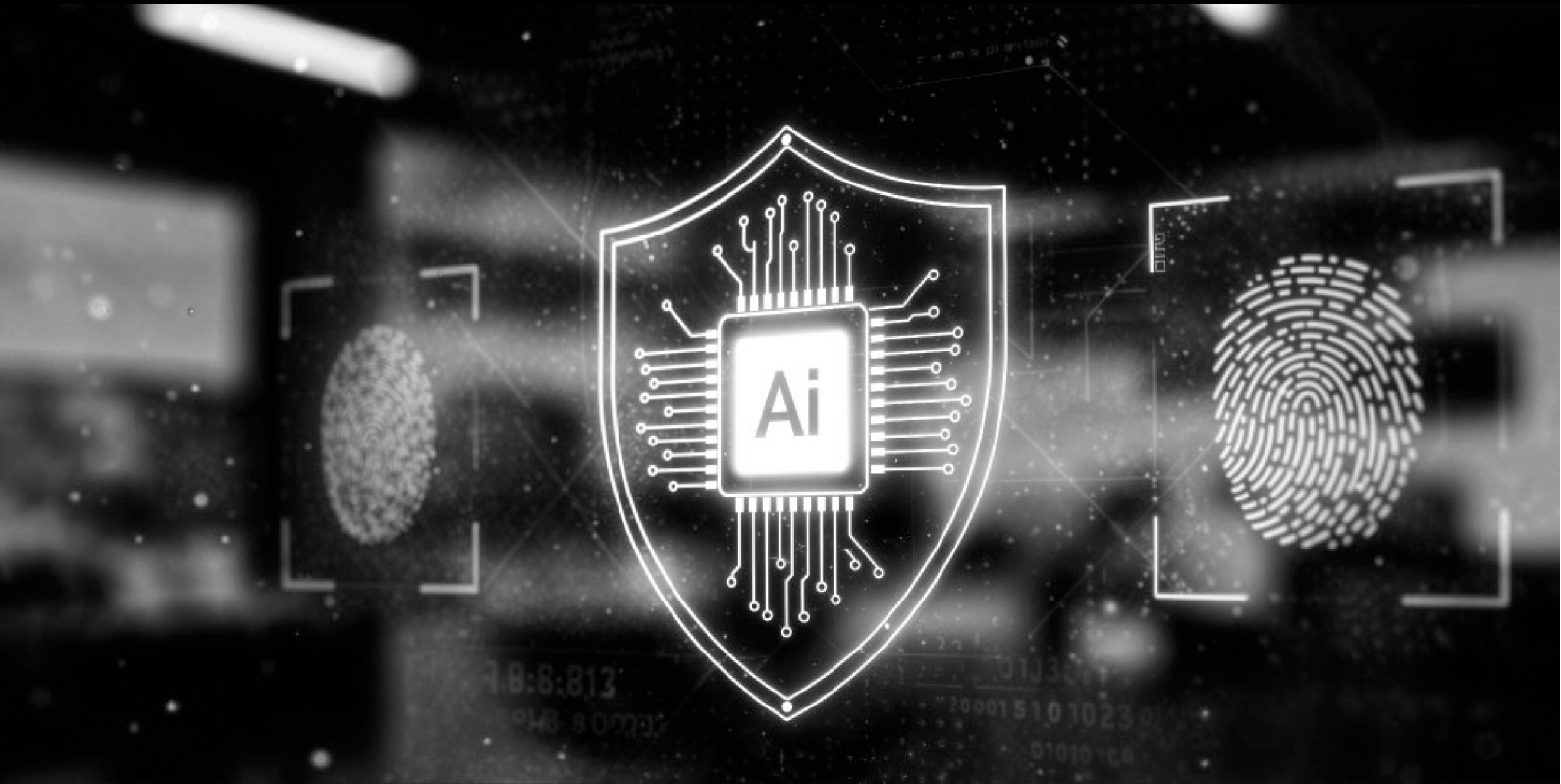




TECHNOLOGY & INNOVATION

Cracking Down or Catching Up? South Africa's Approach to Crypto Regulation: Part 1 – Payments

2 July 2025 7 min read

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Introduction

Crypto assets (“**crypto**”) exist in a unique regulatory space. Unlike traditional currency, crypto is not issued by central banks. Crypto can however be used in similar ways to traditional currency: they can be traded, used for payments, investing, security or capital raising.

No single law governs crypto in South Africa. Instead, regulation is fragmented across various laws, demanding that organisations understand this legal landscape.

This article is the first in a series on crypto regulation, and it maps the current regulation of crypto relating to payments. In the articles that follow, we will also discuss the regulation of crypto through anti-money laundering and counter terrorism laws, financial services laws, and exchange control.

Promise and peril: crypto assets as a form of payment

Many business want to know if they can accept crypto as a form of payment and what the related risks and processes are if they choose to do so. In this section, we focus on the use of crypto for retail payments. The emergence of crypto has provided an alternative means of payment to traditional low value payment systems (“**PS**”) that use government-issued FIAT currency (Rands in the case of South Africa), such as electronic funds transfers, debit card, credit card, real time clearing, and even cash.

