



# Review of Crowdfunding Regulation ▶ 2017

Interpretations of existing regulation  
concerning crowdfunding in Europe,  
North America and Israel

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## IMPRESSUM

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## Foreword

This third edition of our Review of Crowdfunding Regulation published at the end of 2017 marks five years since we first commented the European regulatory landscape for crowdfunding and four years since our cooperation with law firms across Europe and beyond to deliver this detailed overview.

In those five years we have witnessed some 11 EU countries implement national level regulations for securities-based and lending-based crowdfunding, as well as in other markets. This has helped to create local markets and first professional standards. It has not helped to create a European market that would allow investors to allocate assets across borders easily, and it did not help small and medium sized companies to raise funding from those investors.

Yet, the discussion around crowdfunding has resulted in detailed regulatory actions in many countries and to a deeper understanding of crowdfunding in the European institutions. We also have seen very positive and specific regulatory actions regarding crowdfunding at EU level, specifically in the new Prospectus Laws. But we are still far from a single market for crowdfunding. The increase in national regulation has made a more aligned pan-European market less likely. We have today what the EC in 2013 warned member states should avoid. The next five years will therefore be vital for the industry to engage in the political discourse.

Today, when we talk about crowdfunding, we of course also talk about alternative finance, fintech, initial coin and token offerings, and digital platforms. The scope of what crowdfunding was five years ago has changed at least in the use of terminology. And we have seen crowdfunding players in search for scale working closely with new types of investors and new types of asset classes over the past years.

Regulation cannot create safeguards for every situation. It can only create a framework in which professional businesses can operate and investors can find a relevant level of risk protection. Within such framework the crowdfunding sector must establish its own professional sets of behaviours, in alignment with different stakeholders and law makers. For the crowdfunding sector this remains an increasingly difficult challenge. With small margins in competitive markets, platforms fail regularly to reach scale with regards to operational and financial sustainability. Even more reason to engage with all relevant stakeholders in shaping a regulatory framework across Europe that is enabling and protecting at the same time.

At ECN, we are proud to be able to work with our members and the many stakeholders around us in establishing a professional crowdfunding industry, be it our work on the legal review, guidelines of best practices, transparent key performance indicators, market analysis or networking and exchange of knowledge. But we need to be realistic about the effect of such work in a fragmented Europe, as so painfully is being experienced through Brexit. We also need to understand that crowdfunding touches upon many regulatory aspects that are not and will likely not be under the supervision of the European Commission any time soon.

We therefore ask policy makers and regulators, both on national and European level, to engage into a dedicated discourse. We need to work on the framework and conditions for success that will ultimately enable our entrepreneurs, innovators and our private investors to help build a growing economy across Europe and within each member state. Education, equality and economic success may help to eliminate some of the political frictions that have flared up over the past two years. Crowdfunding, that is economic co-creation beyond borders, may be able to play a small part in delivering this.

The work of the European Commission on the Capital Market Union (CMU) will likely contribute to a better allocation of private funds and, as a consequence, to the development of small and medium sized enterprises which in turn will again lead to increased job creation. Crowdfunding has a dedicated part in the CMU and we shall expect specific actions addressing cross border transactions by the European Commission soon. With this, crowdfunding will be able to better support small and medium sized enterprises, which are the backbone of the European economy and the main source for employment and value creation across the continent.

The European Crowdfunding Network is extremely grateful to every single contributor to this paper, who has given her or his expertise free of charge and in a very short time frame. There are too many people involved to mention them all here, but the reader can find their contact details at the end of each contribution. Tanja Aschenbeck-Florange of Osborne Clarke, Germany, and her colleague Thorge Drefke, have assumed all initiative and work in creating this extraordinary paper and we would like to thank them for this.

Details of how crowdfunding of all types is treated under national regulation across Europe and beyond can be found in this publication. With this paper we can only give a small insight in the complexities of European legislation keeping back, but also enabling private capital allocation into entrepreneurship, innovation and job creation. We trust that this paper will be once again a key tool for regulators across Europe and beyond, for entrepreneurs, investors and any other interested stakeholders working on delivering economic growth to Europe.

Oliver Gajda, Executive Director, European Crowdfunding Network, Belgium

## Introduction

Crowdfunding (as well as its most prominent “subtypes” Crowdinvesting and Peer2Peer Lending) evolved to a considerable alternative financing source during the last years – and especially since the last edition of our ECN Crowdfunding Review in December 2014.

With the economic growth and increasing importance – especially for start-ups and SMEs – also the regulatory challenges of Crowdfunding gained weight – on national and especially European level. The rag rug of national Crowdfunding regulation not only results in unfair European playing fields for Crowdfunding stakeholders but also hampers further economic growth for cross-border offers of Crowdfunding. This third edition of the ECN Crowdfunding Review 2017 demonstrates the development of Crowdfunding regulation in the EU as well as shows the developments made in third countries important for Crowdfunding. Also, this edition focuses on cross-border Crowdfunding which – as described – is becoming increasingly important.

We would like to seize this opportunity to thank very much our legal partners for participating and the ECN for making the third edition of the ECN Crowdfunding Review 2017 possible. We hope you will enjoy reading.

Tanja Aschenbeck-Florange, LL.M. (San Francisco), Partner, Osborne Clarke, Germany

# Austria

## 1 Recent developments in the market of Crowdfunding in Austria

In recent years, there has been a rapid development in the Crowdfunding sector in Austria. While in the early stages of Crowdfunding only equity based Crowdfunding was recognisably established and allowed under supervisory legislation, in the last years also lending based Crowdfunding platforms and projects have been launched.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

The equity model is still the most popular way for people in Austria to invest in Crowdfunding projects and can be divided in two main types. In the one type the investor participates in both profit and loss of a company (e.g. as a shareholder of capital companies or companionships), in the second type, however, the investor participates in the profit only (e.g. with some kind of silent partnerships).

Crowdfunding platforms providing projects with the equity model often operate in the field of investment broking and/or contract broking. The main goal of these Crowdfunding platforms is/was to operate beyond the prospectus requirement and to avoid obtaining any licence in the sense of the Federal law on Banking (*Bankwesengesetz – BWG*). Therefore, many Crowdfunding platforms work with the model of silent partnerships. Notwithstanding that, these platforms need to comply with the new Alternative Financing Act (*Alternativfinanzierungsgesetz – AltFG*), which has been entered into force in 2015.

Beyond that, those platforms, which offer a trade market for security papers (*Wertpapiere*) and investment products (*Veranlagungen*) have to operate under stricter regulations and mandatorily need to obtain a licence for financial services according to the Federal law on Banking. Companies which use such platforms to raise capital and issue security papers (*Wertpapiere*) or investment products (*Veranlagungen*) by means of a public offer may be subject to the prospectus requirement approved by the Financial Market Authority (*Finanzmarktaufsicht – FMA*) according to the Capital Market Act (*Kapitalmarktgesetz – KMG*). Moreover, certain investment services might require a licence from the Financial Market Authority in the sense of the Federal Law on the Supervision of Securities (*Wertpapieraufsichtsgesetz 2007 – WAG 2007*).

### 1.2 The Lending Model (individuals lend money to a company or a project in return for repayment of the loan and interest on their investment)

Over the last years, also the lending model has become very popular. In this model Crowdfunding platforms offer loans (*Darlehen*) or subordinated loans (*Nachrangdarlehen*). From the investor's perspective this means that he lends money to a Crowdfunding platform, which eventually returns money with interest. In this model, the investor does not share liability for any losses.

Loans or subordinated loans may fall under the definition of the commercial acceptance and constitute foreign funds for management, or they may equate deposits (deposit business; *Einlagengeschäft*) and therefore they require a licence from the Financial Market Authority (*Finanzmarktaufsicht – FMA*). In this context, the higher administrative court (*Verwaltungsgerichtshof – VwGH*) judged that micro credits raised by companies to cover their continuous operation or investments constitute banking business and therefore require a licence from the FMA. To avoid falling under these strict regulations, companies started raising capital with subordinated loans, which – in most cases – does not constitute banking business.

Bonds are another possibility to receive money from investors. In general, bonds do not require a licence according to the Federal Law on Banking or the Federal Law on the Supervision of Securities, if marketable bearer bonds or registered bonds are issued.

Beyond that, subordinated loans as well as bonds are alternative forms of financing according to the Alternative Financing Act (*AltFG*), which is why capital-seeking companies have to adhere to the regulations and may also profit from the benefits therein.

Unlike other European countries the Peer-to-Peer lending (P2P lending) sector is not very popular in Austria. As already mentioned above, the lending model initially failed as the FMA classified P2P lending to be banking business and therefore requires a licence from the FMA. In 2014 the German platform “*Lendico*” started a new approach to offer P2P lending in Austria. Since the operators had a bank institute acting in the background it was possible for *Lendico* to obtain a licence from the FMA and therefore to offer P2P loans in Austria. In the meantime other platforms started providing P2P lending in Austria as well, but all of them are based abroad. Thus, currently there are no platforms offering P2P lending which are operating directly from Austria.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

The rewards model does not provide a monetary return to the investor. In some cases the investor gets non-monetary rewards, such as prototypes of the financed project or goodies from the company. In Austria the rewards model is not common and there are only very few campaigns in which no monetary reward is granted by the capital-seeking companies. This may be due to the fact that people rather invest their money in projects where there is at least a small chance to get a monetary reward.

The donations model is used to finance creative projects or companies. Also this model does not provide any monetary return. In some cases tickets or other rewards of a rather symbolic value are granted to the investor. One of the most popular platforms in Austria providing the donations model is a platform called “*ES GEHT!*”, which is hosted by a banking institute.

## 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

### 1.4.1 Real Estate Crowdfunding in Austria

Also the sector of real estate Crowdfunding has become very popular over the last years in Austria. Most Crowdfunding platforms which are specialised in real estate Crowdfunding offer real estate investment based on subordinated loans, which are granted by the investors to the real estate developers. As the costs for real estate projects are very high most of them are only partly financed by Crowdfunding. The larger part is usually financed by equity capital and/or bank loans.

Another longer existing possibility to raise capital for real estate projects is the build-owner model (*Bauherrenmodell*), which is a participation model offering the investor co-ownership in the building. Therefore, the investor receives a co-ownership share, which is in most cases also registered in the land register. The investor does not receive a fixed interest rate, he only participates in the rental incomes of the building in the extent of his co-ownership share. The significant advantage over classic property investment (buying a flat or a total building) is that the risk of damage caused by vacancy, depreciations, vis major, etc. splits according to the co-owners consortium agreement. Although the build-owner model is very old, there are only a few Crowdfunding platforms, which offer this model.

### 1.4.2 Renewable Crowdfunding in Austria

Over the last years, in the renewable sector project developers have been using Crowdfunding to finance their projects as well. Meanwhile, some Crowdfunding platforms specialising in projects in the renewable sector have been established.

Most projects in the renewable sector concern renewable energy and therefore these projects primarily aim at financing power plants by Crowdfunding. As the development and realisation of such projects is very costly, the projects are only partly financed by Crowdfunding. Most of this projects use the lending or the equity model.

Beyond that, projects are also often financed with the support of local citizens through so-called participation models or -projects (“citizen participation model” – *Bürgerbeteiligungsmodell*). This model provides the investor either with a participation in the generated energy, or the investor obtains a share in a cooperative, which also enables him to participate directly from the project.

## 1.5 International approach

Only a few projects offered on Austrian Crowdfunding platforms come from abroad. Most of these projects are from Germany or other neighbouring countries. Only in the donation-based Crowdfunding sector there is a larger number of projects from abroad, especially from developing countries.

