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**STRENGTHENING THE LEGAL AND REGULATORY FRAMEWORK FOR  
DERIVATIVES CONTRACTS IN NIGERIA**

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**ABSTRACT**

*In recent years, derivatives have emerged as indispensable financial instruments for risk management, price discovery, and speculative investment within global financial markets. In Nigeria, however, the development and utilisation of derivatives remain emergent, presenting both significant opportunities and regulatory challenges. This paper examines the extant legal and institutional framework governing derivatives transactions in Nigeria, with particular emphasis on the regulatory roles of the Securities and Exchange Commission (SEC) and the Central Bank of Nigeria (CBN). Employing a doctrinal legal research methodology, the paper interrogates the adequacy, coherence, and enforcement of current legal instruments, identifies regulatory gaps, and examines the compatibility of Nigeria's framework with international legal standards and best practices. It finds that the Nigerian financial system stands to benefit immensely from a robust derivatives market, particularly in enhancing financial stability, deepening capital markets, and facilitating economic diversification. However, these are contingent upon the establishment of a comprehensive legal regime, an effective supervisory architecture, and sustained capacity-building initiatives for judicial officers, regulators, and legal practitioners. There is also a need for a more coordinated framework between the SEC, CBN, NGX, and FMDQ to reduce regulatory overlap and provide clear guidance to market participants. These steps will help build trust in the market and attract more investment in the future.*

## 1.1 Introduction

Derivatives contracts have become increasingly significant within the global financial system. The term “derivative” refers to a type of financial contract whose value is dependent on an underlying asset, a group of assets, or a benchmark.<sup>171</sup> Derivatives were originally used to ensure balanced exchange rates for internationally traded goods. International traders needed a system to account for the differing values of national currencies.<sup>172</sup> They have evolved into foundational instruments within the global financial system, underpinned by sophisticated regulatory frameworks and contractual standards. The widespread adoption of standardised documentation, most notably that developed by the International Swaps and Derivatives Association (ISDA), has significantly enhanced legal certainty, enforceability, and market predictability.<sup>173</sup>

In Nigeria, the gradual evolution of financial markets has necessitated the development of sophisticated instruments for risk hedging, speculation, and arbitrage. Thus, derivatives provide investors with the opportunity to manage exposures to interest rates, foreign exchange, equities, and commodities.<sup>174</sup> Although derivatives trading in Nigeria is developing compared to mature economies, its regulation has become critical due to the systemic risk that uncontrolled derivatives trading can introduce. This regulation has advanced alongside the market itself. Hence, the initiation of derivatives trading has enabled investors to manage risks better and diversify their portfolios. It has also attracted more foreign investors and increased market liquidity. A clear sign of this growth is the rise in foreign exchange derivatives traded on the FMDQ platform from ₦6.5 trillion in 2014 to ₦28.7 trillion in 2021, representing a 342% increase. This highlights the increasing importance of derivatives in Nigeria’s financial system. In the period from January to May 2024, the turnover for FX derivatives was ₦14,462,105 million (approximately \$9,313 million), according to FMDQ.<sup>175</sup>

When properly used, derivatives help manage risk and improve economic efficiency. However, some cases have shown that when misused, they can cause significant financial harm. Their complexity often leads to misunderstanding and, at times, has been used by dishonest promoters to take advantage of uninformed investors.<sup>176</sup>

The paper examines the development of derivatives contracts in Nigeria and critically evaluates the legal and regulatory framework that governs them. It focuses on the key statutory

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<sup>171</sup> Fernando, J. (2023), “Derivatives: Types, Considerations, and Pros and Cons,” Accessed at <https://www.investopedia.com/terms/d/derivative.asp> 12/6/2025

<sup>172</sup> Ibid.

<sup>173</sup> Ramos-Munoz, D. (2025). “The Validity of Derivatives Contracts: Legal Doctrine as a Vehicle of Dialogues on ‘Speculation’.” *European Business Organization Law Review*. <https://doi.org/10.1007/s40804-025-00345-w>

<sup>174</sup> Ogebe, E. (2025), “Derivatives in Nigerian Financial Markets: Risk Management, Growth, Challenges and Opportunities” Accessed at: [https://medium.com/@emmanuelogebe\\_1/derivatives-in-nigerian-financial-markets-risk-management-growth-challenges-and-opportunities-844e2ce0a76d#:~:text=Speculation%20and%20Investment%20Opportunities,commodity%20markets%20without%20physical%20ownership](https://medium.com/@emmanuelogebe_1/derivatives-in-nigerian-financial-markets-risk-management-growth-challenges-and-opportunities-844e2ce0a76d#:~:text=Speculation%20and%20Investment%20Opportunities,commodity%20markets%20without%20physical%20ownership) on 2/7/2025

<sup>175</sup> FMDQ Group. (2025). *FMDQ Exchange market turnover: January – May 2025 market turnover report*. <https://fmdqgroup.com/exchange/market-turnover/>

<sup>176</sup> Finnerty, J. D., and Pathak, K. (2011). A review of recent derivatives litigation. *Fordham Journal of Corporate & Financial Law*, 16(1), p.74. Accessed at: <https://ir.lawnet.fordham.edu/jcfl/vol16/iss1/2> on 2/7/2025

provisions, regulatory institutions, and judicial interpretations shaping derivatives transactions. The analysis considers how well the current framework accommodates these financial instruments in light of Nigeria's economic realities and compares it with international best practices. The paper also examines the roles of institutional actors, such as the Securities and Exchange Commission (SEC), the Central Bank of Nigeria (CBN), and central counterparties, and highlights the challenges hindering market growth. Ultimately, it highlights current legal and regulatory gaps and proposes targeted reforms to strengthen Nigeria's derivatives regime and support its integration into the global financial system.

## 1.2 Methodology

This study adopts a doctrinal research methodology, relying on the analysis of statutes, regulatory instruments, judicial decisions, and standard contractual frameworks governing derivatives in Nigeria, including the Investments and Securities Act 2007, SEC Rules, CBN Guidelines, and ISDA documentation. The research is analytical and comparative, drawing limited insights from selected foreign jurisdictions to evaluate the adequacy of Nigeria's regulatory framework.

The study is limited by its library-based nature, as it does not incorporate empirical data. In addition, the paucity of Nigerian judicial precedent on derivatives necessitates reliance on general contract principles and relevant foreign authorities, while the comparative analysis is confined to contextual guidance rather than exhaustive international evaluation.

## 1.3 Nature of Derivatives Contract

According to the International Monetary Fund, "derivatives are financial instruments that are linked to a specific financial instrument or indicator, or commodity."<sup>177</sup> Through which specific financial risks can be traded in financial markets in their own right. Transactions in financial derivatives are normally treated as separate transactions rather than as integral parts of the value of underlying transactions to which they may be linked. This is because derivatives are financial tools that get their value from something else, like a stock, currency, or interest rate. People and companies use them to manage risk or to try to make a profit. Some use derivatives to protect themselves from losses through hedging, while others use them to take risks and earn money through speculation. In simple terms, derivatives help move risk from those who do not want it to those who are willing to take it, for a price.<sup>178</sup>

Thus, the value is derived from the future price of an underlying asset, such as a commodity, currency, interest rate, or security. The contract locks in a specific strike price for the asset, protecting the parties from price fluctuations until a settlement date. They are typically

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<sup>177</sup> International Monetary Fund. (n.d.). *Financial derivatives*. Retrieved July 6, 2025, from <https://www.imf.org/external/np/sta/fd/index.htm>

<sup>178</sup> Finnerty stated that financial derivatives could be defined as financial instruments linked to a specific financial instrument or commodity, through which specific financial risk can be traded in the financial market. Finnerty, J. D., and Pathak, K., Op. Cit. p.75. See also, Osayi, V.I., Kasimu, A. and Nkwonta, H.C. (2018) "Financial Market Derivatives and the Performance of Deposit Money Banks in Nigeria." *International Journal of Economics, Commerce and Management*, 6, 382-396.

considered a form of advanced investing.<sup>179</sup> Parties usually take opposing positions on the future behaviour of an underlying asset, effectively placing financial “bets” on its movement.<sup>180</sup>

The settlement of a derivative contract may be cash-settled, where the difference between the strike price and the market price is paid in cash; or physically settled, where the underlying asset is delivered to the buyer in exchange for the strike price.

