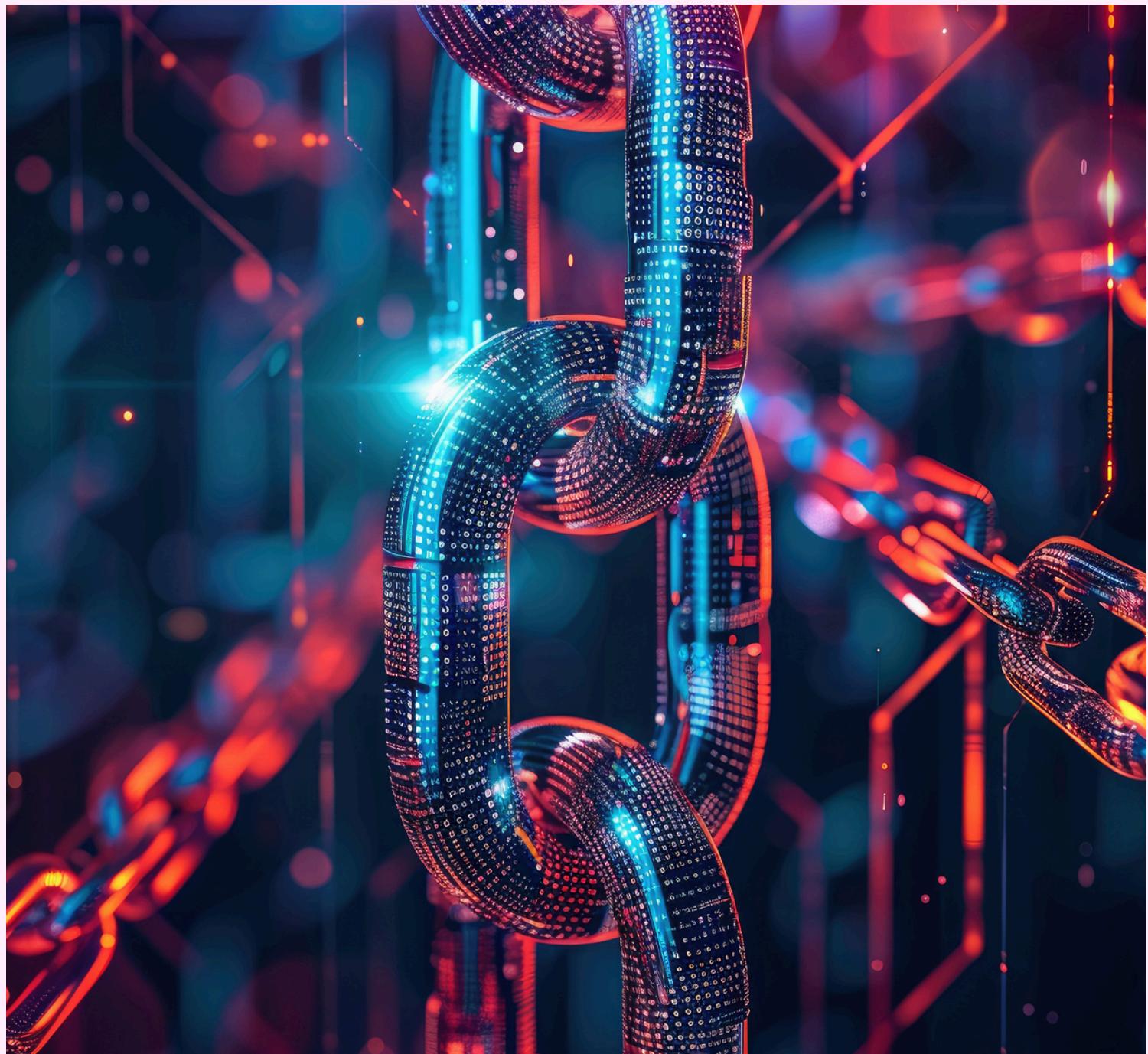


# THE GENIUS ACT & THE REGULATION OF DIGITAL ASSETS: REIMAGINING REGULATORY FOUNDATIONS FOR BLOCKCHAIN INNOVATION

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By: Tola Oshobi, SAN, Olawale Bamidele Adedipe, Christiana Nkechinyere Okechukwu, Afolabi Alawode, Oluwatobi Akinola.