Also in regard to Crowdfunding platforms there are only few international market participants who operate in Austria from abroad. This may be due to the strict legal

requirements, which the platform operators have to meet, are because of the projects provided on the platform.

## 2 Recent developments regarding Crowdfunding regulation in Austria

As a consequence of the increasing number of different Crowdfunding projects and platforms, the legal uncertainties in this context and a lack of consumer protection in some areas, there was a need for legislative actions in order to define rules based on which Crowdfunding projects may be started in Austria.

Therefore the Alternative Financing Act (*AltFG*) was implemented in Austria in 2015. In this context, changes in other laws were necessary as well, especially in the Capital Market Act (*KMG*) and the Federal Law on the Supervision of Securities (*WAG 2007*).

### Overview: Alternative Financing Act

The Alternative Financing Act entered into force on 1 September 2015 and rules the admissibility of financing with alternative financial instruments. The Alternative Financing Act addresses natural and legal persons who are

- operating a company which matches to the criteria for small or mid-sized companies according to the advice 2003/361/EG,
- raise capital directly for their operational activity by issuing alternative financing products and
- make a public offer according to the Capital Market Act to more than 150 individuals.

The Alternative Financing Act does not apply to companies which have a licence according to the Federal Law on Banking, the Capital Market Act, the Federal Law on the Supervision of Securities, the Federal Law on Alternative Investment Fund Managers (*Alternative Investmentfonds Manager-Gesetz – AIFMG*), the Payment Services Act (*Zahlungsdienstegesetz – ZaDiG*), the Insurance Supervision Act (*Versicherungsaufsichtsgesetz – VAG*) or the E-Money Act 2010 (*E-Geldgesetz 2010*)

The material scope of the Alternative Financing Act covers stocks, bonds, shares in corporations and cooperatives, participation rights, silent partnerships and subordinated loans. Except for issuing bonds, the products do not provide the investor with an absolute recovery-right (*unbedingter Rückzahlungsanspruch*), which means that the investor may not claim the amount paid up, especially not in cases of deterioration of the company's economic situation. Therefore, the contracts closed between the issuing company and the investors have to contain a subordination clause.

Although the investment may not grant an absolute recovery-right for the investor, the regional court of Graz (*Landesgericht Graz*) judged that a subordination clause in a contract between the company and the investor is grossly disadvantageous and therefore not applicable. It was argued that the investor shall bear the full economic risk of the investment

without participating in the success of the company. As the decision is not legally binding yet, it remains to be seen how this decision affects existing investment contracts and the future development of the lending based Crowdfunding sector. As a result some companies already switched to profit-participating subordinated loans (*partiarische Nachrangdarlehen*)

### 3 Current Regulation of Crowdfunding in Austria

Depending on which model is used for Crowdfunding, the required capital amount and the intended amount of investors, there will be differences regarding the necessary licences. The Alternative Financing Act contains explicit exceptions to the general licence requirements and moreover provides rules to ensure consumer protection without falling under the strict regime of other relevant regulations.

#### 3.1 Alternative Financing Act

The intention of the legislator when creating the Alternative Financing Act was to simplify Crowdfunding and provide clear rules on the conditions for financing projects by Crowdfunding and for operating a Crowdfunding platform.

Until the Alternative Financing Act was implemented, one of the main obstacles for Crowdfunding has been the cap of the funding volume for each project at EUR 250.000 as an exceeding sum would have caused the application of the prospectus regulation under the Capital Market Act (*KMG*). The main intention was to enable companies to provide projects with a bigger funding volume without causing a lack of consumer protection.

##### 3.1.1 General requirements for issuing alternative finance products

Companies may issue alternative finance products if

- the total amount of the publicly offered alternative finance products does not exceed EUR 1.5 million and
- the amount which is issued to a single person within twelve months does not exceed EUR 5.000, unless the relevant investor is a professional investor according to § 2 (1) Figure 33 of the Alternative Investment Fund Manager Act or a legal person as long as he is not a consumer according to the Consumer Protection Act.

The maximum of EUR 5.000 issued to one single person within twelve months must not be exceeded by a clause which allows the investor to make a new investment after twelve months, when the total invested amount exceeds EUR 5.000.

Beyond the aforementioned exception regarding professional investors and legal persons, an amount exceeding EUR 5.000 may be issued to one single person if the investor (i) informs the issuer that the investment does not exceed twice of his monthly net-income calculated over the last twelve months or (ii) if he informs the issuer that the investment does not exceed 10 % of his financial assets.

### **3.1.2 Abolition of the obligation to publish a prospectus for investment volumes under EUR 1.5 million**

As already mentioned above, until the implementation of the Alternative Financing Act, Crowdfunding projects with an investment volume exceeding EUR 250.000 had to publish a prospectus according to the Capital Market Act. As drawing up a prospectus is very expensive, Crowdfunding became very unattractive for many projects.

Since the implementation of the Alternative Financing Act, investment volumes under EUR 1.5 million do not require a prospectus according to the Capital Market Act. Instead of the prospectus, the company has to disclose the relevant information on the issued product according to the Alternative Financing Information Regulation (*Alternativfinanzierungs- Informationsverordnung – AltF-InfoV*) and publish it to the federal minister for science and research. According to the Alternative Financing Information Regulation the company has to publish an information sheet containing relevant information (i) regarding the company, (ii) on the issued product (iii) regarding the use of the invested amount (iv) on the risk factors which come along with the investment.

In addition to this information sheet companies are obliged to publish a simplified prospectus according to the Capital Market Act if the total amount of bonds or stocks issued by a company in the European Union within twelve months exceeds the volume of EUR 250.000 according to the Capital Market Act.

### **3.1.3 Obligation to publish a simplified prospectus for investment volumes between EUR 1.5 million and EUR 5 million**

If the investment volume is between EUR 1.5 million and EUR 5 million the company is also obliged to publish a simplified prospectus which is much cheaper than a full prospectus.

## **3.2 Licence under the Federal Law on Banking and the Federal Law on the Supervision of Securities**

### **3.2.1 Equity model**

The Federal Law on the Supervision of Securities involves regulations on investment services (*Wertpapierdienstleistungen*), noncore investment services (*Nebendienstleistungen*), financial instruments (*Finanzinstrumente*) and assessments (*Veranlagungen*). As to Crowdfunding models, especially the linguistic terms of financial instruments and assessments are important:

- financial instruments, amongst others, are shares in transferable securities and instruments (e.g. stocks, certificates, loans);
- assessments are, amongst others, uncertified property rights, which serve as a direct or indirect investment for several investors, who bear the risk either alone or together with the issuer, ensuring that investors do not manage the property rights (e.g. uncertified holdings, limited partner participation, closed funds).

The Federal Law on the Supervision of Securities contains organizational requirements as well as good conduct rules, whereby the latter can apply either directly or indirectly (which means applicability to services, which in general do not fall under the regime of the Federal Law on the Supervision of Securities). For any services, which fall under the regime of the Federal Law on the Supervision of Securities, the Financial Market Authority is the competent controlling institution, whereas the Trade Office (*Gewerbebehörde*) is the competent authority for any services, which fall indirectly under the regime of the Federal Law on the Supervision of Securities (e.g. for commercial property consultants that solely convey assessments).

According to the Federal Law on the Supervision of Securities, the commercial provision of the following investment services requires a licence of the Financial Market Authority:

- investment advisory in relation to financial instruments;
- portfolio management by managing portfolios for individual customers with a discretion under a power of attorney of the customer, as far as the customer portfolio contains one or more financial instruments;
- reception and transmission of orders in relation to subjects of one or more financial instruments;
- operating a multilateral trading facility.

Hence, the above-mentioned services can only be provided if either a discrete licence of the Financial Market Authority exists or one cooperates with a securities company or a credit institution as an auxiliary person.

#### **3.2.1.1 Protection of investors**

The Federal Law on the Supervision of Securities contains provisions regarding the protection of investors. In order to avoid any liability of the operator of a Crowdfunding platform for the investors' possible losses, it should be considered not to raise investors' false expectations. Services of the operator of a Crowdfunding platform should be restricted to the reception and transmission of orders of customers (execution-only-orders).

#### **3.2.1.2 Other investment services**

The right to provide other investment services and ancillary services apart from those mentioned above, such as noncore investment services, financial instruments and assessments by companies established in Austria's national territory is governed by the Federal Law on Banking. The latter rules the business of credit institutions and financial institutions, which in principle requires a licence of the Financial Market Authority.

Also the commercial assignment of credits and financing is subject to the Federal Law on Banking, whereas commercial investment advisory is subject to the Trade Law (*Gewerbeordnung – GewO*) and also comprises the procurement of participations, loans and investments. Such activities have to be separated from so-called *loro-emissions*

(*Loroemissionsgeschäft*), i.e. the participation in underwriting third-party issues, which are reserved to credit institutions.

### 3.2.1.3 Summary

In the case of investment services, noncore investment services, or financial instruments or assessments, the Federal Law on the Supervision of Securities might apply and therefore a licence of the Financial Market Authority may be required. If other investment services and ancillary services than those covered by the Federal Law on the Supervision of Securities are provided, the Federal Law on Banking applies. As already mentioned above, the Alternative Investment Act does not apply to companies which have to obtain a licence under the Federal Law on the Supervision of Securities or the Federal Law on Banking and therefore these companies will have to draw up a prospectus according to the rules of the Capital Market Act.

### 3.2.1.4 Lending model

As already mentioned under above, the Financial Market Authority determined that commercial collection of loans on the basis of standardised loan agreements by companies using such loans for financing their on-going business and paying these loans back with interest after a definite period, falls within the scope of § 1 (1) Figure 1 of the Federal Law on Banking. Thus, it is regarded within the commercial acceptance as a fund from other parties for the purpose of administration or as deposits (deposit business; *Einlagengeschäft*), a business reserved to credit institutions and requiring a licence from the Financial Market Authority (FMA UB0001.200/0017-BUG 2012). The Constitutional Court (*Verfassungsgerichtshof – VfGH*) refused to handle a complaint against the aforementioned decision (B 54/13-11) and assigned it to the Highest Administrative Court (*Verwaltungsgerichtshof*), which confirmed the decision of the Financial Market Authority.

By contrast, the emission of loans or subordinated loans does not constitute an assessment in the sense of the Federal Law on the supervision of securities.

### 3.2.2 Donations or rewards model

Depending on the structure in detail, there are good reasons to state that these kinds of investments do not qualify as assessment products (*Veranlagungen*) and therefore should usually not fall under the jurisdiction of the Federal Law on Banking.

## 3.3 Licence under the Payment Services Law

A transfer of funds between investors and the operator of a Crowdfunding platform can constitute payment services (*Zahlungsdienste*) in the sense of the Payment Services Act (*ZaDiG*). Such a transfer of funds occurs if the investors pay their investment amounts to the operator of the Crowdfunding platform, who passes the funds on to an entrepreneur. The Payment Services Act provides for various legal institutes, which are excluded from the applicability of this law; this applies, amongst others, to commercial agents (*Handelsagenten*).

Under various circumstances, especially provided that the operator of a Crowdfunding platform has the authorisation to negotiate, or negotiate contracts on behalf of the funder and the fund seeker, the operator of a Crowdfunding platform may be regarded as a commercial agent. Alternatively – in order to avoid licencing requirements – the operator of a Crowdfunding platform could use an external provider or partner for processing payments instead of acting as an intermediary himself.