Derivative contracts allow market participants to profit from expected price changes in assets they do not directly own. One party (the long position) expects prices to rise, while the other (the short position) expects prices to fall. These contracts can be settled in cash or by physically delivering the asset. In a cash-settled derivative, if the price goes up, the short party pays the long party; if the price goes down, the long party pays the short party. This setup lets both sides benefit or lose based on how the market moves, without owning the actual asset.<sup>181</sup>

Derivatives were originally used to ensure balanced exchange rates for internationally traded goods. International traders needed a system to account for the differing values of national currencies.<sup>182</sup> Financial derivatives are more complex than stocks or bonds, making them harder to understand and value. Because they allow investors to take on leveraged risk, they can lead to large gains, but also significant losses, especially during times of market volatility.<sup>183</sup>

Although derivative instruments vary widely in design, they share certain fundamental features:

- (i) Underlying Asset: The basis upon which the contract derives its value. Examples include crude oil, equities, currencies, or interest rates.
- (ii) Expiration or Maturity Date: The future date on which the contractual obligations become due.
- (iii) Strike Price: The agreed-upon price at which the underlying asset will be bought or sold. This locked price, known as the strike price, is the value reference or consideration upon which the contract will be settled, and the underlying asset will be transferred to the buyer on the settlement date.
- (iv) Settlement Method: Can be either physical delivery of the asset or cash settlement based on the market value difference.
- (v) Counterparties: The transacting parties in the derivative contract, who may be exposed to performance and credit risk.

These features influence the legal rights and obligations of the parties involved and determine the enforceability of the contract under Nigerian law.<sup>184</sup>

These contracts are not without disadvantages. First, they are difficult to value because their price depends on the value of an underlying asset, which is often volatile. Second, there

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<sup>179</sup> Fernando, J., Op. Cit.

<sup>180</sup> Ramos-Munoz, D. Op. Cit., p.3

<sup>181</sup> Aluko & Oyebo. (2024). “An Overview of the Trading and Settlement of Derivative Contracts in Nigeria” p.1. Retrieved from: <https://www.aluko-oyebode.com/insights/an-overview-of-the-trading-and-settlement-of-derivative-contracts-in-nigeria/> on 15/6/2025

<sup>182</sup> Fernando, J., Op. Cit.

<sup>183</sup> Finnerty, J. D., and Pathak, K., Op. Cit., pp. 121-122

<sup>184</sup> Aluko and Oyebo, Op. Cit., p.1

is counterparty risk in OTC transactions, where one party may default on the contract. Third, derivatives are highly sensitive to various factors such as time to expiration, interest rates, and the cost of holding the underlying asset. Fourth, since derivatives lack intrinsic value, their prices can be heavily influenced by market sentiment, speculation, and demand rather than the actual performance of the asset. Lastly, derivatives often involve leverage, which means that small movements in the underlying asset can lead to significant gains or substantial losses.<sup>185</sup>

### **1.3 Classification and Features of Derivatives**

Derivatives can be classified using several criteria, including the nature of trading platforms, the type of underlying asset, and the structure of the contract. The primary classification in the Nigerian context, as globally, distinguishes between Over-the-Counter (OTC) Derivatives and Exchange-Traded Derivatives (ETDs).

#### **1.3.1 Over-the-Counter (OTC) Derivatives**

An over-the-counter (OTC) derivative is a privately negotiated and customised derivative contract that is structured according to the requirements of the contracting parties. The contracting parties do not go through any intermediary or exchange, and thus, each party takes on the counterparty's credit risk by entering into the contract. To hedge this risk, the investor could purchase a currency derivative to lock in a specific exchange rate. Derivatives that could be used to hedge this kind of risk include currency futures and currency swaps.<sup>186</sup>

OTCs are often tailored to meet specific needs, allowing for contract flexibility, including the tailoring of size, maturity, and underlying assets to suit specific needs. Unlike exchange-traded derivatives, OTC contracts are not publicly listed, which means there is no central clearinghouse to guarantee performance. This lack of transparency introduces credit risk, that one party may default, and operational risk from errors in managing the rights and obligations under the contract, especially when proper monitoring is lacking.<sup>187</sup> As a result, they also present a greater lack of transparency and limited regulatory oversight.

Banks and institutional investors predominantly use OTC derivatives. ISDA Master Agreements often govern transactions and are subject to foreign laws, particularly English law. The CBN regulates OTC derivatives involving banks through various guidelines.<sup>188</sup>

One of the primary concerns in Nigeria is the enforceability of OTC derivatives, especially where the contracts are governed by foreign law. Nigerian courts generally uphold such contracts provided they are not illegal or contrary to public policy. The principle of freedom of contract

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<sup>185</sup> Fernando, J., Op. Cit.

<sup>186</sup> Ibid.

<sup>187</sup> Parker, E., and Perzanowski, M. (2023). "Practical Derivatives: A transactional Approach" (4th ed.). *Globe Law and Business Limited*, p.11.

<sup>188</sup> Including the Guidelines for FX Derivatives in the Nigerian Financial Market (2011) and the Revised Foreign Exchange Manual (2018)

allows parties to choose the law governing their transactions.<sup>189</sup> However, enforceability can be affected by regulatory breaches, such as entering into derivatives without required authorisations or in violation of the Investments and Securities Act (ISA) or CBN Guidelines. Courts may also decline enforcement if the contract amounts to gambling or speculative activity without an underlying economic purpose, potentially invoking the Gaming and Lotteries Laws of various states.<sup>190</sup>

### 1.3.2 Exchange-Traded Derivatives (ETDs)

Exchange-traded derivatives are standardised derivative contracts entered into through an exchange, which acts as an intermediary between the parties. The Exchange's clearing house acts as the central counterparty and takes on a limited credit risk from each counterparty. As exchanges are regulated entities, parties trading exchange-traded derivatives are usually registered members licensed to trade on the exchanges.

ETDs are traded on organised exchanges such as the NGX or FMDQ Securities Exchange. These include futures and standardised options. The central counterparty (CCP) clearing model is used, where the clearing house interposes itself between buyers and sellers, reducing credit risk.

ETDs promote transparency, liquidity, and investor protection. They are subject to the regulations of the SEC and the trading rules of the respective exchange. In 2021, NGX launched its derivatives market, offering products such as equity index futures and single-stock futures. In Nigeria's derivatives market, clearing and settlement are essential post-trade processes that ensure contractual obligations are honoured and systemic risk is minimised. Clearing involves verifying trade details, managing counterparty risk, and ensuring that both parties can perform their obligations, while settlement refers to the actual exchange of funds, securities, or commodities on the agreed date.