## 1.0 INTRODUCTION

The rapid evolution of digital finance has amplified the need for regulatory frameworks. Transformative technologies such as cryptocurrency e.g. stablecoins (digital tokens pegged to fiat currencies or other assets), amongst others, are already used for payments, remittances and cross-border settlements. Their emergence has exposed regulatory gaps and consumer protection issues. Thus, in response, in July 2025, the United States enacted the **Guiding and Establishing National Innovation for U.S. Stablecoin (GENIUS Act)**. The law is a legislative framework that creates the first federal licensing and supervisory regime for payment stablecoin issuers.<sup>1</sup> By establishing clear regulatory guidelines, protecting consumers, and fostering an inclusive digital economy, the GENIUS Act seeks to strike a careful balance between enabling technological advancement and ensuring responsible financial governance.<sup>2</sup>

## 2.0 BACKGROUND: WHY THE GENIUS ACT?

Stablecoins gained prominence as a medium of exchange and store of value within the digital financial ecosystem, however the regulatory landscape was fragmented and this led to concerns over their potential to disrupt traditional financial systems, pose risks to consumer protection, and contribute to market instability.<sup>3</sup> Cases such as the collapse of TerraUSD (UST), which wiped out about \$50 billion in value in May 2022<sup>4</sup> and investigations into Tether, whose operators overstated reserves and paid \$18.5 million to settle with the New York Attorney General,<sup>5</sup> highlighted risks. Recognising these challenges, U.S. lawmakers proposed the GENIUS Act to create a cohesive and forward-looking framework that balances innovation with accountability. The Act draws from existing financial regulatory principles while adapting them to the unique characteristics of blockchain-based assets.

## 3.0 STABLECOINS: DEFINITIONS & RISKS

To better understand the implications of the GENIUS Act, it is essential to clarify the key concepts that it regulates.

“*Cryptocurrency*” refers to digital or virtual currencies that use systems for secure transactions and operate on decentralized networks, primarily built on blockchain technology.<sup>6</sup>

“*Stablecoins*” represents a form of cryptocurrency designed to maintain a consistent value over time. As the term “*stable*” suggests, these digital assets are typically pegged to a stable reserve, such as a fiat currency like the U.S. dollar, meaning they are not intended to significantly gain or lose value, unlike more volatile cryptocurrencies.<sup>7</sup>

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Coinshares, “GENIUS Act Ushers in New U.S. Crypto Era” (2025) GENIUS Act Ushers in New Crypto Era in U.S. accessed on 3rd August 2025  
2 Ashikur Rahman Nazil, ‘The GENIUS Act: Regulatory Framework for Stablecoins and Its Implications for the U.S. Financial System’ (19th July 2025) [https://www.researchgate.net/publication/393797013\\_The\\_GENIUS\\_Act\\_Regulatory\\_Framework\\_for\\_Stablecoins\\_and\\_Its\\_Implications\\_for\\_the\\_US\\_Financial\\_System](https://www.researchgate.net/publication/393797013_The_GENIUS_Act_Regulatory_Framework_for_Stablecoins_and_Its_Implications_for_the_US_Financial_System) accessed 27 July 2025.

Risks: The rapid rise of stablecoins has created significant regulatory and operational risks. The TerraUSD collapse showed how algorithmic stablecoins can fail without strong reserves or oversight. Similarly, Tether's misrepresentation of its reserves underscored the need for transparency and regulation. These examples underscore the fragility that can accompany the misuse or mismanagement of stablecoins in the absence of well-defined regulatory oversight. While the technology behind stablecoins offers real promise for transforming financial systems, it also opens the door to market instability, consumer harm, and systemic contagion if not adequately regulated.

