Chapter 5

The Permissibility of Crowd Funding within South Asia: A Comparative Analysis of South Asian Jurisdictions

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ABSTRACT

The chapter will extend upon the extant literature by considering the permissibility of crowdfunding practices within the South Asian region. There is a genuine dearth of research considering these matters, with little research considering the history and permissibility of crowdfunding methodologies within the noted nations. As such the contribution of the chapter is twofold, firstly it represents amongst the first coherent assessments of the use of crowdsourcing based fundraising methodologies within the South Asian region. Secondly it responds to the dearth of research considering the legal permissibility of such practices within the noted nations, while also contrasting the regulatory models of India, Bangladesh, and Sri Lanka with the regulatory models evidenced within selected OECD countries and pertinently the recently reformed model of regulation within the United States, specifically chapter 12 of the Jobs Act (2013).

AN INTRODUCTION TO CROWDFUNDING

Crowdfunding is best understood as the process by which a web based organisation seeks to procure funding from the general public through a web portal, the web portal enables unrelated business enterprises seeking capital to make equity within their entities available to investors. This was not permissible given the restrictions placed on public fundraising by the SEC Act.

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As asserted, Crowdfunding was largely motivated by individuals and organisations promoting profit motivated initiatives through crowdsourcing platforms, and also by the potential benefits to entrepreneurs associated with creating more enabling pathways to accessing startup capital. The existing crowdsourcing platforms (consider Kickstarter, IndiGoGo and similar platforms) limited promoters to accepting donated monies, or selling items for defined sums, with the provision of equity or profit sharing impermissible. However many treaded a unfamiliar and perhaps unexplored path between soliciting general support on behalf of project owners, and offering the possibility of equity sharing which may be conceived to be a security offering, under the technical definition.

The Need for Crowdfunding Provisions and the Howey Test

While it may not be apparent there is a critical distinction between individuals soliciting for support through web based portals, and offering items in exchange for such support and individuals and organisations making equity or profits from a venture available for distribution in exchange for monetary support (Securities and Exchange Commission v. W. J. Howey Co, 1946). While many crowdsourcing models do not involve the issuance of securities in the conventional sense they may be in direct contravention with the Securities and Exchange Commission Act. N D Pope in 2010 noted that some for profit crowdfunding models may be in contravention of the SEC Act, under the rubric of Howey (Pope, 2010).

Additionally prior to the enactment of the JOBS Act, firms wanting to employ crowdfunding techniques when acting in accordance with SEC legislation faced an additional set of challenges. As such the impact of such reforms within the U.S. cannot be understated. The proposed chapter shall consider the permissibility of crowdfunding within the South Asian region with a pertinent focus on India, Sri Lanka and Bangladesh. The chapter is best described as a study in comparative law, considering the regulator provisions enacted within the United States and Australia, and contrasting the evidenced approaches within India, Bangladesh, Nepal and Sri Lanka.

Introduction to Title III of the Jobs Act (2013)

The introduction of the Jumpstart our Business Startups (JOBS) Act was a response to a significant economic slowdown evidenced in the United States. The Act while seemingly focused on job creation is in reality focused on enabling smaller enterprises to avoid onerous securities provisions enacted post the depression. Though the primary motivation behind the act was the easing of regulatory burdens for smaller enterprises, the act provides significant relieve to both small and large enterprises by exempting them from a broad range of seemingly burdensome regulatory pronouncements.

The bill received strong bipartisan support notwithstanding its' significant ramifications, and its unique nature. Proponents of the Jobs Act believe that it will bring much needed system liquidity to emerging organisations starved of capital due to the restrictive lending practices of the banks brought about by sectors recent conservatism. Title III of the Jobs Act is referred to as the Crowdfund Act, and represents perhaps the most intriguing part of the reform program. The provisions found within title III of the Act, enable the use of crowdsourcing methodologies in procuring start-up capital. While such methodologies have been employed within other sectors, to procure resources to address defined needs, perhaps most notably in the charitable sector, and more recently ingeniously in funding artistic works and consumer products, such approaches would be considered unlawful under the Securities Act (1933) and the Securities Exchange Act (1934). As such procuring capital has been a problematic exercise for start-up entities.