraud and ensuring that customers of financial services are shielded from unfair and unlawful practices that might rob them of money, rights, or both. The

³² SG Kramer, "Emerging regulatory framework of Fintech in the US" (Baker McKenzie, 27 May 2016) <<https://www.lexology.com/library/detail.aspx?g=dd2b13d4-7cea-4ae1-8036-4dcbb6364a43>> accessed 11 October 2023

³³ Ibid

³⁴ Ibid.

³⁵ C Bummer, Y Yesha, "Fintech and the Innovation Trilemma" (2019) *The Georgetown Law Journal* 240-241 <<https://www.law.georgetown.edu/georgetown-law-journal/wp-content/uploads/sites/26/2019/02/IFintech-and-the-innovation-Trilemma.pdf>> accessed 11 October 2023.

responsibility of regulators includes promoting investor protection, healthy competition, market confidence, and the stability of financial institutions. Rules Simplicity: Comprehensive regulations that identify and mitigate risks to specific actors and the market as a whole are necessary for maintaining market integrity. To deter dishonest individuals from taking advantage of others, such regulations must also offer robust anti-fraud safeguards. To effectively threaten punishment when rules are broken, the rules must be plainly applied.

Financial Innovation: Regulators should support new products, business models, and technological advancements that help with capital raising, investment diversification, risk management, fraud detection, and better capital market performance.

Thus, in creating a sustainable legal framework for the future of banking in Nigeria, the Central Bank of Nigeria, other regulatory bodies, and where necessary the legislature, must be more proactive, dynamic, and responsive. They must, however, not overregulate as this may curtail innovation.

By implementing a data-driven approach to regulatory regimes, regulators can encourage innovation and provide consumers and industry players with greater options. Regulators can more accurately identify what will likely be the next "big thing" by focusing on the data and metadata surrounding new technology, such as information linked to an investment in new technology and innovation.

Digital disruption provides an opportunity to reach rural areas, and banks should focus on expanding access to financial services through mobile banking, agent's network, and digital wallet in those areas to promote financial inclusion.

Digitalization comes with the need for robust cyber security measures, banks should invest in advanced security systems to protect customer data,

prevent cyber threats, and maintain trust. They must also prioritize data privacy and adhere to strict data protection regulations.

Collaboration between banks, fintech companies, and regulators is crucial to improve the penetration of investment products, encourage responsible practices, and ensure compliance with regulation.

Regulatory agencies should work together to create clear specific licensing regimes for different FinTech businesses in Nigeria.

Regulators must be aware that they are unlikely to have a final regulation or regulatory framework that applies to all situations. Regulators must accept contingency, flexibility, and an openness to new ideas rather than being fixated on finality and legal certainty. Sandboxes and regulatory technologies are a couple of ways to embrace a cooperative, adaptable, and digitalized regulatory framework.

8.0 Conclusion

From the foregoing, it is crystal clear that the banking sector is undergoing a rapid technological revolution, and in the twenty-first century, managing digital disruption has become a key global concern. This study has successfully examined the current legal framework on Fintech, the causes, and challenges in regulating digital disruption. This study found that the fragmented legal framework cannot effectively address issues of digital disruption in the banking sector. Thus, lawmakers should establish a sound regulatory framework in the country to safeguard consumers and corporate entities while using technology to reshape the banking sector. They are also obliged to take a voyage in other jurisdictions such as the United Kingdom and the United States of America in order to aid the enactment of a sustainable legal framework for digital disruption in the banking sector in Nigeria.