## 4.0 KEY PROVISIONS OF THE GENIUS ACT

Some of these key provisions are established below:

### *a. Definition and Classification of a Payment Stablecoin*

The Genius Act defines a payment stablecoin as a digital asset designed to serve as a means of payment or settlement, and is redeemable for a fixed amount based on a national currency.<sup>8</sup> Digital assets backed by national currencies, deposits, or securities are excluded from this definition.<sup>9</sup> Payment stablecoins issued by permitted issuers are expressly excluded from the definitions of security and commodity under federal law.<sup>10</sup> This is different from the definition of stablecoins in Nigeria where the Nigerian Securities and Exchange Commission's amended "Rules on Digital Assets Issuance, Offering Platform, Exchange and Custody (Amended VASP Rules) 2025" classify stablecoins as "virtual assets" designed to maintain a stable value relative to a specified asset or basket of assets, including official currencies.<sup>11</sup> Because the Investment and Securities Act 2025 adds "virtual and digital assets" to the definition of securities, Nigerian stablecoin issuers are treated as securities issuers and are subject to regulatory oversight which is not the position under Genius Act.



3 Covington, "the Genius Act becomes law: Key provisions from the Federal Stablecoin Regulatory Framework" The GENIUS Act Becomes Law: Key Provisions from the Federal Stablecoin Regulatory Framework | Covington & Burling LLP accessed on 2nd August 2025

4 <https://mitsloan.mit.edu/cfi/anatomy-a-run-terra-luna-crash#:~:text=Terra%20the%20third%20largest%20cryptocurrency,Poorer%20and%20less%20sophisticated%20investors>

5 <https://ag.ny.gov/press-release/2021/attorney-general-james-ends-virtual-currency-trading-platform-bitfinex-illegal#:~:text=investigation%20by%20the%20Office%20of,of%20steps%20to%20increase%20transparency>

6 Kaspersky, 'What Is Cryptocurrency and How Does It Work?' (8 December 2018) [https://www.kaspersky.com/resource-center/definitions/what-is-cryptocurrency?srsltid=AfmBOoqRgo0vVP7x7fRmYZuNTOM-h1vdPkV2\\_NuKXB\\_ZhYQAgYHqsw7w](https://www.kaspersky.com/resource-center/definitions/what-is-cryptocurrency?srsltid=AfmBOoqRgo0vVP7x7fRmYZuNTOM-h1vdPkV2_NuKXB_ZhYQAgYHqsw7w) accessed 27 July 2025

7 *ibid*

### ***b. Permitted Payment Stablecoin Issuer***

Only **permitted payment stablecoin issuers** may issue payment stablecoins in the U.S. A PPSI must be:

- A subsidiary of an insured depository institution approved by the appropriate federal banking agency
- A federal qualified payment stablecoin issuer (e.g., a non-bank or federal branch approved by the Office of the Comptroller of the Currency (“OCC”).
- A state-qualified payment stablecoin issuer certified by state regulators

Public companies not engaged primarily in financial activities cannot issue stablecoins unless the Stablecoin Certification Review Committee (SCRC) unanimously approves, ensuring they pose no material risk. Issuers cannot pay interest or yield on payment stablecoins.<sup>12</sup>

### ***c. Licensing and Oversight***

The Act prohibits anyone other than a PPSI from issuing payment stablecoins in the U.S. Violations carry penalties of up to \$1 million per violation and five years' imprisonment.<sup>13</sup> Issuers must hold reserves equal to outstanding stablecoins, comprised of U.S. dollars, short-term Treasuries and other high-quality assets.<sup>14</sup> Reserves must be segregated and cannot be pledged or rehypothecated, except for limited transactions such as certain repurchase agreements. Issuers must publish monthly reserve disclosures and undergo audited financial statements.<sup>15</sup>

### ***d. Foreign Issuers***

Foreign stablecoin issuers may offer or sell stablecoins in the U.S. only if their home regulatory regime is comparable to the GENIUS Act's framework, they register with the OCC, hold sufficient reserves in U.S. financial institutions and are domiciled in jurisdictions not subject to U.S. economic sanctions.<sup>16</sup> They must consent to U.S. jurisdiction and comply with supervisory requirements.



<sup>8</sup> Genius Act, 2 (6).

<sup>9</sup> Genius Act, 2 (17).

<sup>10</sup> Genius Act, 4 (23).