### 1.4 Types of Derivatives Contracts

Derivative products are broadly classified into "lock" and "option" contracts. Lock derivatives, such as futures, forwards, and swaps, bind both parties to the terms of the contract from the beginning until it expires. They are obligatory and must be executed as agreed. Option derivatives, like stock options, give the holder the right but not the obligation to buy or sell the underlying asset at a specific price on or before a set date. The most common derivatives used in financial markets include futures, forwards, swaps, and options.<sup>191</sup> They are considered the four basic building blocks of derivative instruments.<sup>192</sup>

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<sup>189</sup> Itumo, T. M. (2023). "Analysing Nigeria's Choice of Law Regime for Cross-Border Contracts." *Law Pavilion*. Retrieved from: <https://lawpavilion.com/blog/analysing-nigerias-choice-of-law-regime-for-cross-border-contracts/> on 12/6/2025

<sup>190</sup> Ramos-Munoz, D. Op. Cit., p.3

<sup>191</sup> Fernando, J., Op. Cit.

<sup>192</sup> Smithson, C. W., Smith, C. W., Jr., & Wilford, D. S. (1995). *Managing Financial Risk: A Guide to Derivative Products, Financial Engineering, and Value Maximization*, Richard D. Irwin, Inc., p. 42

### 1.4.1 Forwards

These are customised OTC contracts obligating the purchase and sale of an asset at a future date at a predetermined price. Parties bear counterparty risk. This derivative is basically a contract between two parties to buy or sell a specific asset at a set price on a future date. All terms, such as the price, amount, and date, are agreed upon when the contract is made. These contracts help both parties avoid price uncertainty by locking in a price ahead of time.

Forwards are usually used for commodities or currencies and are mostly traded privately, allowing them to be customised to fit the needs of the parties involved. At maturity, the buyer gains if the market price is higher than the agreed price, while the seller gains if the market price is lower.<sup>193</sup>

### 1.4.2 Futures

Futures derivatives are standardised exchange-traded contracts where parties agree to buy and sell at a specified price and future date. For instance, in Nigeria, the NGX facilitates such trades. A futures contract is similar to a forward contract, but it is standardised and traded on an exchange. It was developed in the 1860s to reduce the risk of one party defaulting, which was a common problem with forward contracts.

Futures contracts are guaranteed by a clearinghouse that stands between the buyer and seller, marks positions to market daily, and requires collateral from the losing side each day.<sup>194</sup> This makes futures more secure and liquid than forwards, but also less flexible since they cannot be customised. In some legal disputes, such as *Olympic Natural Gas Co. vs Morgan Stanley Capital Group Inc.*,<sup>195</sup> the distinction between futures, forwards, and other contracts has been a key issue. The court held that the natural gas transactions at issue were forward contracts, not ordinary supply contracts, and thus, payments made under them were protected “settlement payments” made by a “forward contract merchant,” rendering them immune from avoidance in bankruptcy proceedings.

### 1.4.3 Options

An option contract gives the holder the right, but not the obligation, to buy (call option) or sell (put option) an asset at a set price (strike price) on or before a specific date. Options are used for both hedging and speculation. A call option is profitable if the market price is above the strike price at exercise, while a put option is, if the market price is below the strike price. If exercising the option would not result in a profit, it is considered “out-of-the-money” and may expire worthless. The option’s intrinsic value is the immediate gain from exercising it, while its time value reflects the potential for favourable price changes before expiration. The longer the time to expiration, the greater the time value, due to more chances for profitable price movements.<sup>196</sup>

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<sup>193</sup> Finnerty, J. D., and Pathak, K., Op. Cit., p.77

<sup>194</sup> Ibid., p.78

<sup>195</sup> US Court of Appeals for the Fifth Circuit - 294 F.3d 737 (5th Cir. 2002). Retrieved from: <https://law.justia.com/cases/federal/appellate-courts/F3/294/737/545795/> on 2/4/2025

<sup>196</sup> Finnerty, J. D., and Pathak, K., Op. Cit., p.79

There are two types of options: a call option (right to buy) and a put option (right to sell). Call options appeal to investors who expect prices to rise. For a small premium, they gain the chance of a much larger profit if the asset's price goes up; This potential is called leverage. Put options are useful when investors expect prices to fall. They act like insurance, guaranteeing a minimum return even if the asset's value drops sharply.<sup>197</sup> A good example is car insurance, which works like a put option - if your car is wrecked, you can "sell" it to the insurer for the insured value.

#### **1.4.4 Swaps**

Swaps are private agreements to exchange cash flows or liabilities; for example, currency swaps or interest rate swaps. These contracts are widely used by banks and institutional investors. They are agreements where two parties exchange payment obligations based on interest rates or currencies; commonly, one party pays a fixed rate while the other pays a floating rate. They help businesses and investors manage risk, such as protecting against rising interest rates or currency fluctuations, without changing the underlying loan or investment.<sup>198</sup>

Thus, swaps play a vital role in financial risk management by allowing parties to hedge interest rate and currency risks without altering underlying assets, reflecting their importance in modern financial systems.

### **1.5 The Legal Foundations of Derivatives in Nigeria**

The legal framework governing derivatives in Nigeria is rooted in a combination of statutory provisions, regulatory guidelines, and contractual norms, supplemented by common law principles. This hybrid structure reflects Nigeria's evolving financial system, where local legal developments coexist with international best practices, particularly in the context of Over-the-Counter (OTC) contracts. It has always been understood that laws that unequivocally recognise derivatives as legitimate financial instruments and grant regulatory agencies broad, flexible powers to enforce compliance and respond to evolving market dynamics. The law must normally empower regulatory authorities to establish, monitor, and enforce comprehensive rules that govern derivatives markets effectively.<sup>199</sup> Effective regulation is essential for market confidence, risk mitigation, and systemic stability, key to Nigeria's financial development aspirations. All successful derivatives markets operate under some form of government regulation, and that regulation plays a crucial role in maintaining market integrity, financial safety, and customer protection.<sup>200</sup>

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<sup>197</sup> Ibid., p. 80

<sup>198</sup> Ibid., p.83

<sup>199</sup>International Organization of Securities Commissions, Emerging Markets Committee of the International Organization of Securities Commissions. (1996). *"Legal and Regulatory Framework for Exchange Traded Derivatives"*, p. 4.

<sup>200</sup> Ibid., p.2

## **1.5.1 Statutory and Regulatory Instruments**

### **(a) Investments and Securities Act (ISA), 2007**

The ISA is the principal legislation regulating securities transactions in Nigeria. Section 315 defines “securities” to include “options, futures, forwards, swaps, and other derivatives.”<sup>201</sup> The ISA designates the SEC<sup>202</sup> as the apex regulatory body for Nigeria’s capital market. It empowers the Commission to regulate investment and securities businesses, including registering and supervising securities exchanges, capital trade points, derivatives, futures, commodities, and other recognised investment exchanges.<sup>203</sup>

The law grants the ISA authority to create rules and guidelines for overseeing market operations. Accordingly, the clearing of derivatives must adhere to the provisions of the ISA, the SEC Rules, and the rules of the relevant CCP. In 2019, the Securities and Exchange Commission (SEC) established a formal regulatory framework for derivatives trading in Nigeria through two main sets of rules. The first, the Derivatives Trading Rules, outlines requirements for exchange-traded and OTC derivatives, including standards for risk management and operational procedures for derivatives exchanges. The second, the Central Clearing Counterparty (CCP) Rules, sets the legal and operational foundations for the registration and operation of CCPs in Nigeria.

