

Nigeria's SEC releases exposure draft for proposed rules on crowdfunding

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Introduction

In a bid to protect the general public when investing in crowdfunding platforms for underlying Micro, Small, & Medium Enterprises ("MSME"s), the SEC recently released a draft of the Proposed Rules on Crowdfunding (the "Rules").

What is "Crowdfunding" about?

The Rules define crowdfunding as the process of raising funds from the public through an online platform ("Crowdfunding Portal") to finance a project or business.

- It provides that all MSMEs incorporated as a company in Nigeria with a minimum of two-years operating track record can raise funds through a Crowdfunding Portal in exchange for the issuance of shares, debentures, or such other investment instrument as the SEC may determine.
- Complex structures, public listed companies and their subsidiaries, companies with no specific business plan or a blind pool cannot raise money through a crowdfunding portal.

Who are the regulated players?

The Rules apply to key players in a crowdfunding process: crowdfunding portals and intermediaries, issuers and investors. The various players have their obligations and limitations under the Rules.

1. Crowdfunding portal

- The Rules provide that any crowdfunding portal operated, provided or maintained in Nigeria, or those outside Nigeria which actively target Nigerian investors, must be registered with SEC. This also applies if the component parts of the platform, when taken together, are physically located in Nigeria even if any of its component parts is located outside Nigeria.
- The Rules provide detailed requirements for the portal registration including a minimum paid up capital of ₦100 million.
- A Crowdfunding Portal may be registered and operated only by a company registered as a Crowdfunding Intermediary.

- However, only entities registered with the SEC as an Exchange, Dealer, Broker, Broker/Dealer or Alternative Trading Facility may be registered as a Crowdfunding Intermediary.

The Rules set out obligations for the Crowdfunding Portal, including:

- Conducting due diligence on issuers;
- Ensuring data privacy and protection;
- Filing monthly, quarterly and Annual reports with SEC; among other things.

2. Issuer

This is an originator, or creator of the security or investment instrument registered with the intermediary (i.e. the underlying business). Issuers can only make offers on a crowdfunding portal.

The Rules also sets out the obligations for all Issuers.

3. Investors

This is any person or entity that seeks to make, are making, or have made an investment in an investment vehicle.

An investor has some rights under the proposed Rules such as:

- 48 hours grace window to withdraw the investment after offer closes
- Right to withdraw his investment within 7 days of becoming aware of any material adverse change affecting the issuer.
- Right to be refunded debited sums within 48 hours after cancellation or withdrawal.

General restrictions or prohibitions

The Rules provide some restrictions and prohibitions on crowdfunding portals and intermediaries such as:

- Directly or indirectly sponsoring or soliciting for investors to invest in offers listed on its own platform.
- Cross ownerships between intermediaries and issuers.
- Financing an investor to purchase investment instrument.
- Investors cannot transfer their securities or investment instrument for a period of one year except they are transferring to the issuer, an institutional investor or a part offer for sale registered with SEC.

- An issuer cannot also list offers on multiple platforms at the same time.
- The Rules prescribe a maximum amount (between ₦50 to 100m) that can be raised by different categories of MSMEs except MSMEs operating as digital commodities. Under the Rules an investor can only invest 10% of his annual income on all crowdfunding platforms in a year. However, high net worth and qualified institutional investors have no investment limit.
- Any crowdfunding portal or intermediary that fails to comply with these rules (when the Rules are finally issued), will be liable to a fine of not less than ₦1m and the sum of ₦10,000 for every day the violation continues.

Conclusion

- This exposure draft is a welcome development. If issued as final, it will provide credible channels for MSMEs to raise funds from investing public through registered crowdfunding platforms while providing protection for the investors.
- However, the Rules appears to exclude private companies who are bigger than MSMEs from the opportunity to access funding through regulated crowdfunding. In the absence of any provision in this Rules, it can be taken that such companies will need to use existing guidelines in order to raise funds such as private placement or if they intend to solicit the public, through a cooperative investment scheme. The SEC may need to consider this in the final Rules.
- The Rules are also quite specific in scope as they cover only incorporated entities and not registered business names. This means that individuals (or sole proprietors) even if registered as business names will not have access to raise funds from the public through these platforms. Given that a large proportion of MSMEs are within this category, the SEC may need to provide additional clarification.
- In terms of next steps, the tax authorities may need to provide guidance on the taxation of revenue streams generated through the platforms as MSMEs may not be sophisticated enough to interpret the tax rules themselves.

For a deeper discussion, please contact any member of our **Regulatory and Compliance Advisory team** below or your usual contact within PwC Nigeria:

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