### 3.4 Prospectus requirement

#### 3.4.1 General Rule

Companies which are issuing security papers (*Wertpapiere*) or investment products (*Veranlagungen*) to investors by means of a public offer can be subject to the prospectus requirement, namely a requirement to publish a prospectus approved by the Financial Market Authority. Publishing a prospectus according to the Capital Market Act is only necessary if the privileges regarding the prospectus according to the Alternative Financing Act do not apply. For most Crowdfunding projects the Alternative Financing Act applies and therefore no prospectus is required.

The legal basis for publicly offering security papers or investment products for sale is the Capital Market Act. In addition, EU Regulation Nr. 809/2004, as amended, establishes the legal framework for drawing up prospectuses for investments. If the prospectus includes securities for admission to the stock exchange, the Stock Exchange Act (*Börsegesetz – BörseG*) applies as well. The prospectus requirements in accordance with the Capital Market Act are only applicable if the Alternative Financing Act does not apply. This may be the case if (i) the issuing company has a licence according to the Federal law on Banking, the Capital Market Act, the Federal Law on the Supervision of Securities, the Federal Law on Alternative Investment Fund Managers the Payment Services Act, the Insurance Supervision Act or the E-Money Act 2010 or (ii) does not match the criteria set forth in the Alternative Financing act (e.g. total Investment amount over EUR 1.5 million).

A “*public offer*” according to the Capital Market Act is a notification to the public in any form and distributed in any way, which contains sufficient information on the conditions for the offer, allowing an investor to decide whether to buy or subscribe to the securities or investments, or not. The operator of a Crowdfunding platform is usually not subject to such a prospectus requirement, as long as he is not responsible for the “*public offer*”. However, if the operator of a Crowdfunding platform merchandises the Crowdfunding project on a website and thereby makes a public offer, a prospectus might have to be published.

Depending on their structure, subordinated loans do generally not constitute assessments under the Capital Market Act and therefore no prospectus is required. The same should apply to investments of individuals providing money to a company or a project for benevolent reasons or for a non-monetary reward (donations or rewards model).

### 3.4.2 Exceptions of the prospectus requirement

In addition to the aforementioned exceptions from the prospectus requirement according to the Alternative Financing Act, the general prospectus requirement does not apply in exceptional cases exhaustively named in § 3 of the Capital Market Act, amongst others, for offering security papers or investment products in the European Union for a total consideration of less than EUR 250.000, calculated over a period of twelve months.

Moreover, the general prospectus requirement does not apply on offers directed at less than 150 natural or legal persons per member state of the European Economic Area, if such persons are not qualified investors. In general, if Crowdfunding projects are available (e.g. advertised) online, a public offer to more than only 150 natural or legal persons is at hand.

### 3.5 Additional regulations

Other common regulations, to which the operator of a Crowdfunding platform may be subject include:

- the Industrial Code (*GewO*);
- the Law on the Supervision of Securities (*WAG 2007*);
- the Consumer Credit Regulation (*Verbraucher kreditgesetz – VKrG*);
- the Consumer Protection Act (*Konsumentenschutzgesetz – KSchG*).

### 3.6 Regulations on Crowdfunding platforms under the Alternative Financing Act

Apart from information requirements and the general requirements under which alternative investment products can be issued, the Alternative Financing Act contains requirements for the operators of internet platforms. The term “*internet platform*” is defined as a website on which alternative finance products are arranged between the issuing company and the investor. The company seeking funding is defined as “*issuer*” (“*Anbieter*”) in the Alternative Financing Act, which may in some cases be misleading, especially in context with subordinated loans, which are also ruled by the Alternative Financing Act.

If the internet platform provides the investor with investment products, the Crowdfunding platform needs to obtain a permission according to § 94 Figure 75 of the Austrian Industrial Code (*GewO*), meaning that the operator of the Crowdfunding platform needs an authorisation to provide the business of commercial investment consulting (*gewerbliche Vermögensberatung*). If the internet platform provides the investor with alternative finance products according to § 1 (6) of the Federal Law on the Supervision of Securities (e.g. stocks and shares in alternative investment funds), he needs a licence according to § 4 (1) of the Federal Law on the Supervision of Securities, meaning that he is allowed to act as a securities services provider (*Wertpapierdienstleistungsunternehmen*).

According to § 4 of the Alternative Financing Act operators of internet platforms that provide alternative finance products have to

- adhere to the rules on money laundering and the financing of terrorism according to §§ 365m to 365z of the Austrian Industrial Code;
- verify the identities of the companies which offer their alternative financing products on the internet platform and the customers which make investments using the internet platform

Beyond that, operators of internet platforms offering alternative financing products are obliged to disclose information according to § 5 (3) of the Alternative Financing Act to the visitors, in particular:

- information regarding the operator of the internet platform (name, legal form, registered office, information regarding the managing directors, supervisory board and the shareholders.
- information concerning the criteria based on which the issuers are selected for the platform;
- information regarding the type, amount and frequency of fees charged from the issuer and/or investor, as well as
- the information sheet or the simplified prospectus,
- the annual records of the company operating the internet platform.

### **3.7 Regulations on Crowdfunding platforms under the AIFMD Regime in Austria**

#### **3.7.1 Alternative Investment Fund Manager Act (AIFMG)**

Austria implemented the European Alternative Investment Fund Managers Directive (AIFMD) by the Alternative Investment Fund Manager Act (*AIFMG*). As the rules of the Alternative Financing Act might not apply to each operator of a platform (e.g. as the operator operates an alternative investment fund) in some cases the Alternative Investment Fund Manager Act might be relevant. The Alternative Investment Fund Manager Act is heavily based on the AIFMD and in some parts corresponds literally to the AIFMD. Yet contrary to the AIFMD, the Alternative Investment Fund Manager Act also provides the legal possibility to disperse alternative investment funds to private customers.

#### **3.7.2 Definition of an alternative investment fund**

The scope of the AIFMD is broad: it aims at the managers of alternative investment funds (AIFM). The AIFMD is applicable when either the alternative investment fund is authorised pursuant to relevant national law in a member state or has its registered office or head office in a member state and/or the manager of an alternative investment fund (AIF) has its registered office in the European Union.

Due to the broad scope of the AIFMD, it is crucial to the impact of the national AIFMD regulations on Crowdfunding whether any of the participants qualify as an alternative investment fund or an alternative investment fund manager, or not. As defined in the

Alternative Investment Fund Manager Act, an alternative investment fund is any organ for a collective investment undertaking which,

- on the basis of a stipulated portfolio strategy
- raises capital from a number of investors,
- with a view to investing it in accordance with a defined investment policy
- for the benefit of these investors
- as long as the money collected does not directly serve for operational activities.

However, any organ that requires a permit under the Directive 2009/65/EC (UCITS), is excluded from the definition of an alternative investment fund.

In its explanatory remarks regarding the Alternative Investment Fund Manager Act, in respect of the term of an alternative investment fund, the Austrian legislator refers widely to the directive 2011/61/EC and § 4 thereof. Hence, the definitions of alternative investment funds made by European entities should be taken into account when talking about the term of an alternative investment fund.

With regard to the requirement that the money collected does not directly serve for operational activities, the European Securities and Markets Authority (ESMA) in its consultation paper on “Guidelines on key concepts of the AIFMD” published on 19<sup>th</sup> 2012, (“ESMA Consultation Paper”) considers that "an ordinary company with general commercial purpose should not be considered a collective investment undertaking".

In its brochure “Frequently asked questions regarding the applicability of the Alternative Investment Fund Manager Act” as of 30<sup>th</sup> July, 2013, the Financial Market Authority clarifies that the question, whether an organ is to be classified as an AIF, must be examined on an individual basis in any case, having regard to the structural and content factors and not the pure form of an organ. Moreover, the Financial Market Authority refers to the “Final Report – Guidelines on key concepts of the AIFMD” of the European Securities and Markets Authority as of 24<sup>th</sup> May 2013.

### 3.7.3 Company seeking funding

As stated above, the Alternative Investment Fund Manager Act does not apply if the money collected does directly serve for operational activities. In general, a classification of alternative investment funds can be made according to the following criteria:

- The main business purpose of alternative investment funds should not be directed towards the purchase/sale or supply of goods or services that are not part of the financial services sector. In the case of such an operational main business purpose (commercial or industrial purpose), an alternative investment fund can be excluded as a principle.

- The collection of actual capital includes cash transfers as well as fixed financial commitments to the investor (“commitment”). The process of collecting does not need to happen constantly, but can also take place as a one-time process.
- The acquisition of shares must be open to a wide range of investors, but it is sufficient if only one investor actually invests. This excludes vehicles that, due to legal regulations or articles of association (fund regulations), are only open to one investor.
- The investment strategy must be defined and is binding for the manager; the transfer of investment decisions to a third party can be possible. In contrast to conventional mutual funds, the investment strategy does not have to be aligned with the aspect of risk spreading.

Companies seeking funding by means of a Crowdfunding platform can only be operating companies outside the financial sector if

- their business strategy is simply the commercial success of their business,
- they do not intend to follow any defined investment policy, but want to finance their on-going day-to-day business, and
- they operate the facility, the production or the project themselves within their day-to-day business.

In general, a typical start-up or developing company seeking funding for its general commercial business by means of a Crowdfunding platform meets these requirements, so that those companies should usually fall beyond the scope of the Alternative Investment Fund Manager Act.

As there are no consistent European guidelines regarding the term of an alternative investment fund, the Financial Market Authority acclaims that, if it is in the legal interests of a party, it is possible to obtain a notice of assessment (*Feststellungsbescheid*) by the Financial Market Authority to determine whether an operating company is an alternative investment fund or not. The rationale for a legal interest as mentioned before could be that otherwise there is an elevated risk of violating punitive regulations. If the desired determination has been to be not classified as an alternative investment fund, it is incumbent upon the party to prove the relevant evidence and to document it.

Finally, it has to be noted that alternative investment funds are facilitated when the assets acquired through leverage do not exceed a total of EUR 100 million or total assets do not exceed EUR 500 million (“de minimis-barrier”). Although such alternative investment funds must be registered with the competent authority, the other conditions regarding licencing do not apply to funds, which are below this amount’s specified limits.

### 3.7.4 Project company seeking funding

#### 3.7.4.1 Equity model

Although neither the Alternative Investment Fund Manager Act, nor the explanatory notes hereto, nor the Financial Market Authority or courts have dealt with this question, we assume that, following the notion of the German BaFin relating to the comparable German law, companies cannot qualify as operating companies if they are established as a “project company” to finance a single project and do not operate the facility or production themselves.

Accordingly, it cannot be excluded that this kind of “project company” might constitute an AIF within the meaning of the Alternative Investment Fund Manager Act, if it seeks funding in return for a share in the profits or revenue generated by the project.

#### 3.7.4.2 Lending model

A subordinated loan (“*Nachrangdarlehen*”) should generally be capable of being structured as a non-AIF investment, provided that the investor does not share liability for any losses. However, this issue has not been dealt with by the Alternative Investment Fund Manager Act, nor the explanatory notes hereto, nor the Financial Market Authority or courts.

#### 3.7.4.3 Donations or rewards model

Some of the project companies do not offer any kind of revenue, but instead return non-financial rewards. Although neither the Alternative Investment Fund Manager Act, nor the explanatory notes hereto, nor the Financial Market Authority or courts have dealt with this question, we assume that, in the latter case it can be argued that the funds are not invested for the benefit of those investors and the funding therefore contains neither collective investment undertaking, nor alternative investment funds.

#### 3.7.4.4 Crowdfunding platform

As a general rule, since the operator of a Crowdfunding platform does not raise capital from investors for his own business, it should not qualify as an alternative investment fund. Even if the underlying investment qualifies as an alternative investment fund there are persuasive reasons to state that the Crowdfunding platform does not “manage” this underlying investment, but that the Crowdfunding platform merely arranges investment into it. The manager of the alternative investment fund is typically the company seeking funding by means of the Crowdfunding platform. To sum up, there are good reasons for a Crowdfunding platform in general why it should not qualify as an alternative investment fund in the sense of the Alternative Investment Fund Manager Act.