### **(b) SEC Rules on Regulation of Derivatives Trading (2020)**

In response to market evolution, the Commission issued dedicated Rules on Derivatives Trading in 2020. These rules provide the framework for licensing, risk management, margining, and disclosure obligations for entities engaging in derivatives. They mandate central clearing through a Central Counterparty (CCP) and stipulate capital adequacy and operational requirements for participants.

Under these rules, all derivative contracts must be registered and approved by the SEC before being introduced on an exchange. Only entities registered with a recognised exchange or CCP are permitted to trade exchange-traded derivatives, and only CBN-licensed commercial or merchant banks may act as derivatives clearing members.

Generally, the Rules provide a structured regulatory framework that defines key participants like exchanges and central counterparties, sets operational standards, and mandates risk controls to support market development. While focusing on exchange-traded derivatives, the Rules highlight the need for additional regulation of the riskier OTC derivatives segment.<sup>204</sup>

### **(c) SEC Rules on Central Counterparty (CCP Rules)**

These rules, also issued in 2020, regulate the activities of clearinghouses involved in derivatives markets. The rules emphasise the importance of mitigating counterparty risk, increasing

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<sup>201</sup> Investment and Securities Act (ISA), 2007.

<sup>202</sup> Henceforth, The Commission.

<sup>203</sup> Section 13 (a) and (b), ISA, 2007

<sup>204</sup> Williams, N., and Adetuyi, A. (2020, March 16). "Derivatives Trading in Nigeria: The New SEC Rules Amendment." Brooks & Knights. Retrieved from: <https://brooksandknights.com/wp-content/uploads/2020/03/Derivatives-Trading-in-Nigeria-The-New-SEC-Rules-Amendment.pdf> on 5/5/2025

transparency, and ensuring effective governance of clearing institutions. The Rules provide for the participants in the derivatives trading markets. Under the Rules, no person shall trade on exchange-traded derivatives for proprietary or client accounts except that they are registered with a recognized exchange and/ or a CCP as a dealing member or a derivative clearing member.<sup>205</sup> Only CBN-licensed commercial and merchant banks are eligible to register as derivatives clearing members under the Rules.<sup>206</sup>

The SEC Rules provide that any person who violates the Derivatives Trading Rules is liable to a penalty of not less than ₦1 million, with an additional fine of up to ₦25,000 for each day the violation continues.<sup>207</sup> Following the SEC's issuance of the Derivatives Trading Rules and CCP Rules, the Nigerian derivatives market witnessed significant institutional developments. Notably, NG Clearing Limited was successfully registered as a central clearing counterparty, and the NGX secured SEC approval for seven exchange-traded derivative contracts, marking a major milestone in the formalisation and expansion of Nigeria's derivatives market.

#### **(d) Central Bank of Nigeria (CBN) Guidelines**

The regulation of derivatives trading by banks and other financial institutions (OFIs) in Nigeria is primarily anchored in the CBN's broader financial sector reform agenda, which seeks to deepen the financial markets and enhance systemic stability. Central to this regulatory architecture are instruments such as the Guidelines for FX Derivatives in the Nigerian Financial Markets (2011),<sup>208</sup> the Revised Guidelines for the Operation of the Nigerian Inter-Bank Foreign Exchange Market, and the Revised Foreign Exchange Manual (2018).<sup>209</sup> Collectively, these instruments provide the operational and legal framework for the use of derivative products by authorised financial institutions, specifying permissible instruments such as FX forwards, swaps, cross-currency interest rate swaps, and European-style FX options. By delineating the eligibility requirements, trade execution protocols, and documentation standards, these guidelines serve to institutionalise FX risk management practices among market participants. The regulatory emphasis on derivative use as a hedging mechanism aligns with global financial norms and reflects the CBN's commitment to fostering liquidity, transparency, and resilience within the Nigerian financial system.<sup>210</sup>

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<sup>205</sup> Rule 7(1) of the Derivatives Trading Rules.

<sup>206</sup> Rule 4 of the Derivatives Trading Rules.

<sup>207</sup> Sanctions, Derivatives Trading Rules.

<sup>208</sup> Central Bank of Nigeria. (2011, March). "Guidelines for FX Derivatives in the Nigerian Financial Markets." Retrieved from:

<https://www.cbn.gov.ng/OUT/2011/CIRCULARS/FMD/GUIDELINES%20FOR%20FOREIGN%20EXCHANGE%20DERIVATIVES%20IN%20THE%20NIGERIAN%20FINANCIAL%20MARKETS.PDF> on 17/5/2025

<sup>209</sup> Central Bank of Nigeria. (2016, June). "Revised Guidelines for the Operation of the Nigerian Inter-Bank Foreign Exchange Market." Retrieved from: <https://www.cbn.gov.ng/out/2016/ccd/revised%20guidelines%20for%20flexible%20exchange%20rate%20market%202016%20v1.pdf> on 17/5/2025

<sup>210</sup> Ikevude, A., Oguiche, F., and Oyekan, O. (n.d.). "The Nigerian Financial Services Industry: An Overview." G. Elias & Co. Retrieved from: [https://www.gelias.com/images/Newsletter/Financial\\_Services\\_Regulation.pdf](https://www.gelias.com/images/Newsletter/Financial_Services_Regulation.pdf) on 2/7/2025

Complementing the CBN's regulatory efforts is the role of the FMDQ Exchange, which, as a key financial market infrastructure entity and self-regulatory organisation, has developed a suite of operational frameworks to facilitate the practical application of derivative instruments in the Nigerian market. The Market Operational Standards (2018)<sup>211</sup> and Market Framework Version 8 (2020)<sup>212</sup> are particularly instrumental in codifying market conduct principles, clearing and settlement procedures, and risk mitigation measures for exchange-traded derivatives, notably Naira Futures. These frameworks enhance the robustness of the regulatory regime by addressing critical vulnerabilities, including counterparty credit risk, market manipulation, and liquidity mismatches. In totality, the regulatory environment shaped by both the CBN and FMDQ Exchange constitutes a coherent, rules-based system that not only legitimizes the use of derivatives for financial risk management but also positions Nigeria's capital market within the broader context of global best practices in financial market regulation.<sup>213</sup>

#### **(e) International Swaps and Derivatives Association and Private Agreements**

For OTC derivatives, most Nigerian financial institutions adopt the International Swaps and Derivatives Association (ISDA) Master Agreement.<sup>214</sup> The 2002 agreement adds several new provisions, including: a new measure of damages provision, Close-out Amount, which replaces Market Quotation and Loss in the 1992 ISDA Master Agreements; a set-off provision,<sup>215</sup> *force majeure* termination event,<sup>216</sup> and consolidated interest and compensation provisions.<sup>217</sup> In addition, several provisions are amended, including a shortening of grace periods associated with some of the events of default.<sup>218</sup> Although ISDA documentation is governed by foreign law,<sup>219</sup> Nigerian courts have recognised such agreements as enforceable, provided that they do not violate Nigerian public policy. The choice of foreign law in such contracts is upheld by Nigerian courts where the selected law has a rational connection with the transaction.<sup>220</sup>

### **1.5.2 Judicial and Contractual Dimensions of Derivatives**

Although the engagement with derivatives contracts remains limited, most relevant decisions stem from general contract principles rather than derivatives-specific jurisprudence. Nigeria's legal

