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Overview of the Securities and Exchange Commission's Proposed New Rules on the Issuance and Allotment of Private Companies' Securities

Introduction

On 07 May 2024, the Securities and Exchange Commission (**SEC**) released its Exposure Draft on the Proposed New Rules on the Issuance and Allotment of Private Companies' Securities ("**Exposure Draft**"). As the principal regulatory authority of the Nigerian capital market, SEC is empowered to enact regulations governing the operations of this sector. If made effective, the Exposure Draft seeks to govern the issue and trading of debt securities (bonds, debentures, and other instruments) by private companies.

Hitherto, although private companies could offer debt securities via private placement to institutional/qualified investors, they were restricted from offering securities (debt or equity) to the public¹. This therefore resulted in the reliance on OTC markets or private placements for debt securities issuance.

However, the amendment of Section 67 of the Investment and Securities Act 2007 (**ISA**) by Section 43 of the Business Facilitation (Miscellaneous Provisions) Act 2023 (**BFA**), marked a transformative shift in SEC's power to regulate public debt issues by private companies. **The amendment provides that private companies can offer any securities to the public through any lawful means the SEC may by regulation prescribe.**

This article therefore seeks to review the Exposure Draft, focusing on its scope, the requirements for private companies venturing into debt securities issuance, and the accompanying restrictions.

The SEC Exposure Draft

Scope of Application

Regulation 2 of the Exposure Draft provides that it will apply to:

- a) debt securities issued by private companies through various channels, including public offerings, private placements, book building² and other SEC-approved methods.
- b) registered exchanges and platforms that admit debt securities issued by private companies for trading, price discovery, or information repository purposes,
- c) registered capital market operators engaged in issuing and allotting debt securities of private companies.

Under the Exposure Draft, it is important to note that it provides that every private company with existing debt securities held by institutional investors or high-net-worth individuals must register with the SEC within three (3) months from the date of the regulation's issuance. Non-compliance will attract a penalty of ₦2,000,000.00 (Two Million Naira) and a further sum of ₦100,000.00 (One Hundred Thousand Naira) for every day the violation.

Eligibility for the Issuance of Debt Securities by a Private Company

A private company intending to issue securities under the Exposure Draft must meet the following requirements:

¹ See Rule 568 SEC Rules and Section 22(5), CAMA

² Rule 6

- a) The company must be legally registered in Nigeria with a proven operational track record of at least three (3) years.
- b) The company must not offer bonds if it has defaulted on interest payments or failed to repay principal amounts related to previous debt issuances for a period exceeding six (6) months.
- c) The company and the bonds to be issued must undergo evaluation and rating by a recognized rating agency. This is however optional for private placements.
- d) The credit rating of a bond to be issued shall not fall below the investment-grade threshold.
- e) The company must obtain all necessary approvals from other regulatory authorities relevant to the issuance. These approvals should be submitted to the SEC through the designated securities exchange. Additionally, any conditions imposed by regulatory bodies must be strictly adhered to throughout the duration of the bond, ensuring compliance with regulatory standards and investor protection measures.

Requirements for Registration of Debt Securities with the Securities and Exchange Commission

To offer debt securities publicly or through private placement under this Exposure Draft, a private company must submit the following documents through the Securities Exchange:

- a) Resolutions from the board and shareholders authorising the issuance.
- b) Current Corporate Affairs Commission (CAC) report detailing the company's statutory information.
- c) Memorandum and Articles of Association of the issuer, or an undertaking if there have been no changes.
- d) Latest audited accounts for the preceding 3 years, with the latest not more than 9 months old.
- e) Draft prospectus containing essential information such as amount offered, terms of securities, offer period, purpose of offering, risks, etc.
- f) Draft trust deed (or program trust deed for shelf programs).
- g) Draft vending agreement with the issuing house.
- h) Draft joint issuing houses' agreement (if applicable).
- i) Draft underwriting and sub-underwriting agreements (if applicable).
- j) Completed Form SEC 6.
- k) Letter of "No Objection" from relevant regulatory bodies (if applicable).
- l) Details of any collateral or third-party guarantees.
- m) Mandate letter from the issuer to the issuing house.
- n) Consent letters from involved parties, sworn before a Notary Public or Commissioner for Oaths.
- o) Sworn declaration of full disclosure of material facts in the offer document, signed by two directors and the company secretary.
- p) Schedule of claims & litigations with the solicitor's opinion.
- q) Letter of confirmation of going concern from the issuer's directors.
- r) Any additional documents required by the SEC under these regulations.