### 3.8 Conclusion

In conclusion, Crowdfunding is regulated extensively in Austria: pursuant to the provisions of capital market law, under various circumstances, the operator of a Crowdfunding platform might demand a licence according to the Federal Law on Banking or the Federal Law on the Supervision of Securities.

Moreover, for entrepreneurs issuing security papers or investment products to investors by the means of a public offer a prospectus is required, unless the Alternative Financing Act or other exemption clauses are applicable in the individual cases. The application of the Alternative Investment Fund Manager Act to companies seeking funds by means of Crowdfunding platforms would make any attractive cost-reward ratio impossible. Yet, the Alternative Investment Fund Manager Act is not applicable if the money collected serves directly for operational activities, which, in several cases, can benefit Crowdfunding operators alike.

In consideration of the strict rules of Austrian capital market, Crowdfunding should be more liberalised. Implementing the Alternative Financing Act was the initial step into the right direction and should be the base for further legal development in this sector. However currently there are no legislative proposals to be implemented in the near future.

#### 4 Regulatory barriers for Crowdfunding crossing borders

Regulatory barriers for cross-border Crowdfunding may occur in different situations. Therefore it has to be clarified whether Austrian law is applicable to Crowdfunding platforms, to companies and in regard to consumer protection to the investors. In summary, the following constellations are possible where regulatory barriers might occur.

Inbound, when

- foreign Crowdfunding platforms address Austrian investors;
- foreign Crowdfunding platforms address Austrian companies.
- Outbound, when
- Austrian Crowdfunding platforms address foreign (EU) investors
- Austrian Crowdfunding platforms address foreign companies/projects.

As there are no guidelines from the Financial Market Authority nor any supreme court decision, cross-border Crowdfunding implicates legal uncertainty which is caused by widespread regulations that affect international Crowdfunding projects and platforms.

##### 4.1 Applicable law

The application of Austrian law in most cases depends whether there is a public offer according to the Capital Market Act. Therefore, Austrian jurisdiction also follows a marketing focused approach.

The public offer is defined as “any communication to the general public in any form whatsoever that: contains adequate information on the terms and conditions of an offering (or an invitation to subscribe) for securities or an investment, and on the securities or investment themselves; and gives potential investors a basis on which to reach an informed decision on the purchase or subscription to securities or the investment.”

Offering a financial instrument may only be qualified as public offer according to the Capital Market Act if it is (possibly amongst others) also addressed to Austrian investors. It does not matter from where and from which country the offer is based; moreover the Austrian Capital Market Act may also apply to foreign companies. If financial instrument are placed on online platforms the application of the Austrian Capital Market Act depends on whether Austrian investors should be addressed by the offer, or not.

The main criteria for assessing whether there is a public offer according to the Capital Market Act is the language used in the offer, the information on contact persons, paying agencies and tax rules. A disclaimer that informs the investor that single markets are excluded from the offer, constitutes another indication of not addressing people in these markets, and thus, that there is no public offer according to the Capital Market Act.

To sum up, it can be said, that Austrian legislation may be applicable to various cross-border matters. Even though legislation is quite similar as in Germany, the Austrian Financial Market Authority has not released clear guidelines yet, which provide clear rules based on which it can be assessed if there is a public offer.

## 4.2 Inbound

### 4.2.1 Foreign Crowdfunding platforms addressing Austrian investors

As mentioned above, foreign Crowdfunding platforms enter into the Austrian market by placing a public offer according to the Capital Market Act. If the offer addresses Austrian investors, Austrian law might be relevant for (i) the operators of the Crowdfunding platform and/or (ii) to the issuing companies.

#### 4.2.1.1 Crowdfunding platform

As the Alternative Financing Act does apply if there is a public offer according to the Capital Market Act, the licencing regulations regarding internet platform operators do also apply for platform operators from abroad. In regard to these licencing obligations the Alternative Financing Act does only provide regulations for “*internet*” platforms. As there are no platforms in Austria, which operate without an internet platform, this fact does not have any effect, but should be mentioned.

#### A. Licencing obligations for investment products

As already mentioned above, if the operator of a platform offers investment products, he has to be entitled to provide the business of commercial investment consulting (*gewerbliche Vermögensberatung*) according to § 94 Figure 75 of the Austrian Industrial Code. Since commercial investment consulting is a regulated business, the operator of a Crowdfunding platform needs to submit a certificate of competence to the local trade authority before commencing the activity, meaning offering finance products via an internet platform in Austria.

Crowdfunding platform operators from the European Economic Area who address Austrian investors may take action in Austria without submitting a certificate of competence if they exercise their activities in Austria only temporary and occasionally and (i) the business is also regulated in their home state or (ii) if the business is not regulated and has been carried out in their home state for at least one year within the last ten years.

The foreign platform operator has to indicate the establishment of the business in Austria to the Federal Minister of Economics and Labour by giving information on his insurance cover. The indication needs to be renewed every year if the business is conducted only temporary and occasionally.

Announcing the establishment of the business, the Crowdfunding platform operator has to provide the Federal Minister of Economics and Labour with the following documents:

- an evidence of his nationality;
- an evidence that the Crowdfunding platform operator is allowed to provide the business in his home state, including the registered office of his business;
- if the business is conducted in Austria temporary and occasionally, an evidence that the business has been carried out in his home state for at least one year within the last ten years;
- if the business should be conducted permanently in Austria, a certificate of competence.

#### B. Licencing obligations for finance products

For distributing finance products according to § 1 (6) of the Federal Law on the Supervision of Securities (e.g. stocks and shares in alternative investment funds), a platform operator needs a licence according to § 4 (1) of the Federal Law on the Supervision of Securities, meaning a licence as securities services provider (*Wertpapierdienstleistungsunternehmen*). In general, the licence is granted by the financial market authority when the following conditions are met:

- the Crowdfunding platform has to be organised as a corporation or cooperative;
- the initial capital must amount to at least EUR 50.000 and has to be at the free disposal of the management of the Crowdfunding platform, unless the securities services provider has a pecuniary damage liability insurance (*Vermögensschadenhaftpflichtversicherung*);
- the managing directors of the securities services provider need the necessary reliability and adequate experience to lead such company;
- the securities services provider has to meet the conditions according to § 5 (1) Figures 2 to 4a and 6, 7, 9, 10, 11 and 14 of the Federal Law on Banking. These conditions contain special requirements on the organizational structure on the company, which acts as a securities services provider.

For companies from the European Union there are special exceptions from the above-mentioned licence obligation. According to the Regulation EU 575/2013 (Capital Requirements Regulation, CRR) credit institutions, which have their corporate seat in the European Union, may provide services according to Article 2 to Article 8 of the Directive EU 2013/36 regarding investment products as far as they act through a branch in Austria or under the freedom of providing services (*Dienstleistungsfreiheit*). Moreover, the licence which the CRR-credit institution obtained in the respective member state has to cover taking action in a foreign member state of the European Union.

If the financial services are carried out under the freedom of providing services, the supervisory authority in the respective home member state of the CRR-credit institution has to inform the Austrian Financial Market Authority about the performance on services and has to provide detailed information on the particular services which will be provided in Austria according to the attachment of the Directive EU 2013/36.

If the financial services should be carried out through a branch, the supervisory authority in the respective home member state of the CRR-credit institution has to inform the Austrian Financial Market Authority and has to provide detailed information on the CRR-credit institution. At least two months after the information was provided by the supervisory authority in the respective home member state to the Financial Market Authority, the company is allowed to provide services through the branch.

#### 4.2.1.2 Company

##### A. Prospectus requirement

Companies seeking funding listed on foreign Crowdfunding platforms and addressing Austrian investors may be affected by the Austrian prospectus requirement. Placing a public offer which is addressing investors from Austria leads to the application of the Austrian Capital Market Act and/or the Alternative Financing Act. Depending on whether the conditions for the application of the Alternative Financing Act are met, the company will only have to provide the investor with an information sheet according to the Alternative Financing Act or a simplified prospectus according to the Austrian Capital Market Act.

If the Conditions for applying the Alternative Financing Act are not met (e.g. total Investment amount over EUR 1.5 million) the prospectus regime of the Austrian Capital Market Act applies and therefore the company has to provide the investor with a full prospectus which is very expensive.

##### B. Other regulations

Beyond the prospectus requirement or the obligation to provide an information sheet according to the Alternative Financing Act, the company is also subject to the general rules according to the Alternative Financing Act as already mentioned in section 3.6 of this article. Therefore the special regulations regarding the capped maximum investment amount and the amount issued to one single investor should be observed, otherwise further licence obligations

according to the Austrian Banking Act, the Federal Law on the Supervision of Securities, the Alternative Investment Fund Manager Act or the Capital Market Act may apply as already described in detail above.

#### **4.2.2 Foreign Crowdfunding platforms addressing Austrian companies**

Also if foreign Crowdfunding platforms approach Austrian companies, Austrian law may apply in two different situations:

- to the Crowdfunding platform, which may be subject to licence obligation and information obligations;
- to the Austrian company seeking funding, which might be subject to prospectus and information requirements.

##### **4.2.2.1 Crowdfunding platform**

###### **A. Licencing obligations**

As the Alternative Financing Act is only applicable if there is a public offer according to the Capital Market Act, which addresses Austrian investors, the licence obligations provided by the Alternative Financing Act do not apply to foreign platform providers. Only if the foreign Crowdfunding platform hosts projects from Austrian companies and addresses Austrian investors, the Alternative Financing Act would be applicable and the platform needs a licence as already described.

Beyond the licencing obligations, which are directly provided in the Alternative Financing Act, the Crowdfunding platform may be subject to licencing provisions according to the Federal Law on the Supervision of Securities for providing securities services. But as the services are not provided in Austria, meaning that it is not addressed to Austrian individuals, it is not applicable.

The same applies for any licencing obligations according to the Alternative Investment Fund Manager Act. As the Alternative Investment Fund Manager Act addresses alternative investment fund managers, the licencing requirements depend on the registered office of the alternative investment fund manager, meaning the operator of the Crowdfunding platform.

###### **B. Information obligations and other regulations**

Information Obligations are also determined in the respective regulations such as in the Alternative Financing Act, the Federal Law on the Supervision of Securities, and the Alternative Investment Fund Manager Act. These obligations do not apply in case a foreign Crowdfunding platform addresses Austrian companies either, because the applicability of this regulations depends on whether Austrian investors are approached, or not.

In fact, the extensive regulations provided by the Federal Law on the Supervision of Securities do only apply to legal entities as defined in § 15 of the Federal Law on the Supervision of Securities. Therefore, only Austrian investment firms and Austrian securities

services providers are subject to those regulations. Foreign investment firms and credit institutions only fall within the compliance regulations of the Federal Law on the Supervision of Securities if they act through a branch in Austria and therefore address their services to Austrian investors.

#### 4.2.2.2 Company

##### A. Prospectus requirement

According to § 2 of the Capital Market Act the prospectus requirement is only applicable if the company makes a public offer. As already mentioned, a public offer according to the Capital Market Act presupposes that it addresses Austrian investors. If the Crowdfunding platform does only address its services to companies seeking funding, but not to investors in Austria, the prospectus requirement is not applicable if the Austrian companies act on foreign Crowdfunding platforms.