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<sup>211</sup> Central Bank of Nigeria. (2018). "OTC FX Futures Market Operational Standards." Retrieved from: [https://fmdqgroup.com/exchange/wpfd\\_file/otc-fx-futures-market-operational-standards-2018/](https://fmdqgroup.com/exchange/wpfd_file/otc-fx-futures-market-operational-standards-2018/) 16/5/2015

<sup>212</sup> Central Bank of Nigeria, Enhancing Financial Innovation and Access (EFInA), & Gender Subcommittee. (2020). "The Market Framework: Version 8." Retrieved from: [https://www.cbn.gov.ng/out/2020/dfd/framework%20for%20advancing%20women's%20financial%20inclusion%20in%20nigeria\\_final\\_5mb.pdf](https://www.cbn.gov.ng/out/2020/dfd/framework%20for%20advancing%20women's%20financial%20inclusion%20in%20nigeria_final_5mb.pdf) 16/5/2025

<sup>213</sup> Central Bank of Nigeria. (2021). "Guidelines for FX Derivatives in the Nigerian Financial Markets." Retrieved from

<sup>214</sup> International Swaps and Derivatives Association (ISDA). (2002). "ISDA Master Agreement." Retrieved from: <https://www.isda.org/book/2002-isda-master-agreement-mylibrary/> on 15/6/2025

<sup>215</sup> Section 6(f), *Ibid.*

<sup>216</sup> Section 5(b)(ii), *Ibid.*

<sup>217</sup> Section 9, *Ibid.*

<sup>218</sup> Section 5(a), *Ibid.*

<sup>219</sup> English or New York law

<sup>220</sup> see *Sonnar (Nig.) Ltd. v. Partenreedri M.S. Nordwind* (1987) 4 NWLR (Pt. 66) 520).

framework, being rooted in English common law, respects the freedom of contract principle. Thus, parties to a derivatives agreement are free to determine the terms of engagement, provided these terms do not contravene public policy or existing statutes. The courts will generally uphold such contracts unless they are tainted by fraud, illegality, or lack of capacity.

Parties to derivatives contracts often designate foreign law, especially English law, as the governing law and opt for foreign jurisdictions for dispute resolution. In *Sonnar (Nig.) Ltd. vs Partenreedri M.S. Nordwind*,<sup>221</sup> the Supreme Court of Nigeria held that Nigerian courts will recognise a foreign jurisdiction clause where the chosen forum has a connection with the contract. Essentially, while parties may include a foreign jurisdiction clause in their agreement, Nigerian courts will not automatically enforce it. If one party challenges the clause, arguing that litigating abroad would cause undue hardship or injustice, the court may retain jurisdiction. This ensures that even in cross-border derivatives contracts, access to justice and fairness can override strict adherence to party autonomy. However, in situations where a dispute involves Nigerian public policy, courts may assume jurisdiction notwithstanding the contractual choice. This is particularly true in cases involving regulatory violations, insolvency, or consumer protection. Derivatives contracts that are deemed contrary to public policy may be unenforceable in Nigeria. While speculative trading is not illegal *per se*, courts may scrutinise transactions that resemble wagering or gambling,<sup>222</sup> particularly if they involve synthetic or highly leveraged positions with no intent to take delivery of the underlying asset.<sup>223</sup>

Also, where the structure of a derivatives transaction is used to circumvent foreign exchange controls, tax laws, or prudential limits, courts may invalidate such contracts on grounds of illegality or fraud.<sup>224</sup> The Supreme Court in *Awojugbagbe Light Industries Ltd vs PN Chinukwe & Ors*<sup>47</sup>, *Alhaji Ayotunde Seriki vs Sefiu Olukorade*<sup>225</sup> it was held that no person involved in any immoral or illegal act or transaction should be allowed to come to court to seek redress. Such a contract invokes the common law maxim *ex turpi causa non oritur actio*, meaning that no action arises from a dishonourable or illegal cause.

While significant progress has been made in regulating derivatives in Nigeria, the legal framework is still developing. For instance, there is no derivatives-specific legislation akin to the United States' Dodd-Frank Act.<sup>226</sup> or the EMIR.<sup>227</sup> Existing laws are mostly fragmented across

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<sup>221</sup> (1987) 4 NWLR (Pt. 66) 520

<sup>222</sup> Nigerian courts have traditionally struck down contracts that amount to wagering, as seen in *Okagbue vs Okagbue* (1966) NMLR 197, where a contract deemed purely speculative and lacking an underlying commercial purpose was invalidated. This principle could influence the treatment of derivative contracts that resemble speculative bets.

<sup>223</sup> Akatugba, A. M. (2021). "Contemporary Judicial Attitudes of the Nigerian Courts Toward Contracts Tainted with Illegality." *Madonna University Nigeria Faculty of Law Journal*, p.7

<sup>224</sup> Central Bank of Nigeria. (2020). "CBN Rule Book Volume I: A Compendium of Policies and Regulations." Retrieved from: <https://www.cbn.gov.ng/out/2020/fmd/cbn%20rule%20book%20volume%201.pdf> on 2/6/2025

<sup>225</sup> (1999) 3 NWLR (Pt 595) 469 at 480 – 481

<sup>226</sup> United States Congress. (2010). "Dodd-Frank Wall Street Reform and Consumer Protection Act," Pub. L. No. 111–203, 124 Stat. 1376. Retrieved from <https://www.congress.gov/111/plaws/publ203/PLAW-111publ203.pdf> on 2/6/2025

<sup>227</sup> European Securities and Markets Authority, The European Market Infrastructure Regulation (EMIR). Retrieved from” [https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52\\_qa\\_on\\_emir\\_implementation.pdf](https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf) on 4/7/2025

multiple regulatory bodies, and there is a lack of judicial precedent specifically addressing derivatives disputes. Even in the United States, lawsuits often follow major losses in derivative investments, with investors claiming they were misled about the risks or profit potential. Fund managers may face allegations of breaching their fiduciary duty by using complex or risky derivatives, especially in the opaque over-the-counter market. The lack of transparent pricing and the novelty of some products can lead to fraud, misunderstandings, or poorly anticipated risks. Some investors are exploited due to unfamiliarity with these instruments, while others try to escape losses by exploiting contract loopholes. These disputes often end up in court when the financial stakes are high.<sup>228</sup>

Courts often struggle to balance the legal acceptance of derivatives with public concerns about speculation. While the markets and regulators support derivatives, many people still see them as risky or unfair. Judges must follow legal rules but also consider changing social views. If the law is too strict, it can cause problems; if it's flexible, it can adapt more easily. Courts also help the public understand which fears about speculation are reasonable under the law.<sup>229</sup>

Moreover, legal uncertainty persists around corporate authority to enter into derivatives, especially for public sector entities or corporations with restrictive constitutional documents. The issue of *ultra vires* contracts remains a legal risk if board or shareholder approval is not properly secured.

## **1.6 Institutional Regulation and Market Operators for Derivatives Trading**

The regulation and supervision of derivatives contracts in Nigeria involve a combination of governmental and private sector institutions. These bodies are charged with oversight, licensing, rule-making, clearing, and settlement responsibilities. Together, they shape the operational and legal environment for both exchange-traded and over-the-counter derivatives. There is a strong element of private ordering. The private ordering of derivatives has achieved greater certainty through the widespread use of standard documentation, primarily based on the ISDA model.<sup>230</sup> The lead regulator is the SEC, with the CBN playing a limited role in banks and other financial institutions. Self-regulatory organisations, such as securities exchanges, also play a crucial role in the regulation of the Nigerian derivatives markets. There is a nagging concern pertaining to the risk of potential conflicts and inefficiencies caused by fragmented regulatory structures, and the benefits of consolidating regulatory authority where practical.<sup>231</sup> The regulation of swaps and related derivatives involves multiple regulatory bodies, each with distinct mandates, making coordination necessary to address potential overlap and regulatory ambiguity within the financial system.

