

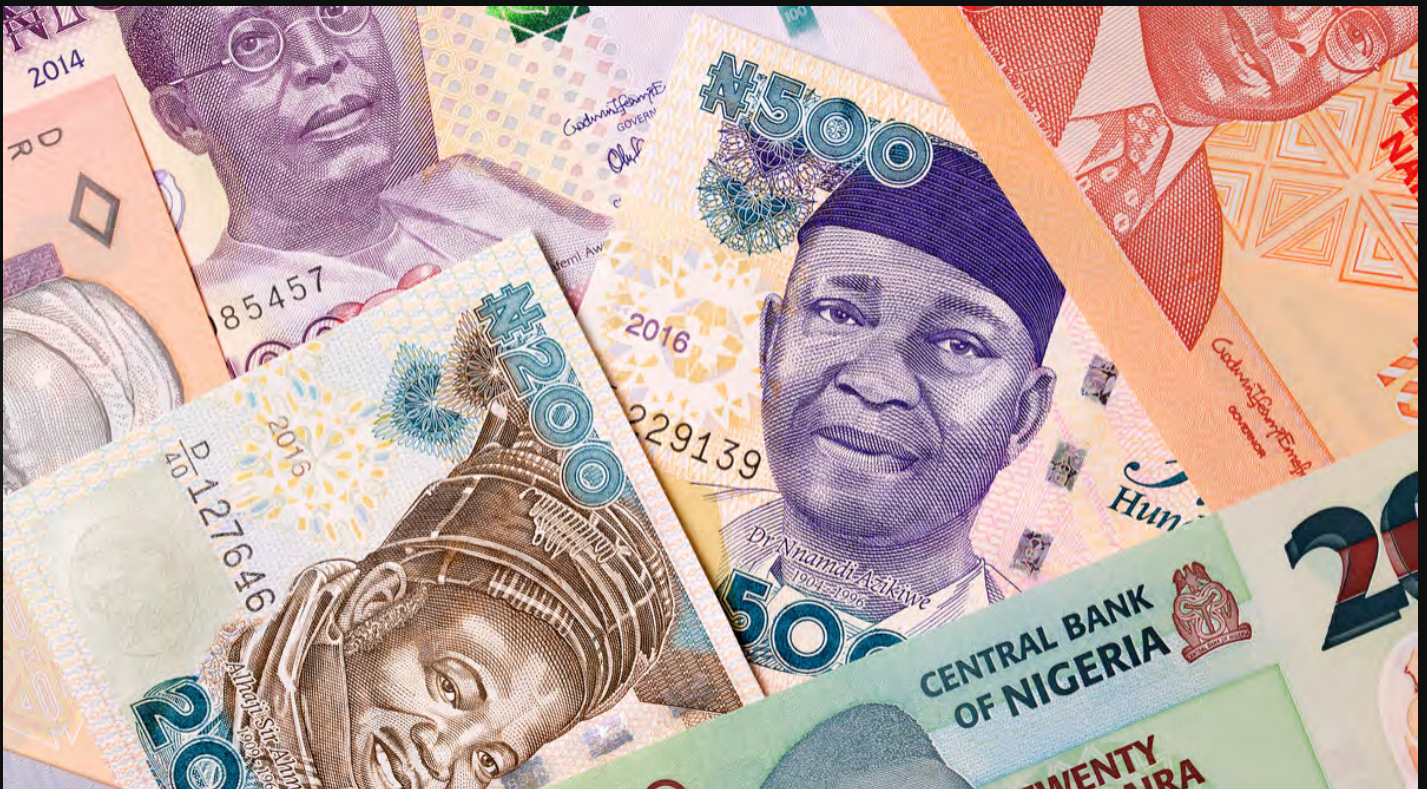
# AELEX

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## THE CHANGING FACE OF FINANCE IN NIGERIA – CROWDFUNDING





## INTRODUCTION

The ways in which an average Nigerian approaches financing has changed drastically within the past decade and the current financial services market is a reflection of this. Technological advancements and economic developments have created a robust world of finance. The shift has been quite dynamic and can be a lot to keep up with.

This article highlights one of the practices changing the face of finance in Nigeria - **CROWDFUNDING**.

## CROWDFUNDING

Crowdfunding is the practice where a large number of individuals contribute small amounts of money to a collective pot to fund a project or venture. It is like the “family and friends financing model” but takes advantage of the global village phenomenon which social media and the internet presents. Broadly, there are four (4) types of Crowdfunding:

- i. Donation-Based Crowdfunding;
- ii. Loan-Based Crowdfunding;
- iii. Reward-Based Crowdfunding; and
- iv. Equity Crowdfunding.

The flexibility of the internet means Crowdfunding could take on other forms or a combination of these four.

## DONATION BASED CROWDFUNDING

As the name suggests, Donation-Based Crowdfunding is soliciting donations from the public to fund projects or ventures which are usually humanitarian. It is now common to see social media requests for funds to pay medical bills, purchase appliances and equipment for a start-up, or to fund pet projects. This can be done via social media apps like Twitter or Facebook or dedicated Crowdfunding apps like GoFundMe, Kickstarter or Donate-Ng.