<sup>11</sup> Clause 5.0. of the Amendments to the Rules on Digital Assets Issuance, Offering Platform, Exchange and Custody (Amended VASP Rules) 2025

### **e. Federal vs State Regulation**

A state-qualified issuer with less than \$10 billion in outstanding stablecoins may opt to be regulated solely by state authorities if the state regime is “substantially similar” to the federal framework. Once an issuer’s outstanding stablecoins exceed \$10 billion, federal oversight applies.<sup>17</sup>

### **f. Consumer Protection under the Act**

Another key provision of the Genius Act is its consumer protection framework, which requires PPSIs to comply with state consumer protection laws applicable to stablecoins, particularly in relation to marketing, fee disclosures, and redemption processes.<sup>18</sup> Stablecoin holders are prioritized in bankruptcy proceedings, and the act imposes strict transparency obligations.<sup>19</sup> With this provision, the Genius Act establishes itself as the first legislation in the United States to impose tailored consumer protection obligations on issuers of payment stablecoins.



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12 Covington, “the Genius Act becomes law: Key provisions from the Federal Stablecoin Regulatory Framework” The GENIUS Act Becomes Law: Key Provisions from the Federal Stablecoin Regulatory Framework | Covington & Burling LLP accessed on 2nd August 2025

13 Genius Act, 3 (f)

14 Genius Act, 3(d)

15 Client Alert, The GENIUS Act: A New Era of Stablecoin Regulation, Gibson Dunn, 18 July 2025 <https://www.gibsondunn.com/the-genius-act-a-new-era-of-stablecoin-regulation/> accessed on 29 September 2025

16 Client Alert, What the GENIUS Act Means for Payment Stablecoin Issuers, Banks, and Custodians, WilmarHale 18 July 2025

<https://www.wilmerhale.com/en/insights/client-alerts/20250718-what-the-genius-act-means-for-payment-stablecoin-issuers-banks-and-custodians>  
Accessed on 29th July 2025

## ***g. Anti Money Laundering /Counter Terrorism Financing (AML/CFT) Provisions***

PPSIs are now classified as financial institutions and must maintain anti-money laundering and counter-terrorism financing obligations under the Bank Secrecy Act. This includes Know Your Customer (KYC) and Customer Identification Program (CIP) requirements. They must also conduct risk-based Customer Due Diligence, including enhanced due diligence for high-risk clients, as well as monitor transactions and file Suspicious Activity Reports (SARs).

## ***h. Prohibition of Tying Arrangements***

Pursuant to Section 4(a)(8)(A) of the Act, tying arrangements are expressly prohibited. In effect, a PPSI is prohibited from conditioning the issuance of a stablecoin on the customer's agreement to purchase any additional paid product or service from the PPSI. This provision reinforces consumer choice and promotes fair competition by ensuring that access to stablecoins is not used as leverage to compel uptake of unrelated offerings.<sup>20</sup>



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17 Genius Ace, 4 (c) (1)

18 Genius Act, 4 (B).

19 Client alert, The GENIUS Act of 2025: Stablecoin Legislation Adopted in the US , Letham and Watkins LLP, (24 July 2025) <https://www.lw.com/en/insights/the-genius-act-of-2025-stablecoin-legislation-adopted-in-the-us> accessed on 24th July 2025

20 Genius Act, 4a (8)(a)

## *i. Enforcement Mechanisms Under the Act*

Federal agencies are empowered to enforce the Act's licensing and compliance mandates. Specifically, federal payment stablecoin regulators including the Office of the Comptroller of the Currency (OCC) and the Federal Reserve may initiate enforcement actions against federally licensed stablecoin issuers.

## **5.0 BROADER IMPLICATIONS OF THE GENIUS ACT 2025**

The GENIUS Act positions the U.S. as a leader in global stablecoin regulation and signals a strategic shift towards integrating blockchain technology into mainstream finance. Analysts note that the Act's openness to non-bank and foreign issuers fosters innovation, while Europe's **Markets in Crypto-Assets Regulation (MiCA)** takes a more cautious stance, requiring stablecoin issuers to be licensed credit or electronic-money institutions and imposing stricter capital and redemption rules. The divergence reflects differing views: the U.S. sees stablecoins as a potential competitive advantage, whereas the EU focuses on risk mitigation. For global players particularly Nigerian financial institutions operating in a top-tier crypto market, the Act opens new opportunities. By becoming licensed in the U.S. as foreign stablecoin issuers, these institutions can enhance their international competitiveness and support the growth of Nigeria's digital asset ecosystem.