### **(a) Securities and Exchange Commission (SEC)**

The SEC is the apex regulatory body for Nigeria's capital market under the Investments and Securities Act (ISA), 2007. The SEC is empowered to license market participants, approve trading

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<sup>228</sup> Finnerty, J. D., and Pathak, K. Op. Cit., p. 122

<sup>229</sup> Ramos-Munoz, D. Op. Cit., p.12

<sup>230</sup> Ramos-Munoz, D. Op. Cit., p.2

<sup>231</sup> Emerging Markets Committee of the International Organization of Securities Commissions, Op. Cit.

platforms, and issue binding rules. The SEC Rules on Derivatives Trading and the Rules on Central Counterparties are core regulatory instruments through which the SEC governs derivatives activities.

The SEC ensures that derivatives contracts offered to the public or traded on exchanges meet disclosure, margining, and governance standards. It also reviews applications for new derivative products and monitors systemic risks arising from speculative activity.<sup>232</sup> The Derivatives Trading Rules require that a Derivatives Contract be registered with the SEC in the prescribed manner, and its approval granted before such contract is introduced on any exchange.<sup>233</sup>

However, the Commission is not without its constraints, such as limited technical capacity, fragmented oversight with other financial regulators, and an underdeveloped market infrastructure. These weaknesses hinder effective enforcement, real-time monitoring, and the growth of a transparent and resilient derivatives market.<sup>234</sup>

### **(b) Central Bank of Nigeria (CBN)**

The Central Bank of Nigeria (CBN) plays a critical role in regulating derivatives involving commercial and merchant banks, especially in the foreign exchange and fixed income markets. It issues prudential guidelines, risk management frameworks, and policy directives on acceptable instruments.<sup>235</sup> The CBN also serves as a liquidity provider in the interbank derivatives market and enforces monetary and macro-prudential policy through structured derivative instruments.<sup>236</sup>

The CBN faces legal and jurisdictional constraints in regulating derivatives, as existing laws such as the CBN Act 2007 and BOFIA 2020 do not expressly define or provide a comprehensive framework for derivative instruments, creating overlaps with the SEC.<sup>237</sup> And since Nigeria's derivative market is developing, and the CBN's regulatory efforts are hampered by limited technical capacity and a shortage of specialised expertise, as well.<sup>238</sup>

### **(c) Nigerian Exchange Limited (NGX)**

The Nigerian Exchange (NGX), formerly the Nigerian Stock Exchange (NSE), operates Nigeria's premier exchange for equity and derivatives trading. In 2021, the NGX launched its derivatives market with products such as equity index futures and single stock futures. It oversees the

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<sup>232</sup> Rule 6(3) of the Derivatives Trading Rules.

<sup>233</sup> Rule 3(1) and (2) of the Derivatives Trading Rules.

<sup>234</sup> International Monetary Fund, (2019) "Financial Sector Stability Assessment (FSSA)". Retrieved from: <https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Nigeria-Financial-Sector-Stability-Assessment-40576> on 2/7/2025

<sup>235</sup> For example, the CBN Guidelines for FX Derivatives (2011) and the Revised Foreign Exchange Manual (2018) regulate Naira-settled forwards and futures, a major innovation in Nigeria's risk management regime, as discussed under the previous section.

<sup>236</sup> Central Bank of Nigeria, Understanding Monetary Policy Series 4, Liquidity Management, 2021. Retrieved from: <https://www.cbn.gov.ng/Out/2022/MPD/Series%204.pdf> on 2/7/2025

<sup>237</sup> Sections 2-6, CBN Act, Rule 96, SEC Rules 2013.

<sup>238</sup> CBN, Financial Stability Report, June 2023, pp. 56–58. Retrieved from: <https://www.cbn.gov.ng/Out/2024/FPRD/JUNE%202023%20FSR%20-%20FINAL.pdf> on 17/5/2025

operations of trading members, enforces market conduct rules, and provides a platform for price discovery and trade matching.<sup>239</sup>

The NGX operates through a regulatory subsidiary, NGX Regulation Limited (NGX RegCo),<sup>240</sup> which reviews applications for derivative licenses and conducts compliance audits. It works closely with the SEC to ensure the integrity of the trading environment. In August 2019, the SEC approved the Nigerian Exchange Limited (NGX) Rulebook on Derivatives Market,<sup>241</sup> which became effective on 14 April 2022. It applies to all the members and users of the NGX derivatives platform, setting out membership requirements (clearing and non-clearing), procedures for conducting trades, and general guidelines for the listing of derivative products on the NGX.

#### **(d) FMDQ Securities Exchange**

The FMDQ Group, through its subsidiary FMDQ Securities Exchange Limited,<sup>242</sup> facilitates OTC trading in fixed income and currency derivatives. It has been instrumental in the development of Naira-settled FX Futures, providing real-time quotes, post-trade reporting, and market data. FMDQ also provides central clearing services and has pioneered efforts to deepen the OTC derivatives space. Further, FMDQ collaborates with the CBN and market participants to issue operational standards and product frameworks, such as the FMDQ Derivatives Market Framework.<sup>243</sup>

FMDQ introduced rules for the trading of derivatives on its platform in 2021, which were approved by the SEC, and its exchange-traded derivatives platform went live in July 2023.<sup>244</sup> Recent amendments to FMDQ's Derivatives Market Rules were approved by the SEC on 7 May 2024.<sup>245</sup> FMDQ Exchange is actively developing its exchange-traded derivatives (ETD) market, with a focus on capacity building through the training of market participants ahead of its formal

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<sup>239</sup> Nigerian Exchange Group (NGX Group) (2021). "Strengthening the Competitiveness of African Economies". Retrieved from:

[https://ngxgroup.com/launch-of-west-africas-first-exchange-traded-derivatives-receives-further-boost-as-sec-approves-7-ngxs-derivatives-contracts/#:~:text=Nigerian%20Exchange%20Limited%20\(NGX%20or,in%20accessing%20and%20using%20capital%20on%203/7/2025](https://ngxgroup.com/launch-of-west-africas-first-exchange-traded-derivatives-receives-further-boost-as-sec-approves-7-ngxs-derivatives-contracts/#:~:text=Nigerian%20Exchange%20Limited%20(NGX%20or,in%20accessing%20and%20using%20capital%20on%203/7/2025)

<sup>240</sup>Nigerian Exchange Group. (2025). "Protecting Investors and Supporting Healthy Capital Markets." Retrieved from [https://ngxgroup.com/regulation/#:~:text=NGX%20Regulation%20Limited%20\(NGX%20REGCO,Market%20Development](https://ngxgroup.com/regulation/#:~:text=NGX%20Regulation%20Limited%20(NGX%20REGCO,Market%20Development)

<sup>241</sup> Called the "Rule Book". See the Nigerian Stock Exchange. (n.d.). "Rulebook of the Nigerian Stock Exchange: Derivatives Market." Retrieved from: <https://ngxgroup.com/ngx-download/rulebook-of-the-nigerian-stock-exchange-derivatives-market-sec-approved-august-2019/?wpdmdl=28452&refresh=623db5788cbd81648211320> on 5/7/2025

<sup>242</sup>FMDQ Group. (n.d.). "Who We Are." Retrieved from <https://fmdqgroup.com/#:~:text=WHO%20WE%20ARE,an%20Information%20Technology%20Services%20Company>

<sup>243</sup> FMDQ Group. (2020). "FMDQ Derivatives Market Framework (Version 8)". See: <https://fmdqgroup.com/>

<sup>244</sup> <http://www.efaidnbmnnibpcajpcglclefindmkaj/https://fmdqgroup.com/wp-content/uploads/2021/03/SEC-Approved-FMDQ-Exchange-Derivatives-Market-Rules.pdf>

<sup>245</sup> FMDQ Group. (2025, May 9). "Sundry Amendments to FMDQ Exchange Derivatives Market Rules." Market Bulletin MB-47. Retrieved from: <https://fmdqgroup.com/exchange/market-bulletin/sundry-amendments-to-fmdq-exchange-derivatives-market-rules/> on 3/5/2025

launch. The upcoming FMDQ ETD market will offer a range of derivative products, fixed income, currency, equity, and commodity ETDs, each tied to relevant underlying assets.