## LOAN-BASED CROWDFUNDING

Also known as Peer to Peer Lending, this involves individuals lending money to other individuals or entities for interest or return on their investment. This is different from the other types of Crowdfunding as the lenders are repaid their initial capital, sometimes with interest. PiggyVest and FarmCrowdy are examples of Nigerian businesses optimising this type of Crowdfunding (usually through apps with investment features) and they are usually licensed by the Central Bank of Nigeria.

## REWARD-BASED CROWDFUNDING

Under this category, individuals donate to a project or venture in exchange for a reward or gift which is usually unrelated to the project or venture. A unique example is a Twitter influencer @lilearthangelk - termed 'The Naked Philanthropist'- who raised about \$1 million in January 2020 for the Australian wildfire relief efforts by promising to send an erotic picture of herself to every person who donated at least \$10 (about N3,600).[1]

## EQUITY CROWDFUNDING

Although similar to Reward-Based Crowdfunding, this is distinguishable as, in exchange, the donors receive equity in the project or venture. Accessibility to this type of funding has a lot of advantages for small and medium sized businesses who would not have to rely on loans or private equity or venture capital firms.

However, Equity Crowdfunding has its risks, especially to the general public who are not sophisticated investors with experience and knowledge of the capital markets. It is easy to see how the investing public may get swindled out of their investment. Some may argue that individuals only donate a small amount to the collective pot which means limited individual risks.

However, in light of the current legal restrictions, the Securities and Exchange Commission ("SEC") has warned that Equity Crowdfunding is banned in Nigeria and announced that the SEC is looking to regulate Equity Crowdfunding and introduce a proper framework.[2] This is following in the footsteps of jurisdictions like the United Kingdom, New Zealand and the United States of America who have enacted laws which regulate various types of Crowdfunding.

## LEGAL REGULATION (PROHIBITIONS/ RESTRICTIONS)

Where Crowdfunding dealings involve the sale of securities, such as loan or equity, it may be subject to restrictions and Nigerian securities regulations. As such, it is essential to understand the nature of the crowdfunding in light of the Nigerian legal framework to ensure compliance,

[1] Melanie Chalil, 'US Model Raises US\$1m for Australia Bush Fires with Nude Photos, Instagram Deactivates Her Account' (Malay Mail 07 January 2020) <[https://www.msn.com/en-sg/entertainment/celebrity/us-model-raises-usdollar1m-for-australia-bush-fires-with-nude-photos-instagram-deactivates-her-account/ar-BBYHFp5](https://www.msn.com/en-sg/entertainment/celebrity/us-model-raises-usdollar1m-for-australia-bush-fires-with-nude-photos-instagram-deactivates-her-account/ar-BBYHFp5?)> accessed 24 February 2020

[2] Goddy Egene, 'SEC Rules Out Crowdfunding in Nigeria for Now' (This Day, 15 August 2016) <https://www.thisdaylive.com/index.php/2016/08/15/sec-rules-out-crowdfunding-in-nigeria-for-now/> accessed 24 February 2020. A unique example is a Twitter influencer @lilearthangelk - termed 'The Naked Philanthropist'- who raised about \$1 million in January 2020 for the Australian wildfire relief efforts by promising to send an erotic picture of herself to every person who donated at least \$10 (about N3,600).[1]



particularly in relation to Loan-Based Crowdfunding. Donation-based Crowdfunding and Reward-based Crowdfunding are generally not regulated.

The provisions of the Companies and Allied Matters Act 1990 (“CAMA”) and the Investment and Securities Act 2007 (“ISA”) prohibit Equity Crowdfunding for private companies in Nigeria (both by the private company and by a concerned individual). Section 22(5) of CAMA provides that private companies cannot invite the public to subscribe for shares; deposit money for a fixed period; or deposit money payable at call unless authorized by law. Section 67 of ISA further provides that no person can make an invitation to the public to acquire or dispose of any securities of a body corporate unless the body corporate is a public company. Public companies are also restricted in their use of Equity Crowdfunding as currently understood because public offerings in Nigeria are subject to strict security rules and regulations.

It is however recommended that both section 22 of CAMA and section 67 of ISA be amended to create a carve-out that allows private companies utilize Equity Crowdfunding. Indeed, as stated earlier, SEC has expressed intentions to introduce regulations on the use of Equity Crowdfunding by small businesses in Nigeria.[3] The aim is for SEC to regulate the platforms on which Equity Crowdfunding would take place and ensure the investing public are protected. This would be a welcome development for companies in Nigeria, particularly small and medium sized businesses

(SME) and start-ups who are looking to non-traditional financing methods to raise capital for their activities.



## CONCLUSION

One of the main challenges faced by start-ups and SMEs in Nigeria is raising or accessing capital to fund and grow their business. Alternative modes of financing are a necessity especially where traditional modes of financing fail to meet the demand or are unduly burdensome. It is however important for the government and regulators to legislate and facilitate the operation of Equity Crowdfunding and Loan-Based Crowdfunding while ensuring that the Nigerian public are protected from fraud or theft. The government and regulators also need to ensure that Crowdfunding is not overregulated so they do not discourage issuers and investors.

## ENDNOTE

This article is part of the series titled *THE CHANGING FACE OF FINANCE IN NIGERIA* highlighting the various modern financial developments in Nigeria.

Do look out for, and read, the next part in our series.

[3] Feyisayo Popoola, 'SEC to Introduce Crowdfunding Regulation' (The Punch, 22 October 2019) <<https://punchng.com/sec-to-introduce-crowdfunding-regulation/>> accessed 21 January 2020

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