Registration fees payable by a Private Company

The registration fees payable by a private company seeking to issue debt securities are structured as follows:

- a) For the first ₦500,000,000 the fee is 0.15%.
- b) For the next ₦500,000,000, the fee is 0.145%.
- c) Any balance above ₦1,000,000,000 incurs a fee of 0.1425%.
- d) A non-refundable filing fee of ₦100,000 is payable to the securities exchange.

Restrictions to the Issuance of Debt Securities

The Exposure Draft imposes certain restrictions/limitations on private companies regarding debt securities issuance. These include:

- a) **Private companies are prohibited from offering their equity securities (shares) to the public under any circumstances.**
- b) Debt securities issued under the Exposure Draft can only be sold to qualified investors.
- c) Only registered capital market operators can participate in debt securities issuances under these regulations.
- d) **No private company or its representatives can offer, sell, or allocate securities to the public without prior clearance from the securities exchange and registration of the securities by the Commission.**
- e) Securities purchased in a public offer under the Exposure Draft can only be traded on a registered securities exchange and are available exclusively to qualified investors.
- f) Companies can only register up to three debt securities issuances within one year, with the total amount raised not exceeding ₦15,000,000,000 (Fifteen Billion Naira). Further issuances would require the company to re-register as a public company.
- g) Private companies may list their securities on a registered securities exchange within thirty (30) days after completion of allotment.
- h) The proceeds from the issuance must be used only for the purposes stated in the offer document, and any deviation requires prior approval from the SEC.
- i) Detailed information on the issuance must be filed with the SEC on the appropriate SEC Form within ninety (90) days after its conclusion.
- j) Only plain vanilla bonds/debentures, Sukuk, and other debt instruments determined by the SEC may be issued.

Failure to comply with the Exposure Draft

Any individual who issues or allots securities without prior approval from the SEC or breaches any provisions outlined in these rules may face one or more of the following penalties:

- a) An initial penalty of not less than ₦10,000,000 (Ten Million Naira), with an additional ₦100,000 (One Hundred Thousand Naira) per day for each ongoing violation.
- b) Suspension or withdrawal of registration for the involved capital market operator(s).
- c) Disgorgement of proceeds or income derived from the transaction.
- d) SEC may ratify or revoke a transaction if it is deemed in the public interest to do so.

Conclusion

The publication of the proposed draft regarding the issue of securities by private companies clearly reflects the SEC's proactive approach to protecting investors and demonstrates its commitment to its oversight functions. While SEC's functions and powers³ broadly allow it to regulate investment/securities business and protect the integrity of the market, its powers in relation to public offers are generally specific to public companies⁴. The amendment of Section 67, by Section 43 of the BFA on the other hand should be noted to be in relation to allowing private companies to offer securities to the public. This denotes that the intent of the BFA is in relation to the regulation of public offers by private companies and not nonpublic offers by private companies. In this regard, there also seems to be conflicting provisions in the Exposure Draft. Rule 2 states that it applies to debt issues by private companies through public offers or private placement. However, Rule 7 states that debt securities issued under the rules will be sold only to qualified investors; who are typically not retail investors, thereby restricting it from the public.

The cap imposed on the sum that can be raised in a year by a private company also poses a challenge to the borrowing powers of companies, notwithstanding their financial capacity to raise more. This may present challenges for capital raised by private companies, particularly medium to large-scale corporates, whose commercial needs and borrowing capacity may very well exceed the limit imposed per year. Furthermore, Rule 4, will have a retrospective effect by imposing penalties on transactions concluded before the release of the proposed Rules.

Consequently, whilst achieving a balance between regulatory oversight and fostering a conducive environment for private sector growth is necessary, this must be achieved by developing a transparent, efficient, and inclusive platform for investors, regulators, and private companies alike.

³ Section 13(a), (b), (g), (n), (o), (u), (dd)

⁴ Section 13 (c), (d),



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