**(e) NG Clearing Limited**

NG Clearing Limited<sup>246</sup> acts as the central counterparty clearing house (CCP) for derivatives traded on NGX and other exchanges. Its function is to mitigate counterparty risk by guaranteeing contract performance, managing margin calls, and ensuring settlement finality. By standing between counterparties in a transaction, NG Clearing ensures financial system stability and builds market confidence in derivatives contracts. It operates under the SEC's CCP Rules and must meet strict governance, capital, and risk management standards.

**(f) International Swaps and Derivatives Association (ISDA)**

The ISDA is a professional association that has been operating since 1985 as a global trade organisation that plays a central role in promoting the safe and efficient functioning of derivatives markets, and promotes and improves the trading of swaps and derivatives.<sup>247</sup> The ISDA is a private trade organisation whose members, mainly banks, transact in the OTC derivatives market. This association helps to improve the market for privately negotiated OTC derivatives by identifying and reducing risks in that market. Its core mission is to reduce counterparty risk, enhance market transparency, and strengthen the legal and operational infrastructure of global derivatives markets. Although not a Nigerian entity, the International Swaps and Derivatives Association (ISDA) plays a foundational role in the legal framework for OTC derivatives in Nigeria. Most Nigerian banks and institutional counterparties adopt the ISDA Master Agreement for swaps, forwards, and other non-standardized contracts. ISDA documentation introduces legal certainty, standardization, and netting provisions critical for risk mitigation.

The acceptance and oversight of speculation and derivatives, whether by self-regulatory or regulatory bodies, constitute a complex and evolving framework. Rather than offering a fixed solution, this framework reflects a network of interrelated and continually adapting ideas.<sup>248</sup> As such, regulatory authorities must be explicitly empowered by law to establish, monitor, and enforce comprehensive rules governing derivatives markets.<sup>249</sup>

Regulatory oversight of derivatives markets should focus on sound contract design, alignment with the cash market, safeguards against manipulation, effective clearing systems, and adequate capital and margin standards.<sup>250</sup> To keep markets stable and fair, it's important to carefully check how contracts are written, how margins are managed, and how trades are cleared. These steps help reduce the risk of default and system failures.

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<sup>246</sup> NG Clearing. (n.d.). "Clearing Services." Retrieved from: <https://www.ngclearing.com/services/clearing-services/> on 3/5/2025

<sup>247</sup> International Swaps and Derivatives Association (ISDA). (n.d.). "About ISDA." Retrieved from: <https://www.isda.org/about-isda/> on 5/5/2025

<sup>248</sup> Ramos-Munoz, D. Op. Cit., p.7

<sup>249</sup> Emerging Markets Committee of the International Organization of Securities Commissions, Op. Cit., p.4

<sup>250</sup> Ibid., pp. 8-9

## 1.7 Evolving Corporate Authority in Derivatives

Legal challenges may arise where one party lacks the corporate authority to enter into derivatives contracts. The English case *Hazell vs Hammersmith and Fulham London Borough Council*<sup>251</sup> underscores the critical importance of a counterparty's legal capacity in financial transactions. In this landmark decision, the UK House of Lords ruled that local London councils lacked statutory authority to engage in interest rate swaps, rendering such contracts void. This highlighted that even widely used financial instruments like derivatives are unenforceable if one party lacks legal power to enter the agreement, especially in the case of public bodies bound by enabling legislation.<sup>252</sup>

Nigerian law requires that companies act within the scope of their memorandum and articles of association. If a contract is entered into *ultra vires*, that is, beyond corporate powers, it may be declared void. Transactions outside a company's constitutional objects are invalid, even if entered in good faith.

However, the 2020 CAMA has significantly relaxed the *ultra vires* doctrine. While the doctrine aimed to protect investors and creditors, it also hindered corporate growth and third-party transactions. It validates *ultra vires* acts once executed and allows companies to engage in any business unless explicitly restricted by their Articles of Association.<sup>253</sup> This shift provides greater flexibility for companies but introduces potential complexities when interpreting the interplay between the Memorandum and Articles of Association regarding business objects.<sup>254</sup> In derivatives contracts, this may enhance legal certainty for counterparties but still requires due diligence to ensure compliance with internal corporate limits and sector-specific regulations.

## 1.8 Comparative Insights for Nigeria's Derivatives Reform

Examining the regulatory frameworks of developed financial markets provides useful insights for Nigeria's derivatives market development. Key lessons can be drawn from the United States, European Union, and South Africa, each of which has established comprehensive and sophisticated regimes for derivatives trading.

### 1.8.1 United States of America

Recent concerns highlight the systemic risks posed by derivatives, especially credit default swaps, which some blame for triggering the global financial crisis. Warren Buffett famously called

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<sup>251</sup> *Hazell v. Hammersmith & Fulham London Borough Council*, [1992] 2 A.C. 1 (H.L.). Retrieved from: [https://www.ato.gov.au/law/view/.../JUD/\\*1992\\*2AC1/00004](https://www.ato.gov.au/law/view/.../JUD/*1992*2AC1/00004) on 6/7/2025

<sup>252</sup> Raisler, K. (1997). "The Risks of Financial Derivatives," p. 477, Chapter 23B. International Monetary Fund. Retrieved from IMF eLibrary: <https://www.elibrary.imf.org/display/book/9781557755032/ch043.xml#:~:text=Related%20Publications-.Abstract,bank%20lending%20fixed%20rate%20mortgages> on 23/6/2025

<sup>253</sup> Sections 35 and 39(3) CAMA, 2020

<sup>254</sup> Abiona, A. D. (2020). "Ultra Vires Doctrine under the Nigerian Company Law: An Appraisal of the Companies and Allied Matters Act (CAMA)." Retrieved from: [https://www.academia.edu/64788226/ULTRA\\_VIRES\\_DOCTRINE\\_UNDER\\_THE\\_NIGERIAN\\_COMPANY\\_LAW\\_AN\\_APPRAISAL\\_OF\\_THE\\_COMPANIES\\_AND\\_ALLIED\\_MATTERS\\_ACT\\_CAMA\\_2020](https://www.academia.edu/64788226/ULTRA_VIRES_DOCTRINE_UNDER_THE_NIGERIAN_COMPANY_LAW_AN_APPRAISAL_OF_THE_COMPANIES_AND_ALLIED_MATTERS_ACT_CAMA_2020)

derivatives “financial weapons of mass destruction,” warning of their potential danger when misused.<sup>255</sup> In response to these risks, the United States Treasury enacted a regulatory regime aimed at increasing transparency, limiting speculative trading, and tightening oversight of derivatives market participants. They also amended the Commodity Exchange Act<sup>256</sup> and securities laws. These changes sought to curb market manipulation, fraud, and other abuses that threaten financial stability.<sup>257</sup>

Similarly, the Dodd-Frank Act<sup>258</sup> reformed the U.S. derivatives market by imposing stringent regulatory requirements. Key provisions include mandatory central clearing of standardised OTC derivatives, comprehensive trade reporting to regulators, and increased capital and margin requirements for market participants. The Act also enhanced the powers of the Commodity Futures Trading Commission (CFTC) and the United States Securities and Exchange Commission (SEC)<sup>259</sup> to oversee derivatives markets. This regulatory overhaul improved market transparency, reduced systemic risk, and strengthened investor protections. Nigeria can benefit from adopting similar mandates for central clearing and trade reporting to mitigate counterparty risks and enhance market integrity.