In addition to the Capital Market Act, the Alternative Financing Act provides information obligations to investors. As well. In particular, companies have to provide the investor with an information sheet instead of a full prospectus if the requirements of the Alternative Financing Act are met respecting the issued product. Also the Alternative Financing Act is only applicable if there is a public offer. Regarding the definition of a Public offer, the Alternative Financing Act refers to the Capital Market Act and therefore a Public offer does only exist if it is addressed to Austrian investors, which is why alternative financing products from Austrian companies issued by foreign Crowdfunding platforms and excluding Austrian investors are not subject to the information obligations according to the Alternative Financing Act.

### 4.3 Outbound

The outbound situation means that an Austrian Crowdfunding platform enters foreign (European) markets and therefore investors from foreign countries should be approached. Two situations may occur:

- Austrian Crowdfunding platforms approach foreign (EU) investors or
- Austrian Crowdfunding platforms approach Austrian investors and host a company/project from another EU member state on its platform

#### 4.3.1 Austrian Crowdfunding platforms approaching foreign (EU) investors

If an Austrian Crowdfunding platform enters foreign European markets at least one of the main persons has a very close connection to Austria (e.g. an Austrian Crowdfunding platform is hosting a project in which only German investors may participate).

Also within the outbound situation the application of Austrian regulations mainly depend on whether Austrian investors are approached by the project and the Crowdfunding platform. The main criteria to assume if Austrian investors should be addressed, is the use of the German language. This leads to difficult delimitation problems between approaching Austrian

or German investors. Therefore other criteria have to be considered such as the legal system according to which the Crowdfunding platform or the company addresses investors. Moreover, a disclaimer, which excludes single markets from the application of the offer, may be an indication of the approach of Austrian investors by the Crowdfunding platform.

#### 4.3.1.1 Crowdfunding platform

##### A. Licencing obligations

As already described above, Austrian investors are not approached by the public offer and therefore the Alternative Financing Act and the licencing obligations contained therein are not applicable to the Crowdfunding platform.

The application of the licencing obligations according to the Federal Law on the Supervision of Securities depends on whether the services of the Crowdfunding platform are provided in Austria. Since Austrian investors should not be approached in the above mentioned situation this licencing obligation does not come into effect either.

Only if the Crowdfunding platform manages an Alternative Investment Fund, it might be licenced according to § 5 of the Alternative Investment Fund Managers Act. As Crowdfunding platforms do not offer alternative investment funds, this licencing obligation is negligible.

##### B. Information obligations and other regulations

As the Alternative Financing Act does not apply, the information obligations and also other obligations provided therein do not come into effect.

Moreover, as Crowdfunding platforms need no licencing under the Federal Law on the Supervision of Securities, Austrian Crowdfunding platforms which do not provide services in Austria are not covered by the definition of a legal entity according to § 15 of the Federal Law on the Supervision of Securities and thus they are not subject to the extensive regulatory provisions.

#### 4.3.1.2 Company

##### A. Prospectus requirement

As far as no Austrian investors are approached by the Crowdfunding platform, again neither the prospectus requirement according to the Capital Market Act, nor the information obligations (information sheet) according to the Alternative Financing Act are applicable in the situation of an Austrian Crowdfunding platform offering products to foreign investors.

Austrian Crowdfunding platforms approaching Austrian investors and present a company/project from another EU member state on the platform

In this situation an Austrian Crowdfunding platform offers an investment from abroad (e.g. Crowdfunding project from Germany) to Austrian individuals. The main condition for the application of several Austrian regulations is again that the Crowdfunding platform provides

a public offer according to the Capital Market Act and thus, that Austrian individuals are addressed. As already mentioned, the language used and the respective legal system are the most important indicators to assume whether Austrian investors should be approached by an offer.

#### 4.3.1.3 Crowdfunding platform

##### A. Licencing requirements

If the respective project matches the criteria for applying the Alternative Financing Act, the licencing requirements therein have to be met. In particular the Alternative Financing Act refers to the requirements set forth in the Austrian Industrial Code and the Federal Law on the Supervision of Securities. Therefore, if investment products are offered, the Crowdfunding platform needs to obtain a permission according to § 94 Figure 75 of the Austrian Industrial Code, meaning that the operator has to be entitled to provide the business of commercial investment consulting.

If the Crowdfunding platform provides the investor with alternative finance products, a licence to run the business of a securities services provider according to the Federal Law on the Supervision of Securities has to be obtained as well.

Beyond the regime of the Alternative Financing Act, the platform also needs to be licenced for providing the business of commercial investment consulting or securities services provider. Moreover, if the Crowdfunding platform offers an investment, which is an alternative investment fund according to the Alternative Investment Fund Manager Act, the Crowdfunding platform will also need to be licenced as alternative investment fund manager.

##### B. Other financial regulations

As the Crowdfunding platform needs licencing at least under the Austrian Industrial Code or the Federal Law on the Supervision of Securities, the extensive information obligations nominated in these regulations need to be met.

Especially the information obligations, which are provided within the Federal Law on the Supervision of Securities, are very comprehensive. A Crowdfunding platform has to meet these obligations if it provides alternative finance products and has a licence as securities services provider. Beyond information obligations the Federal Law on the Supervision of Securities includes other provisions such as the obligation to implement a risk-management or to conduct adequacy investigations, as well as general organisational requirements (e.g. required recordings).

To summarise, as far as licencing requirements as well as other financial regulations are concerned, Austrian law is fully applicable if an Austrian Crowdfunding platform approaches Austrian investors and presents a company/project from another EU member state on its platform.

#### 4.3.1.4 Company

##### A. Prospectus requirement

As in the above-mentioned situation, in most cases Austrian investors are addressed and the conditions for a public offer according to the Capital Market Act are met. The Alternative Financing Act refers to the definition of the public offer in the Capital Market Act and therefore it is also applicable if the product can be qualified as alternative financing product.

If the respective product meets the requirements provided in the Alternative Financing Act, no prospectus according to the Capital Market Act needs to be published. Only in case that the company issues bonds or stocks and the total amount within twelve months exceeds the volume of EUR 250.000, a simplified prospectus needs to be published. Instead of the prospectus according to Capital Market Act the company has to publish an information sheet pursuant to the Austrian Alternative Financing Information Regulation containing relevant information (i) regarding the company, (ii) on the issued product (iii) regarding the use of the invested amount (iv) on the risk factors which come along with the investment.

If the product cannot be subsumed under the Alternative Financing Act (e.g. total investment amounts over EUR 1.5 million) the company has to publish a prospectus, which is approved by the Financial Market Authority. As drawing up a prospectus is very expensive, most products of Crowdfunding projects are adjusted so that they fall within the scope of the Alternative Financing Act.

##### B. Other financial regulations

Beyond the prospectus regulation, companies may also be subject to information obligations according to the Federal Law on the Supervision of Securities, as the company will have to provide information regarding the product to the Crowdfunding platform. In this context it should be mentioned that the company is liable for the information provided to the Crowdfunding platform.

### 4.4 Impact of EU regulations

#### 4.4.1 Prospectus requirement

In Austria the prospectus requirement is set by the Capital Market Act. The Capital Market Act was comprehensively revised in order to fulfil the requirements according to the European Prospectus Directive (2003/71/EG).

Beyond the required regulations regarding securities, the Capital Market Act is also applicable to investment products. Regarding the prospectus requirement, the main difference between securities and investment products is that the prospectus of investment products are subject to a simplified approval procedure while the prospectus of securities has to be approved by the Financial Market Authority.

The application of the Capital Market Act depends on whether there is a public offer, meaning a notification to the public in any form and distributed in any way, which contains sufficient information on the conditions of the offer, allowing an investor to decide whether to buy or subscribe to the securities or investments, or not.

The Capital Market Act does not apply to products, which are subject to the Alternative Financing Act, which is why for these products no prospectus, but only an information sheet needs to be published.

#### **4.4.2 AIFM-Directive (AIFMD)**

The Alternative Investment Fund Managers Directive (2011/61/EU) has been implemented in Austria by the Alternative Investment Fund Managers Act, which sticks very close to the text of the Directive. As already mentioned above, the Alternative Investment Fund Managers Act may be applicable if companies do not operate the facility itself and the on-going business of the respective project is not handled by the company seeking funding. The subsumption of products under the Alternative Investment Fund Managers Directive to products is very casuistic and varies widely within the European Union, which is the reason why cross border distribution may be difficult.

#### **4.4.3 Markets in Financial Instruments Directive (MiFID)**

The practical significance of the MiFID is very limited in the view of Crowdfunding. In Austria most Crowdfunding platforms offer products, which are based on profit-sharing subordinated loans. As the MiFID is only applicable to transferable securities and since there is no Crowdfunding platform in Austria, which offers these types of products, this ruling is negligible.

The second Markets in Financial Instruments Directive (MiFID II) 2014/65/EU has not been implemented in Austria yet. The first draft of the respective federal acts has already been submitted to the national council for evaluation. Crowdfunding may be affected by extended supervisory rights for the Financial Market Authority, stricter limitations in regard of commissions and further information obligations.

#### **4.4.4 Payment Services Directive (PSD)**

The Payment Services Directive (PSD, 2007/64/EG) was implemented by the Payment Services Act (*ZaDiG*) in Austria. Under certain circumstances a Crowdfunding platform may carry out remittance services according to the Payment Services Act and therefore it needs to apply for a licence.

Such remittance services are carried out by the Crowdfunding platform if the investor pays the investment amount to the operator of the Crowdfunding platform, who then forwards the payment to the company. There is no jurisdiction in Austria according to which a Crowdfunding platform may be regarded as a commercial agent. As already mentioned – in order to avoid licencing requirements – the operator of a Crowdfunding platform could also

use an external provider or partner for processing payments instead of acting as an intermediary himself.

In regard to the second Payment Services Directive (PSD II, EU 2015/2366), which needs to be implemented in Austria at least until January 2018, no legislative proposal has been released yet. For this reason the further legal development is very uncertain.

#### 4.5 Summary

As there is no European Crowdfunding legislation and the legislation in the finance sector (irrespective of whether they are based on legal acts of the European Union or not) is already very concentrated, cross border Crowdfunding will become more and more difficult in all its types. In some cases, due to the applicability of single legal acts and rules the legal situation remains highly unclear even on national level and additional international aspects increase the complexity of cross-border Crowdfunding. Since the member states implement individual regulations – which may simplify national Crowdfunding matters – international Crowdfunding is often made more difficult.

Following legal aspects impede the development of international Crowdfunding aspects:

- Some licences which might be needed to provide international Crowdfunding are only issued if the Crowdfunding platform/company has its registered office or at least a branch in Austria.
- The applicability of Austrian laws is often conditional on addressing Austrian Individuals and therefore the scope of application is very wide. This impedes especially inbound situations as foreign companies and Crowdfunding platforms are subject to information and prospectus obligations.
- Unlike in other European countries (e.g. Germany) there is neither a jurisdiction regarding Crowdfunding nor are there legal statements from the Financial Market Authority to unresolved legal issues, which causes legal uncertainty.
- Dropping the prospectus requirement for Projects with a total investment amount under EUR 1.5 million according to the Alternative Financing Act may impede outbound cross-border Crowdfunding as (i) other countries do not have these exception of the general prospectus requirement or (ii) they provide other benefits which do not match with Austrian laws. Moreover, if the company is obliged to draw up a full prospectus according to the Austrian Capital Market Act, the prospectus has to be adopted to comply with the regulations of other member states of the European Union, which multiplies the costs for drawing up the prospectus.

## 5 Lessons learned from Austrian regulation for a possible harmonised European Crowdfunding Regulation

The implementation of the Alternative Financial Act was accompanied by an increased consumer protection and numerous forms of relief for Crowdfunding platforms and companies,

which are using Crowdfunding to finance their business. Nevertheless, there is still a vast spectrum for further legal development.