## **6.0 CHALLENGES AND CONSIDERATIONS**

While the Act offers regulatory, it raises several key challenges:

- a. Restricted Scope of Activities for Issuers:** The Act severely limits the business functions of permitted PPSIs. Issuers may only engage in issuing, redeeming and managing reserves. This limited remit may hinder innovation for fintech firms seeking to integrate diverse digital financial services.<sup>21</sup>
- b. The prohibition of yield-Bearing stablecoins:** The ban on interest-bearing stablecoins differentiates payment stablecoins from investment products but may limit decentralized finance (DeFi) innovation.<sup>22</sup>
- c. Jurisdictional Complexity and Regulatory Overlap<sup>23</sup>:** Entities must navigate both federal and state regulatory frameworks leading to potential overlaps and creating uncertainty.
- d. Global Coordination:** A growing contrast is emerging between how Europe and the United States approach digital asset regulation. While Europe has adopted a more cautious, risk-focused regulatory stance which is evident in its slow progress with the Digital Euro. The United States however, through the GENIUS Act, appears to be leaning into innovation. The difference in Digital Asset Regulations between the U.S. and EU frameworks could disrupt global markets and create challenges for cross-border issuance

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<sup>21</sup> Sidley, "The Genius Act: A Framework for U.S. Stablecoin Issuance"(2025) <https://www.sidley.com/en/insights/newsupdates/2025/07/the-genius-act-a-framework-for-us-stablecoin-issuance#:~:text=Timing%20Considerations,contributed%20to%20this%20Sidley%20Update>. Accessed 29th July 2025

## 7.0. CONCLUSION

The GENIUS Act marks a watershed in digital asset regulation. By mandating full reserve backing, prohibiting re-hypothecation and yield payments, and establishing a licensing regime, the U.S. aims to encourage stablecoin innovation while safeguarding consumers and financial stability. The Act's success will depend on timely implementation, harmonisation with state laws and the ability to adapt as the technology evolves. As other jurisdictions consider their own frameworks, the GENIUS Act will shape the global debate on how best to regulate digital assets.

22 Ben Nadareski, The GENIUS Act Killed Yield-Bearing Stablecoins. That Might Save DeFi Coin desk, 16 July 2025

<https://www.coindesk.com/opinion/2025/07/15/the-genius-act-killed-yield-bearing-stablecoins-that-might-save-defi> accessed on 29th July 2025

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**Babalakin & Co is a firm with broad experience on the subject of Information Technology, Technology and Telecommunication and all matters encompassing it. If you have any questions or would like information on the issues discussed, please contact:**



**Tola Oshobi, SAN**

Partner

[toshobi@babalakinandco.com](mailto:toshobi@babalakinandco.com)



**Olawale Bamidele Adedipe**

Associate

[adedipe@babalakinandco.com](mailto:adedipe@babalakinandco.com)



**Christiana Nkechinyere Okechukwu**

Trainee Associate

[okechukwu@babalakinandco.com](mailto:okechukwu@babalakinandco.com)



**Oluwatobi Ogo-Oluwa Akinola**

Trainee Associate

[okinola@babalakinandco.com](mailto:okinola@babalakinandco.com)



**Afolabi Samuel Alawode**

Trainee Associate

[aalawode@babalakinandco.com](mailto:aalawode@babalakinandco.com)

## —OFFICE LOCATIONS—

### LAGOS OFFICE

1261A Adeola Hopewell Street  
Victoria Island, Lagos State.  
(+234)2012718700, 2718806, 2718808,  
2718711, 27188004, (+234)2702802

### ABUJA OFFICE

4, River Benue Street,  
Off Ibrahim Babangida Boulevard,  
Maitama District, Abuja.  
(+234) 9-2780930, 2780933-9

### PORT HARCOURT OFFICE

3, Williams Jumbo Street,  
Old GRA, Port Harcourt  
Rivers State.  
(+234)703506876