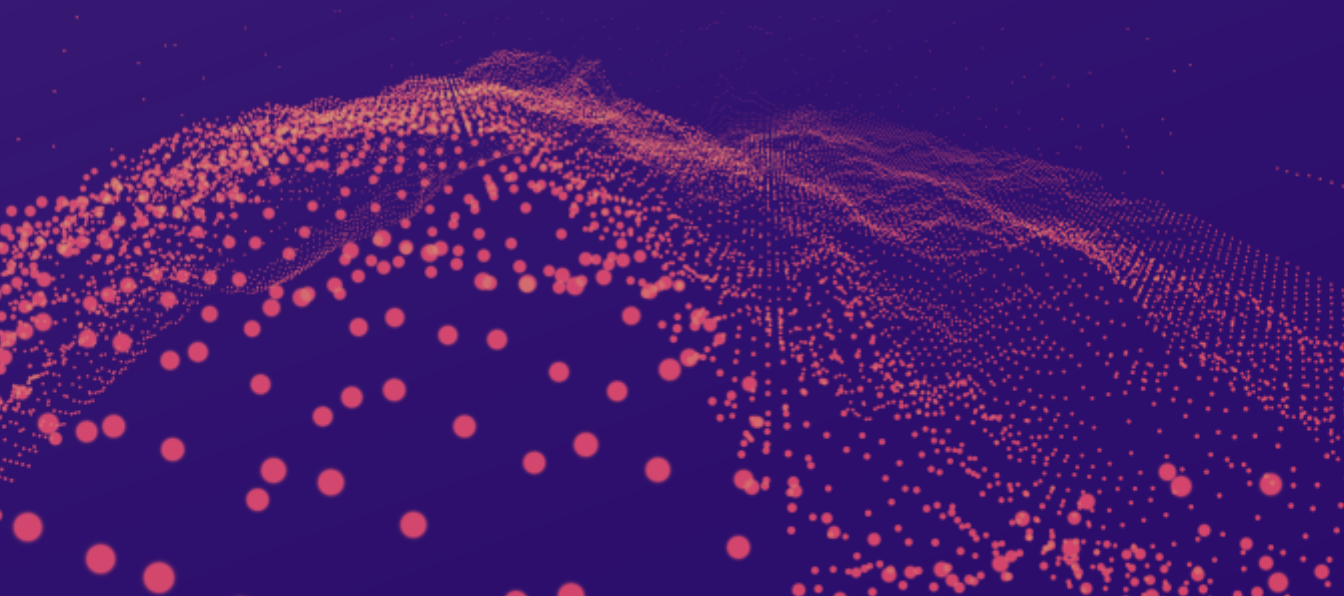




Regulatory Framework For Crowdfunding In Nigeria



INTRODUCTION

Crowdfunding involves the use of aggregated units of capital sourced from a wide pool of individuals through an online platform to fund a new business venture, a project or a cause.

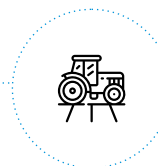
Simply put, crowdfunding is a way by which funds are raised virtually either by individuals or companies usually in small amounts from a large number of people to finance a project or an idea. The Securities Exchange Commission (SEC)'s Exposure Draft on crowdfunding defines it as "the process of raising funds to finance a project or business from the public through an online web-based platform". It comprises three factors: the people, the project and the platform: People, fundraisers and funders, come together to propose and support a project on an online platform.

The conventional types of crowdfunding platforms are: Reward-based Crowdfunding, Donation-based crowdfunding, Equity-based crowdfunding and lending-based crowdfunding.

The relative ease of crowdfunding has seen so many project sponsors (individuals and MSMEs) adopting this innovative financial source over the more traditional sources of finance. With crowdfunding, raising capital is relatively easy as founders do not have to suffer from the psychological pressure of loan repayment with interest rates rivalling the principal sum.

Naijafund, Naturfund, farmcrowdy, piggyvest, Kickstarter, Indiegogo are some examples of crowdfunding platforms in Nigeria.

A number of the crowdfunding platforms such as EZ farming, Farmcrowdy, and Thrive Agric in Nigeria are already players in the agricultural sector.



Regulatory Framework For Crowdfunding In Nigeria

On January 21, 2021 the Securities and Exchange Commission (SEC) approved the new Rules and Amendments to its existing Rules and Regulations pursuant to the Investments & Securities Act (ISA) 2007. This new rule includes a guide on crowd funding. It is worthy of note that these rules only apply to investment-based crowdfunding.