### 5.1 Role model (“dos”)

For developing harmonised European legislation, the following aspects may be considered as a indicatory role model:

- Abolition of the prospectus requirement for Crowdfunding projects, which do not exceed a total Investment sum of EUR 1.5 million. The implementation of this benefit brought legal certainty on the question of whether a prospectus according to the Capital Market Act needs to be published and moreover lead to a financial relief for companies as drawing up a prospectus is very expensive. Especially start-ups often cannot afford drawing up a prospectus.
- The information sheet leads to more consumer protection since the consumer does not get such complex information as it is provided in a full prospectus in accordance with the Capital Market Act.
- By providing the opportunity for professional investors to invest in the project with an unlimited amount (i) capital thresholds may be achieved more easily and (ii) Crowdfunding becomes more attractive for professional investors.

### 5.2 Aspects that should be avoided (“don'ts”)

- The financing threshold for non-professional investors is set with a total amount of EUR 5.000 for each project per year. Although there are exceptions from this threshold (if the investor informs the issuer that the investment does not exceed twice of his monthly net-income calculated over the last twelve months or if he informs the issuer that the investment does not exceed 10 % of his financial assets), it should be increased while maintaining the aforementioned exceptions.
- Companies, which have a licence according to the Federal Law on Banking, the Capital Market Act, the Federal Law on the Supervision of Securities, the Federal Law on Alternative Investment Fund Managers, the Payment Services Act, the Insurance Supervision Act or the E-Money Act 2010 cannot participate from the benefits of the Alternative Financing Act. As the Alternative Financing Act is not applicable to those companies they may not mix different forms of financing.

## 6 Conclusion

Summed up, it can be stated that the national legislator made a step into the right direction by recognising the regulatory gap, which was a consequence of the increasing interest in Crowdfunding. This resulted in the implementation of the Alternative Financing Act, which brings a number benefits for Crowdfunding on national level.

Also in other European countries Crowdfunding develops rapidly and the national legislator counteracts this development with individual legislation in each member state. This

leads to a fragmentation of the legislation on Crowdfunding in Europe and makes international Crowdfunding very difficult even within the European Union.

From an Austrian perspective, the following European legislative measures should be taken in order to harmonise Crowdfunding within the European Union:

- standardisation of linguistic terms used within the financial market; especially respectively Crowdfunding;
- implementation of a council regulation or at least a directive, which eliminates the prospectus requirement in all member states of the European Union and replace this obligation with issuing a standardised information sheet equally accepted by all member states. At least total funding amounts and thresholds for the investment of individual persons should be harmonised in order to ensure cross-border Crowdfunding;
- clarification of which products may be provided by foreign Crowdfunding platforms, which already have a licence for the business of securities services providers or investment firms in their home state, under the freedom of providing services.

## 7 Summary – Crowdfunding regulation

| Country  | Austria  |
|--|--|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulations</b> | <ul style="list-style-type: none"> <li>• First national Crowdfunding regulation, the Alternative Financing Act was implemented as of 1st September 2015.</li> <li>• Situation regarding the allowance of issuing subordinated loans (not profit-participating) to customers remains unclear as they may provide a severe disadvantage.</li> <li>• General situation regarding general licencing requirements of Crowdfunding became clearer by implementing the Alternative Financing Act.</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>                             |  |
| <b>General regulation</b>  | <ul style="list-style-type: none"> <li>• If the Crowdfunding platform provides alternative finance products, a licence as securities service provider according to the Federal Law on the Supervision of Securities is mandatory.</li> <li>• If providing investment products, a licence for providing the business of commercial investment consulting according to Austrian Industrial Code is necessary.</li> <li>• The most popular form of Crowdfunding is issuing subordinated loans, which are usually qualified as investment products.</li> </ul>                                 |
| <b>Prospectus requirement</b>  | <ul style="list-style-type: none"> <li>• No prospectus requirement for alternative financing products, which do not exceed a total investment amount of EUR 1.5 million.</li> <li>• Simplified prospectus requirement for alternative financing products with a total investment amount between EUR 1.5 million and EUR 5 million and if bonds or stocks are issued with a total amount exceeding EUR 250.000 per year.</li> <li>• Full prospectus requirement for all other issued securities and investment products, which are not covered by the Alternative Financing Act.</li> </ul> |
| <b>AIFMD-regulation</b>  | <ul style="list-style-type: none"> <li>• Only applicable if the project company does not carry out the on-going business of the facility; meaning outsourcing of operational activities.</li> <li>• Only little practical relevance for Crowdfunding as most companies try to avoid/bypass the application of the AIFMD regime because of its extensive regulations and the requirement of a licence from the Financial Market Authority.</li> </ul>   |
| <b>Payment service regulation</b>  | <ul style="list-style-type: none"> <li>• Forwarding money collected from investors to the company may constitute money remittance.</li> <li>• A licence from the Financial Market Authority may be required.</li> <li>• Unclear situation whether this service may be covered by the exception for commercial agents.</li> <li>• Corporation with a payment service provider/bank is therefore recommended.</li> </ul>   |

|   |  |
|---|--|
| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• Consumer Credit Regulation (Verbraucherkreditgesetz – VKrG).</li> <li>• Consumer Protection Act (Konsumentenschutzgesetz – KSchG).</li> </ul>   |
| <p><b>Regulatory barriers</b></p>           |  |
| <p><b>Inbound</b></p>                       | <p><b>Foreign Crowdfunding platform addressing Austrian investors</b></p> <ul style="list-style-type: none"> <li>• Most Austrian regulatory laws are applicable if Austrian investors are addressed by a public offer according to the Capital Market Act.</li> </ul> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• Alternative finance products <ul style="list-style-type: none"> <li>– Crowdfunding platforms, which have a licence as CRR-credit institution from another EU member state do not have to apply for an additional licence.</li> <li>– If there is no licence from a member state, the Crowdfunding platform has to apply for a licence in Austria.</li> </ul> </li> <li>• Investment products <ul style="list-style-type: none"> <li>– Licence for conducting the business of commercial investment consulting in Austria is mandatory.</li> <li>– If conducted only temporary and occasionally, the activity has to be indicated to the local trade authority.</li> <li>– If conducted permanently, the Crowdfunding platform needs to be licenced under the freedom to provide services by submitting the respective certificates of competence to the trade authority.</li> </ul> </li> </ul> <p><i>Foreign company / project</i></p> <ul style="list-style-type: none"> <li>• Prospectus requirement according to Capital Market Act. <ul style="list-style-type: none"> <li>– General rule determines that issuing securities or investment products requires a full prospectus according to the Capital Market Act.</li> </ul> </li> <li>• Alternative Financing Act <ul style="list-style-type: none"> <li>– If the product issued is covered by the Alternative Finance Act, drawing up a prospectus is not required.</li> <li>– Investors needs to be provided with a standardised information sheet which contains information on the product and the company.</li> </ul> </li> </ul> <p><b>Foreign Crowdfunding platform addressing Austrian companies / projects</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• Alternative finance products <ul style="list-style-type: none"> <li>– Licencing as securities service provider according to the Industrial Code is not necessary since the service is not provided in Austria.</li> </ul> </li> <li>• Investment products</li> </ul> |

|                        |   |
|------------------------|---|
|                        | <ul style="list-style-type: none"> <li>- Business of commercial investment consulting is not conducted in Austria and therefore licencing requirements according to the Industrial Code do not apply.</li> </ul> <p><i>Austrian company/project</i></p> <ul style="list-style-type: none"> <li>• As Austrian investors should not be approached, the prospectus requirement as well as other obligations under the Alternative Financing Act do not apply.</li> <li>• A disclaimer, stating that the Austrian market is excluded from the offer should be provided to ensure that Austrian regulatory laws are not applicable.</li> </ul>   |
| <p><b>Outbound</b></p> | <p><b>Austrian Crowdfunding platform addressing foreign investors</b></p> <ul style="list-style-type: none"> <li>• Only foreign investors should be approached in this situation</li> </ul> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• Alternative Finance products <ul style="list-style-type: none"> <li>- Licencing as securities service provider according to the Industrial Code is not necessary since the service is not provided in Austria.</li> </ul> </li> <li>• Investment products <ul style="list-style-type: none"> <li>- Business of Commercial Investment Consulting is not conducted in Austria and therefore licencing requirements according to the Industrial Code do not apply.</li> </ul> </li> </ul> <p><i>Austrian company/project</i></p> <ul style="list-style-type: none"> <li>• As the offer is not addressed to Austrian investors, there is no public offer according to the Capital Market Act and therefore the prospectus requirement according to Capital Market Act and the Alternative Financing Act is not applicable.</li> <li>• To ensure that Austrian investors are excluded from the offer, a disclaimer is recommended.</li> </ul> <p><b>Austrian Crowdfunding platform addresses foreign companies/projects</b></p> <ul style="list-style-type: none"> <li>• As the offer addresses Austrian investors, Austrian regulatory requirements apply to their full extent.</li> </ul> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• Alternative finance products <ul style="list-style-type: none"> <li>- Crowdfunding platforms need a licence according to the Federal Law on the Supervision of Securities, in order to be allowed to act as a securities services provider.</li> <li>- Licence is granted by the Austrian Financial Market Authority.</li> </ul> </li> <li>• Investment products <ul style="list-style-type: none"> <li>- The business of commercial investment consulting is conducted in Austria.</li> </ul> </li> </ul> |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>- Crowdfunding platforms need a licence according to the Industrial Code.</li> <li>- The operator of the platform has to meet several regulatory requirements and he is obliged to prove his qualification before conducting the business.</li> </ul> <p><i>Foreign company/project</i></p> <ul style="list-style-type: none"> <li>• Prospectus requirements           <ul style="list-style-type: none"> <li>- Requirements according to Capital Market Act (if applicable) and information obligations according to the Alternative Financing Act have to be met.</li> <li>- General rule determines that issuing securities or investment products requires a full prospectus according to the Capital Market Act.</li> </ul> </li> <li>• Alternative Financing Act           <ul style="list-style-type: none"> <li>- If the product issued is covered by the Alternative Finance Act, drawing up a prospectus is not required.</li> <li>- Investors needs to be provided with a standardised information sheet which contains information on the product and the company.</li> </ul> </li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | <ul style="list-style-type: none"> <li>• Most Crowdfunding platforms act under the regime of the Alternative Financing Act; no prospectus requirement applies if the total investment amount does not exceed EUR 1.5 million.</li> <li>• Only minor practical relevance.</li> </ul>  |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• The Alternative Investment Fund Manager Act may be applicable if project companies do not operate the facility themselves and the on-going business of the respective project is not handled by the company seeking funding.</li> <li>• Crowdfunding platforms try to avoid application of the AIFMD.</li> <li>• Insignificant practical relevance for Crowdfunding in Austria.</li> </ul>  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• Only applicable to transferable securities.</li> <li>• Does not have any practical relevance for Crowdfunding in Austria.</li> </ul>  |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• Activity of Crowdfunding platform may be qualified as remittance service and therefore a licence according to Payment Services Act is required.</li> <li>• Unclear whether Crowdfunding may be subsumed under the exception for commercial agents.</li> <li>• External payment service provider should be used to elude licencing requirements.</li> </ul>  |

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# Belgium

## 1 Recent developments in the market of Crowdfunding in Belgium

Over the last three years there were the following significant developments in Belgium regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Early Crowdfunding in Belgium was limited by the low prospectus exemption threshold of EUR 100.000. In addition, issues surrounding the interpretation of definitions of various financial services and the banking monopoly further limited the potential of (equity) Crowdfunding.