## 1.8.2 The European Market Infrastructure Regulation (EMIR)

EMIR requires that certain OTC derivatives be centrally cleared and reported to trade repositories to increase transparency and reduce counterparty credit risk. EMIR also mandates risk mitigation techniques for non-centrally cleared derivatives, including timely confirmation, portfolio reconciliation, and dispute resolution mechanisms.<sup>260</sup> The EU’s approach highlights the importance of a comprehensive regulatory infrastructure and robust supervisory coordination. Despite broad regulatory and contractual acceptance, European courts frequently face challenges to the validity and enforceability of derivatives. As David Ramos-Muñoz observes, regulation and market norms have not fully addressed deeper legal and societal concerns about speculation,

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<sup>255</sup> Annual Letter to Shareholders from Warren Buffett, Chairman, Berkshire Hathaway, Inc., Feb. 21, 2003, at 15, available at:

<http://www.berkshirehathaway.com/letters/2002pdf.pdf>. See also Paletta, D. (2010, April 27). “Democrats Deny Buffett on a Key Provision.” *The Wall Street Journal*. Retrieved from: <https://www.wsj.com/articles/SB10001424052748703465204575208030785525128> on 3/7/2025

<sup>256</sup>United States. Commodity Futures Trading Commission. (n.d.). *Commodity Exchange Act*. U.S. Government. Retrieved from <https://www.cftc.gov/PressRoom/MediaAdvisories/Pages/files/commodityexchangeact.pdf> 10/5/2025

<sup>257</sup> U.S. Department of the Treasury. (2009, May 13). “Regulatory Reform: Over-the-Counter (OTC) Derivatives.” [Press release]. Retrieved from <http://www.ustreas.gov/press/releases/tg129.htm> and Lynch, S. N., and Ng, S. (2009, May 14). “U.S. Moves to Regulate Derivatives Trade.” *The Wall Street Journal*, pp. C1, C3.

<sup>258</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act (2010). Retrieved from: <https://www.congress.gov/111/plaws/publ203/PLAW-111publ203.pdf> on 15/6/2025

<sup>259</sup> The United States Securities and Exchange Commission is an independent agency of the United States federal government, created in the aftermath of the Wall Street crash of 1929. Its primary purpose is to enforce laws against market manipulation. USA.gov. (n.d.). “Securities and Exchange Commission.” <https://www.usa.gov/agencies/securities-and-exchange-commission>

<sup>260</sup> European Securities and Markets Authority, *The European Market Infrastructure Regulation (EMIR)*, Op. Cit.

leaving courts without clear guidelines to distinguish between legitimate and illegitimate transactions.<sup>261</sup>

Nevertheless, the EMIR provides valuable lessons for Nigeria's developing derivatives market by emphasising transparency, risk mitigation, and regulatory oversight. Its key features, such as mandatory central clearing of standardised OTC contracts, trade reporting to repositories, collateral and risk management requirements for non-cleared trades, and tiered obligations for different categories of counterparties,<sup>262</sup> offer a framework that Nigeria can adapt. By adopting similar mechanisms through institutions like SEC Nigeria and FMDQ, the country can strengthen market infrastructure, reduce systemic risk, and align with global best practices to foster a secure and efficient derivatives ecosystem.

## 1.9 Findings

The paper specifically finds that, first, Nigeria currently lacks a consolidated, comprehensive statutory framework specifically tailored to derivatives. The existing legal regime is fragmented across the Investments and Securities Act (ISA), CBN Guidelines, SEC Rules, and foreign-governed ISDA contracts, creating regulatory uncertainty and limiting enforceability, especially for OTC contracts.

Secondly, there is a notable absence of Nigerian judicial precedent directly addressing derivatives disputes. Courts typically apply general contract law principles without tailored guidance. Simultaneously, many regulators, legal practitioners, and market operators lack the specialised expertise required to interpret, supervise, or litigate complex derivatives transactions.

Thirdly, oversight of Nigeria's derivatives market is divided among several institutions, the SEC, the CBN, and private ordering institutions such as NGX and FMDQ, with overlapping roles and uncoordinated rulemaking. This fragmentation fosters gaps, conflicting regulations, and inefficiencies in market supervision.

Fourthly, despite regulatory progress, Nigeria still lacks critical infrastructure such as widespread central clearing, real-time trade repositories, margining systems, and strong post-trade risk controls. The absence of these market-supporting systems exposes participants to heightened counterparty and systemic risk.

Consequently, the following recommendations are put forward:

1. Harmonisation of existing legal instruments to clarify enforceability standards, define the legal status of derivatives, and consolidate oversight mandates. This legislation should incorporate elements of the ISA, SEC Rules, and international best practices such as Dodd-Frank and EMIR, ensuring legal certainty and uniformity across the market.
2. Implement targeted legal capacity-building programmes for judges, regulators, and other practitioners. These should include CLE-certified courses, judicial colloquia, and collaborations with international organisations such as ISDA. Additionally, establish a

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<sup>261</sup> Ramos-Munoz, D. Op. Cit., p.2

<sup>262</sup> European Securities and Markets Authority, The European Market Infrastructure Regulation (EMIR), Op. Cit.

financial markets division within key commercial courts to handle derivatives-related matters.

3. Establish a coordination office through statutory or executive action. This inter-agency body should include representatives from all relevant regulators and be tasked with harmonising rulemaking, streamlining supervision, and issuing joint guidance. The office should be supported by a permanent secretariat and empowered to facilitate periodic reviews of derivatives market practices and reforms.
4. Mandate the expansion of central clearing infrastructure (e.g., NG Clearing Ltd and FMDQ Clear) and trade repositories for both OTC and exchange-traded derivatives. Regulators should require real-time transaction reporting, daily margining, and stress testing for market participants. Incentives should be introduced to encourage migration from bilateral to centrally cleared platforms.

### **1.10 Conclusion**

The paper examined the complex legal and regulatory architecture governing derivatives, emphasising the interplay between statutory enactments, regulatory oversight by institutions such as the SEC and CBN, and the adoption of international contractual frameworks like the ISDA Master Agreement. Unlike traditional investments like stocks, derivatives are mainly used to manage risk, not to grow wealth over time. They help businesses and investors protect themselves from losses by locking in prices for things like interest rates, currencies, or commodities, making them especially useful in uncertain markets. Nigeria's derivatives market holds immense potential for hedging and investment diversification. However, realising this potential requires strengthening the legal and institutional framework. With appropriate reforms and regulatory coordination, Nigeria can position itself as a hub for derivatives trading in Africa.