Who Can Raise Funds?

Certain entities are eligible to raise funds through a crowd funding portal which is operated by a registered crowdfunding intermediary (see discussion below) in exchange for the issuance of investment instruments which are:

a. MSME's which have been incorporated in Nigeria with a minimum of two years' operating track record; and

b. MSME's incorporated in Nigeria with less than two years operating track record but having a strong technical partner that possesses a minimum of 2years operating track record or has a core investor.

Companies with more than N500, 000, 000 (Five Hundred Million Naira) in assets cannot raise funds through a crowdfunding portal registered in Nigeria. Also, an issuer shall not host an offer concurrently on multiple crowdfunding portals.

Crowdfunding Intermediary

The SEC Rules require a Crowdfunding portal to register with SEC and such portal can only be operated by a crowdfunding intermediary. Only registered entities such as Exchanges, Dealer, Brokers, or Alternative Trading Facilities may be registered as a crowdfunding intermediary.

The Rules provides that: "a dealer registered by the Commission for the purpose of crowdfunding will be considered a 'Restricted Dealer' and can only carry out activities covered authorized under the Rules. A Crowdfunding portal located outside the country will be considered as operating in Nigeria if it targets Nigerian investor.

The Crowd funding intermediary is expected to carry out due diligence on the prospective issuers intending to use its portal,

disclose and display information relating to its portal, provide investor education programmes and ensure that issuers comply with the responsibilities and obligations prescribed by the SEC rules.

In order to register as a crowdfunding intermediary, an application needs to be made to the SEC along with Certified True Copies (CTC) of the Certificate of Incorporation, Memorandum and Articles Of Association, CAC forms showing the statement of share capital, return of allotment and particulars of directors, latest copies of audited accounts or statement of accounts signed by its auditors and management not more than Nine (9) months old, business plan and information on the crowdfunding IT system to be adopted.

Issuers

An issuer can only offer its investment instrument through a crowdfunding portal operated by a registered crowdfunding intermediary. For an issuer to be hosted on a crowdfunding portal, such issuer shall submit the relevant information to the intermediary including information that explains the key characteristics of the company, information on the expertise of its management, audited financial statements or audited statements of affairs.



The issuer may offer or sell investment instrument under the SEC rules through a crowdfunding portal without prior registration of the securities or investment instruments pursuant to the Act subject to limits on the capital it can raise during a 12-month period. A micro enterprise shall not raise more than 50 million within a 12-month period whilst a small / medium company shall not raise between more than 70million and 100 million respectively within 12-month period without prior registration.



The issuer is expected to file a short, easy to read and standardized offering document to the crowdfunding intermediary providing key information on the issuer, the offering amount to be raised and duration, nature of business or proposed, financial information relating to the issuers.

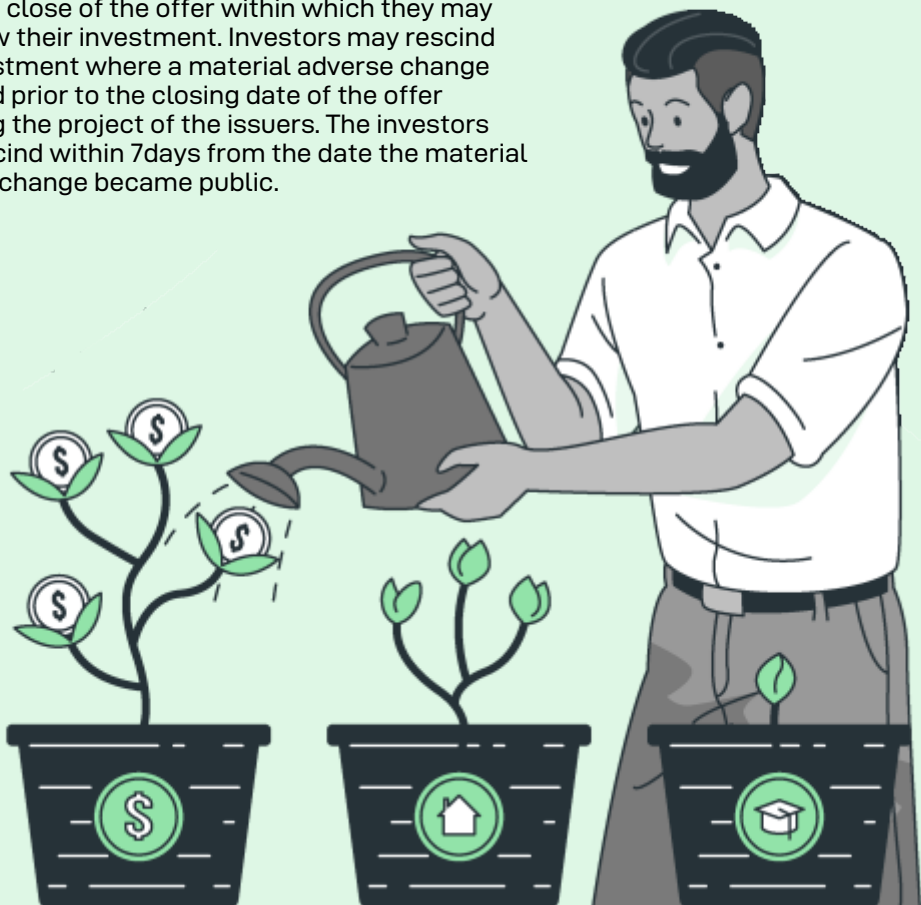
The offering document must be made available to the investor via the crowdfunding portal and shall not be posted on websites or any other media besides the crowdfunding portal. Also, the crowd funding intermediary is expected to deliver the offering materials to SEC at the time they are posted on its portal.