To this day pure equity Crowdfunding involving the issue of “securities” in Belgium is limited. Only one player which is a licensed financial service firm is in a position to promote direct equity participation. Bonds have also been offered by Platforms but in collaboration with licensed financial institutions.

“Equity” Crowdfunding is rather organized through the issue of (subordinated) profit participating notes (i.e., investment instruments). For the purpose of this paper, we qualify the issue of these profit participating notes as falling within equity Crowdfunding, although this is open to discussions.

From 2014 onwards, Crowdfunding started to get some traction in Belgium with the increase of the prospectus exemption for Crowdfunding purposes to issues up to EUR 300.000.

Shortly thereafter, tax initiatives benefiting crowdfunders were put in place by the government. In May 2017 already a few projects promoted by licensed Platforms had benefited from the Crowdfunding Tax Shelter. This is the case for both Projects under the equity or the lending model.

This said this Prospectus Exemption threshold is low compared to some other European countries. In consequence some Platforms have developed systems of co-investment of the crowd alongside professionals. They almost systematically issue a (simplified) prospectus.

By now the Belgian market is populated with a few Platforms (both MiFID or not MiFID licensed) offering investments on a regular basis. Indeed, some financial institutions have put in place their own Platforms, other financial institutions closely cooperate with existing Platforms and even advertise Crowdfunding as an alternative to financing by the bank!

The game changer is the implementation in 2017 of a Crowdfunding Platform Act (dating from end 2016) enabling the licensing of Crowdfunding Platforms and activating the benefits of the Crowdfunding Tax Shelter. This act also takes (to some extent) cross border activities into account. The FSMA has now licensed several Platforms and is (timidly) officially opening the market to foreign Platforms.

This said the Belgian market remains relatively modest. According to a survey by Look & Fin, Crowdfunding for entrepreneurs (across the equity or lending model) was estimated at EUR 11 million in 2016 in Belgium

## **1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

One of the most active Platforms in Belgium, which has also extended its activities to France, is a lending based Platform. There are no major hurdles to lending based Crowdfunding, other than these deriving from the threshold of the Prospectus Act. Lending to start-ups can now also benefit from limited tax exemptions.

Peer-to-peer lending: Until recently there was no peer-to-peer lending in Belgium. The main hurdle is the strict banking monopoly which only authorizes credit institutions (and the like) to collect deposits and other repayable funds from the public in Belgium. Pure peer-to-peer lending is thus currently not possible in Belgium.

A first timid peer-to-peer initiative has been launched recently (2017). However, it is limited to lending to the crowd by pooled investors as direct peer-to-peer lending is not permitted. In other words, an investment vehicle is put between the lenders and the financiers. That investment vehicle issues profit participating notes of different categories in correlation to the risk of the underlying loans.

## **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

One of the first Crowdfunding initiatives in Europe was launched in Belgium. It was specifically geared towards the music industry. The Donations or Rewards Models is now widely used in Belgium to fund all kind of non-for-profit, social, creative or even personal needs and initiatives.

There are a wide variety of Platforms offering rewards based Crowdfunding. The model is also more and more used by companies to benefit from publicity. The beer sector, for instance, is an avid user of the model: a brewers' needs for a beer tunnel was enthusiastically supported by the crowd and a micro brewer developed its image around crowdfunded and crowd-selected beers.

## **1.4 Real Estate Crowdfunding / Renewable Crowdfunding**

### **1.4.1 Real Estate**

Although there are real estate Crowdfunding initiatives in Belgium, they are not yet as widespread as in other countries. This said with the announced entry of several French Platforms on the Belgian market one except that this sector will gain market shares. French Platforms looking into the Belgian market predominantly fund real estate projects. Real estate platforms tend to use lending based Crowdfunding. French platforms tend to issue

bonds which are tradeable securities. Recently a Belgian platform (*Beebonds*) has done the same, with the assistance of financial institutions in order to fund a real estate fund.

### 1.4.2 RES Projects

Real estate Platforms must be seen together with RES Projects Platforms which gain in popularity. Some new Platforms specialize in RES projects. One has recently been licensed by the FSMA (Ecco nova) RES projects are also financed through the use of cooperative companies which can easily issue new shares. In practice most RES projects are funded by local citizen cooperatives which are grouped in the Rescoop network. Major utility companies also tend to set-up cooperatives to cooperate with the crowd on specific local RES projects (usually wind turbines). Ecopower CVBA, an upcoming licensed utility company, active both in Flanders and Wallonia, mostly but not solely in wind turbines, is also organized as a cooperative to allow the public to have a direct say and co-invest in RES projects.

## 1.5 International approach

Belgium is traditionally an open economy, although regulatory hurdles have slowed down cross border activities of Platforms.

With the adoption of the Crowdfunding Platform Act it is anticipated that French and Dutch Platforms will actively enter the Belgian Market. The Act regulates the access to the Belgian market for foreign Platforms and also the conditions for a Belgian licensed Platform to take initiatives abroad.

Other foreign US or UK Platforms have had a more discrete “appeal” in Belgium since a few years.

## 2 Recent developments regarding Crowdfunding regulation in Belgium

### 2.1 Overview

In April 2014, the Belgian Government took a first Crowdfunding legislative initiative which aimed at opening the Crowdfunding market (for the purpose of this article referred to as the “Crowdfunding Act”). The main feature of that Act was to increase the threshold of the so called “prospectus exemption”, thereby making it possible to appeal to the crowd for the financing of projects of up to EUR 300.000 EUR and EUR 1.000 per investor without an obligation to issue a prospectus (the “Crowdfunding Exemption”, as further defined below).

One year later, in April 2015 the government acknowledges that the absence of tax incentives was a deterrent to Crowdfunding. The Belgian Government introduced tax incentives specifically geared towards Crowdfunding.

The “Tax-Shelter” for Crowdfunding enacted on 10 August 2015, but entering into force retroactively on 1 July 2015 provides for tax incentives for both equity-based and lending-based Crowdfunding schemes (the “Crowdfunding Tax Shelter Act” as further defined below).

Finally, the Act of 18 December 2016 entering into force in February 2017 organizes a full framework for Crowdfunding (the “Crowdfunding Platform Act” as further defined below). The act sets-out the conditions for licensing Crowdfunding Platforms, it further defines the alternative finance services that such Platforms can offer, it activates the Tax Shelter introduced by the law of August 2015 and increases the thresholds of the Crowdfunding exemption for licensed Crowdfunding Platforms in the Prospectus law to EUR 300.000 per project and EUR 5.000 per investor (the “Crowdfunding Platform Exemption”, as further defined below).

## **2.2 First Crowdfunding initiative: amended prospectus requirements, April 2014**

Before May 2014, there was no specific legislation addressing Crowdfunding issues.

In March 2014, the Belgian Finance Minister announced a Crowdfunding initiative addressing mainly, but not only, the public offering thresholds. The initiative was said to address “both the legal burdens for promoters and investor protection”.

The Belgian Act of 25 April 2014 (which addresses various issues, amongst which Crowdfunding) included provisions amending the Prospectus Act (hereafter, the “Crowdfunding Act”). The Prospectus Act is an act of 16 June 2006 on public offers of investments instruments, amended by the Act of 17 July 2013.

The Crowdfunding Act that came into force on 17 May 2014, introduces, among others, a prospectus exemption and provide for better crowd-investor protection.

The Crowdfunding Act amended article 18 of the Prospectus Act and increased the ceiling to benefit from the exemption from the obligation to issue a prospectus from EUR 100.000 to EUR 300.000. To protect investors, the exemption limits the investor’s investment to a maximum of EUR 1.000 per project, in the absence of prospectus. These two conditions are cumulative. Additionally, all documents concerning the offer must mention the total value offered as well as the maximum subscription amount per investor (the “Crowdfunding Exemption”).

In addition, the Act of 25 July 2014 exempts persons or institutions carrying out intermediation for public offerings falling within the scope of the Crowdfunding Exemption, from the obligation pursuant to Article 56 of the Prospectus Act, to be licensed as a credit institution or investment firm. This provision was crucial (but has been amended later). Article 13 of the Prospectus Act defines intermediation as any action towards investors, including temporary or incidental, in every capacity, in the placement of investment instruments on behalf of the offeror or issuer, against compensation or any benefit in kind, directly or indirectly provided by the offeror or issuer.

### 2.3 Tax Incentives for Crowdfunding, August 2015

The Belgian Federal Government introduced in 2015 (the “Crowdfunding Tax Shelter Act”) two types of tax incentives to encourage investment in start-ups. The first one consists of a personal income tax reduction for equity investments in start-ups (for equity based Crowdfunding). The second one is a tax exemption on interests of loans to start-ups (for lending based Crowdfunding).

#### 2.4 Tax shelter for equity investments

For investments in start-ups that qualify as a “small company” and for investments in starter funds, the personal income tax reduction amounts to 30% of a maximum investment of EUR 100.000 per investor per taxable period. A tax reduction of 45% is granted for investments in a micro-undertaking as defined in EU accounting directive 2013/34.

The total amount of the investment qualifying for a tax exemption may not exceed EUR 250.000 per start-up. This threshold has been criticized as it is not in line with the above-mentioned prospectus exemption threshold which is set at EUR 300.000.

Another fiercely criticized (anti-abuse) limitation is that the management of the start-up cannot benefit from the exemption. This discourages management of making equity investment in its own company! Indirect investment by the management, through management companies, is also excluded.

The Act sets a number of additional conditions to qualify for the tax exemptions:

- A. The exemption is only available for investment in qualifying companies, not in business held by private individuals;
- B. The shares of the small company must be registered shares;
- C. The shares must be acquired at incorporation or pursuant to a capital increase;
- D. They must be held at least 4 years (safe transfer due to decease of the investor). In case of early transfer, the benefit of the tax reduction is not lost but proportionally reduced to the period of ownership vs. the 48 months’ period;
- E. Investments in kind are excluded from the scope of the tax shelter exemption. The capital of these shares must be fully paid up;
- F. Some companies are excluded from the scope of the tax shelter (companies in reorganization, listed companies, finance and investment firms, real estate companies, etc.);
- G. The funds invested cannot be used for the distribution of dividends, for acquiring financial assets or onwards lending;
- H. The tax reduction is further capped to 30 % of the shares of the company per investor. If the investor as a higher stake in the company, he will not benefit from the exemption above for any shares held above the 30% cap.

The tax reduction is only available to private individuals (investors,) not to companies. An individual may benefit, through various qualifying investment of up to EUR 100.000 tax reduction per taxable period.

“Starter funds” means funds that invest at least 80 % of their assets in starters and are regulated by the FSMA (i.e., the Belgian Financial Services and Market Authority).

Only shares issued by small companies qualify. These are companies as defined by article 15 of the Belgian Companies Code. The company must be small in the year of issuance when the investors benefit from the tax exemption. Small companies are considered qualifying start-ups if they are no older than 4 years. They must be registered in the EEE.

The 45% reduction is available to the smallest companies, so -called “micro undertakings”. This is an undertaking that has (i) maximum 10 employees, (ii) a turnover of maximum EUR 700.000, and (iii) a total balance sheet value not exceeding EUR 350.000. Small and medium sized undertakings benefiting from the 30% reduction are undertakings which have (i) maximum 50 employees, (ii) a turnover of maximum EUR 40.000.000, and (iii) a total balance sheet value not exceeding EUR 20.000.000.

#### **2.4.1 Withholding tax exemption on loans**

Individuals who provide a loan to a start-up (as defined above) will benefit from a complete withholding tax exemption on interests produced by the first tranche of maximum EUR 15.000 of that loan. The maximum exempted amount is to be understood per taxpayer per year. The withholding tax rate on interest of most loans in Belgium is of 27%.