The South African Reserve Bank (“**SARB**”) – who regulates and enforces South Africa’s national payment system (“**NPS**”) – does not however presently recognise crypto as a form of currency; crypto is neither “money” issued by the SARB; nor is it “e-money”, as only registered South African banks are able to issue e-money. This means that crypto as a means of payment is unregulated.

Risks and benefits of crypto as a form of payment

Using crypto as a means of payment has both risks and benefits. Crypto makes use of the distributed ledger technology (“**DLT**”) to verify and record transactions between crypto wallets. A crypto payment is therefore completely “peer-to-peer” between the payer (the customer) and payee’s (the retailer) crypto wallets. This is in contrast to a FIAT payment which needs to be (i) “cleared” (i.e. the exchange of payment instructions between banks); and (ii) “settled” (i.e. the discharge of payment obligations between banks in central bank assets). A traditional payment therefore requires a multitude of parties to function: this includes the issuing / payor bank and the acquiring / payee bank, but it also includes the other role players in the NPS, including the payment system operator (STRATE, BankServ, Visa, Mastercard), and the South African Multiple Option Settlement (“**SAMOS**”) operated by SARB. It may also include other payment services providers like system operators or third party payment providers if those are utilised.

The immutability of DLT means that crypto transactions are final and irreversible and can only be refunded by the receiving party. If a customer makes a mistake or their crypto wallet is used fraudulently by someone else, they will have no right of recourse. This is unlike card transactions which can be challenged on the basis of fraud and a charge back can be requested.

The lack of regulation and the fact that there are no intermediaries for crypto payments greatly reduces the costs associated with the conventional banking system. The converse is that this can create risks for users. The role players in the NPS referred to above are highly regulated and must comply with the requirements of the NPS, including applicable laws, directives issues by the SARB, the Payment Association of South Africa’s Constitution, card issuer rules, and other documents. This is not the case for crypto which is not issued by a central agency (like the SARB); and whereas crypto payments are otherwise unregulated. What this also means is that the usual charge back procedures, fraud prevention measures, and dispute resolution processes are not applicable to crypto payments, resulting in a lesser degree of consumer protection.

One of the main hallmarks of a traditional payment system is interoperability: different banks and their systems, applications, and infrastructure are able to communicate with each other. To put this in simple terms: even if I bank with FNB and a merchant banks with Standard Bank, by using the NPS, I am able to transact using my FNB card at a merchant and that transaction is cleared and settled between the banks in terms of the NPS.

Crypto eliminates single points of failure in the payment instruction and transaction itself: this makes intermediary error or failure impossible. Whereas traditional PSs include a risk of fraud or a role player in the payment chain making an error. Crypto however still carries with it a risk with regards to a person’s digital wallet as it stores their private keys. Crypto can also still be used for other fraudulent purposes like money laundering and financing terrorism.

Payment processes

Crypto is not a currency and it is not currently part of the NPS: it functions on a separate system: the blockchain. With crypto payments, a retailer has to accept the specific crypto coin (e.g. Bitcoin or Ethereum) that the consumer wants to use, and it must have its own crypto wallet with a crypto address that may be used for the transfer of that specific crypto coin. Pick ‘n Pay – for example – accepts payment in Bitcoin.

There is however an increasing popular alternative to accepting crypto directly, and this is where crypto is accepted through the use of a crypto wallet partnered with a mobile payment app or payment gateway / platform. The most widely used example of this is Luno's partnership with Zapper that allow crypto payments at over 31,000 Zapper merchants in the country, including Dischem and FlySafair.

How this works is that a customer using Luno can pay a merchant using crypto. Luno receives the cryptocurrency payment from the customer, and it then converts the crypto to the merchant's chosen fiat currency (e.g. ZAR) and settles the merchant's account. Zapper can be used for in-store and online purchases. This feature is particularly useful for merchants who want to accept crypto payments without dealing with the complexities of managing and converting the crypto themselves. It also helps to mitigate the volatility associated with crypto.

Luno has also partnered with Stich Pay to offer a similar service for online payments. VALR, ACT Pay, Fivewest, and Peach Payments are some examples of further payment gateways that allow payments using crypto in a similar manner for online payments. Keep in mind however that payment apps and gateways charge transaction fees, and by their nature add an additional intermediary between the customer and merchant.

Concluding remarks on crypto payments

Retailers are free to implement crypto as a form of payment. This is however done at their own risk and that of their consumers: any such use will not be subject to the usual protections of the NPS and the oversight of SARB. Although developments in the market mean that it is easier than ever for retailers to accept crypto as a means of payment.

While crypto is not regulated as part of the NPS, they are regulated by other means, primarily through the regulation of the institutions that provide *services* in relation to crypto i.e. crypto asset services providers or CASPS. We will discuss how this regulation works in the articles that follow in this series.

For assistance with your crypto needs, contact a member of our team.

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