Where an issuer has made an application to the crowdfunding intermediary, the application is then sent by the intermediary to SEC specifying the promoters, directors and shareholders highlighting holders of at least 5% and above of the issuer' shares. Where the intermediary approves the offering, its portal shall be open for no more than 60days. This may be extended for no more than 30 days. An issuer will not be allowed to receive more than the target sum as every intermediary must adopt an IT system which limits the amount to the target sum and rejects additional subscriptions.

Where the issuer is unable to raise the minimum threshold, which is 50% of the target sum from investors, the offer shall be withdrawn and the issuer will only commence a new one not earlier than 30 days after the said withdrawal and demonstrate to the crowdfunding intermediary that all relevant financial and other information have been updated. Where the minimum is not reached at the end of the offer the intermediary shall refund all monies received to investors within 48 hours. However, where the target amount is reached completely or meets the minimum threshold the intermediary shall direct that the funds be paid within 24 hours or one week to the issuer.

Investors

Investors may be allowed to invest in companies hosted on the crowdfunding portal subject to the investment limit. A cooling off period is given to the investors from the time of investment until 48 hours after the close of the offer within which they may withdraw their investment. Investors may rescind the investment where a material adverse change occurred prior to the closing date of the offer affecting the project of the issuers. The investors may rescind within 7 days from the date the material adverse change became public.



Penalty/ Revocation

Where a crowdfunding intermediary fails to comply with the Rules, he shall be liable to a fine of not less than N100, 000.00 (One Hundred Thousand Naira) and the sum of N5, 000.00 (Five Thousand Naira) for every day the violation continues.



The rules also provide that SEC can revoke the registration of any Crowdfunding portal where it fails to meet up with the requirements of the rules, fails to operate or maintain the crowd funding portal for a period of 6 (Six) consecutive months or fails to pay the prescribed fees. These registration requirements do not apply to; (i) a technology service provider providing the infrastructure; software or the system to an operator; (ii) an

operator of a communication infrastructure that enables orders to be routed to an approved stock market and; (iii) an operator of a financial portal that aggregates content

and provides links to financial sites of service and information provider. The Crowdfunding portal is also required to conduct due diligence on issuers, ensuring data privacy and

protection, filing monthly, quarterly and annual reports with SEC.

Conclusion

Crowdfunding allows innovators to access low-cost capital. Traditionally, an innovator would need to rely on "personal savings, home equity loans, personal credit cards, friends and family members to raise funds." With crowdfunding, innovators can find funders from around the world, sell both their products and equity, and benefit from increased information flow. Secondly, crowdfunding platforms serve as "network orchestrators" by curating the offerings that are allowed on their platform by creating the necessary organizational systems and conditions for resource integration among other players to take place. Additionally, Crowdfunding reduces costs for investors as these platforms reduce search costs and transaction costs, which allows increased participation in the market. In our opinion, these rules are a welcome innovation by SEC due to the clamor for regulations of crowdfunding to protect various investors against fraudulent online web-based platforms within the Nigerian space.

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