The (exempted tranche of the) loan must have a maturity of at least 4 years. Unlike what is the case for the tax shelter for equity investments, both start-up companies and individuals can benefit from exempted loans as long as they meet the criteria of a small company (as defined above). These companies may not be registered for more than 48 months at the Crossroads Bank for Enterprises.

Also unlike what is the case for the tax shelter for equity investments, managers granting a loan to their own start-up may benefit from the withholding tax exemption.

The loan must be provided through a regulated Crowdfunding Platform. The Act activating the tax shelter provisions through the regulation of Crowdfunding Platforms was only to be adopted in December 2016, thereby freezing the withholding tax exemption in the interim period.

### **2.5 The Act regulating the framework for Crowdfunding Platforms, December 2016**

The Act of 18 December 2016 regulating Crowdfunding Platforms, sets-out a comprehensive framework for Crowdfunding (the “Crowdfunding Platform Act”).

### 2.5.1 Scope

The scope of that Act is limited to equity and lending based-Crowdfunding. Are out of scope: a) rewards based Crowdfunding; b) merely advertising of Crowdfunding offers (e.g. some social media or newspapers); c) offers addressed to less than 150 persons or to legal entities and to qualified investors.

Alternative Finance Services providers are defined as the providers who offer these services on a professional basis in Belgium and are not (MiFID) licensed financial services providers. Alternative Finance Services consist of commercializing, through an internet Platform, investment instruments issued by entrepreneurs, start-up funds or financing vehicles, whether in the context of a public offering or not, to the crowd. Alternative Finance Services providers may not provide regulated investments services, except for providing investment advice and receiving and passing on investment orders. Thus, they cannot offer services relating to the placing of financial instruments, with or without firm commitments.

### 2.5.2 Licensing of Crowdfunding Platforms

An active Alternative Services Provider (“Crowdfunding Platform” or “Platform”) must obtain a license from the FSMA.

The Platform must offer these services through a commercial company with central management located in Belgium (except for foreign licensed EEA Platforms). The names of the controlling persons must be disclosed and they must meet fit and proper requirements. Directors must be natural persons and the management of the Platform must be in the hands of at least two persons.

The Platform must put in place an appropriate organization adapted to the nature, scale and complexity of its activities to guarantee its continuity. The same applies to its IT structure. A civil liability insurance with minimum coverage set by law is also mandatory.

These conditions must be met at all times and the FSMA must be notified of any changes.

Platforms may not receive or keep funds or financial products from their clients or be debtor of their clients and they may not be holder of a mandate on their clients’ accounts. Financial flux cannot be managed by a Platform

Licensed Platforms pay an annual fee to the FSMA.

Crowdfunding Platforms may develop other commercial activities which do not harm their reputation. For these they must put in place a distinct internal organization and separate accounting.

In April 2017, five Platforms were licensed under the interim regime put in place by the Crowdfunding Platform Act for Platforms active prior to adoption of that Act (Crofun, Ecco Nova, Ekigroup, Lookandfin, MyMicro invest). Ekigroup was barred shortly thereafter. Additionally, two regulated investment services firm have notified the FSMA that they will also offer alternative investment services in Belgium (KBC securities, and Hands-on BV – a

company from the Netherlands which will also be active in Belgium). Ecco nova focuses specifically on RES-Projects.

### 2.5.3 Mini MiFID

The Crowdfunding Platform Act imposes that Platforms request information from their clients to assess their financial knowledge. A warning must be issued to clients not demonstrating sufficient financial knowledge. A client file must be opened and all relevant information kept for five years.

The Platforms must inform investors of the identity and status of the Platform, the cost of the alternative funding service, the conflict of interests' policy, information on potential tax advantages, the principal characteristics of the offered investment instruments etc.

### 2.5.4 Financing vehicles

The Crowdfunding Platform Act defines a new entity, the financing vehicles, which in practice were already often used by Crowdfunding Platforms to bundle the crowd. A financing vehicle is an issuer of investment instruments (but not an UCIT) whose activity exclusively consist of taking participations or providing loans to one or more issuers-entrepreneurs and which is financed by investors, who decide independently in which issuers-entrepreneurs they wish to invest by way of an investment in the vehicle, it being understood that the profit generated by their investment can only be determined by the profit offered by the issuer-entrepreneur for the participation taken or loan offered by the vehicle ("Financing Vehicle").

Special rules and obligations apply to these financing vehicles investing in issuers-entrepreneurs. They must be managed in the interest of the crowd. The crowd must be informed of the links existing between the Platform and the Financing Vehicle and of potential conflicts of interests. The Financing Vehicle annually discloses the costs related to its use. Special compartmented accounting per project must be put in place.

### 2.5.5 Increased prospectus exemption

The Crowdfunding Platform Act increased the threshold of the exemption to issue a prospectus for public offers of investments instruments. Such offers do not require a prospectus if the offer is for a total consideration of less than EUR 300.000, with a maximum investment of EUR 5.000 per person and per project (the "Crowdfunding Platform Exemption").

To benefit from that exemption all documents must mention these maximums. The instruments must be distributed by licensed Platforms or investment firms. Some more risky investment instruments such as options or contracts for difference are excluded from the scope of the exemption.

Issuers who do not meet these conditions may still benefit from the 2014 Crowdfunding Exemption setting the cap at EUR 1.000 per investor per project (instead of EUR 5.000).

### 2.5.6 Regime applicable to EEA Platforms

Platforms licensed in the EEA may obtain access to the Belgian market if they are licensed in their home country to offer similar services and obtain agreement from the FSMA. Fit a proper requirements apply to management of a Belgian branch, if any. Licensed investment firms of other member states can directly offer their services in Belgium subject to registering with the FSMA in order to provide alternative investment services.

A French platform *Raizers* has already been provisionally licensed under the regime put in place for EEA Platforms.

## 3 Current Regulation of Crowdfunding in Belgium

### 3.1 License as an investment service firm

#### 3.1.1 Equity Model / Lending Model

Licensed Platforms may not provide regulated investments services, except for providing investment advice and receiving and passing on investment orders. Thus, they cannot offer services relating to the placing of financial instruments, with or without firm commitments.

The new Investment Services Act of 25 April 2016 (replacing the Act of 6 April 1995) regulating investment firms, defines “investment services”, inter alia, as the reception and transmission of orders in relation to one or more financial instruments, the execution of orders on behalf of clients, investment advice and the placing of financial instruments with or without a firm commitment basis.

“Financial Instruments” (as defined by an Act of 2002 on the supervision of the financial sector) include securities such as shares, bonds and other debt instruments. The definition of financial instrument used for the regulation of investment firms is narrower than that of “investment instruments” under the Prospectus Act, Investment instruments encompasses all types of instruments (including debt instruments) permitting financial investments, whatever the nature of the underlying assets.

To avoid that MiFID obligations would apply to Platforms, the FSMA clearly reviewed and narrowed the definition of placement services.

The FSMA had already made a first attempt to define the term in its 2004 board report. It specified that the following factors are indicative of a regulated “placement service” being offered:

- the existence of an agreement (whether written or oral) between the issuer and the financial intermediary whereby the intermediary acts on behalf of the issuer
- a consideration paid by the intermediary to the issuer.

The FSMA further indicated that these indicators are usually accompanied by the financial intermediary providing marketing and advertising services, and “door-to-door” selling to, or cold calling of, potential investors.

In its 2015 annual report, the FSMA further clarifies the term putting the emphasis on the fact that a placement service entails assisting the client during the entire process, including managing financial flows. This allows differentiation with permitted services such as receiving and transmitting orders.

The Crowdfunding Platform Act further amended the notion of financial services monopoly in favor of financial service firms provided for in the Prospectus Act (article 56). It now specifies that Platforms may commercialize investment instrument. The mere commercialization of investment instruments is not considered a placement service. In parallel, the Crowdfunding Platform Act suppressed an exemption introduced in 2014 providing that persons or institutions carrying out intermediation for public offers falling within the scope of the “Crowdfunding Exemption” are exempted from the obligation to be licensed as a credit institution or investment firm.

However, if Platforms wish to offer (non-exempted) financial services regarding financial instruments then they will require MiFID licensing.

The FSMA has further pointed out that Crowdfunding Platforms organizing a market for the financial instruments offered through the Platform could be considered a multilateral trading facility, which also requires a license.

### **3.1.2 Donations or Rewards Model**

The Donation and Rewards model is subject to very few regulations as it does not fall within the scope of most financial regulations.

## **3.2 Bank monopoly for the collection of public savings**

In principle, only credit institutions (and the like) are authorized to collect deposits and other repayable funds from the public in Belgium (section 68bis Prospectus Act, previously regulated under the Banking Act).

The Crowdfunding Platform Act further confirms that Crowdfunding Platforms may not receive or hold monies, financial products from their clients or be indebted to their clients (article 17).

In practice this means that the funds must be collected by either the issuer or payment institutions licensed to manage payments. Adequate protection must be put in place to guarantee that the collected funds cannot be used for any other purpose than either reimbursing the investor (if the fundraising venture fails) or investing in the project (in case of success).

The banking monopoly can also be circumvented by issuers and financing vehicles' either by collecting non-repayable funds (i.e., by collecting the funds at the end, once the funding operation's success is already secure and it is certain that no funds need to be repaid) or by issuing a prospectus, as the Prospectus Act provides for an exemption to the banking monopoly.

### 3.3 Prospectus requirements

#### 3.3.1 Equity Model / Lending Model

The Prospectus Act defines a public offer as a communication to persons in any form and by any means, presenting sufficient information on the terms of the offer and the investment instruments offered so as to enable an investor to decide to purchase or subscribe to these investment instruments, and which is made by the person who is in a position to issue or transfer the investment instruments or by a person who acts for the account of the aforementioned person.

##### (1) General exemptions

The Prospectus Act requires the publication of a prospectus and the approval by the FSMA for offers of investment instruments when the total investment offered is equal or higher than EUR 100.000.

An offer of investment instruments does not qualify as a public offer, if:

- A. it is addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors; or
- B. the total consideration per investor and per offer is more than EUR 100.000, calculated over a period of 12 months.

##### (2) Crowdfunding Exemption

As seen above, the new Crowdfunding Exemption introduced in the Prospectus Act provides that the following operations do not qualify as a public offer of investment instruments, if they are offers:

- A. for a total consideration of less than EUR 300.000;
- B. with a maximum investment of EUR 1.000 per person and per project.

All documents concerning the offer must indicate the total value offered as well as the maximum subscription amount per investor.

The Crowdfunding Exemption is an addition to the Prospectus Act . In consequence, the old exemption, i.e., concerning offers for less than EUR 100.000 is still in place. Under that exemption the investment per person is not capped at EUR 1.000.

In order to benefit from the Crowdfunding Exemption, the Prospectus Act provides that the offeror is required to demonstrate to the FSMA that the public offer complies with the conditions of exemption and this PRIOR to the offer. For continuous offers, the offeror must demonstrate this each 12 month. The FSMA has put a notification procedure in place.

The FSMA recommends to issuers benefiting from the prospectus exemptions to point out to the public that the offer takes place without the publication of a prospectus and also to stress the risks associated with the investment instruments offered.

### **(3) Crowdfunding Platform Exemption**

The Crowdfunding Platform Act of 2016 introduced a second (above discussed) Crowdfunding Platform Exemption.

Offers through a licensed Platform or investment firm do not require a prospectus for offers for a total consideration of less than EUR 300.000, with a maximum investment of EUR 5.000 per person and per project.

### **(4) Cooperatives**

Note that cooperatives in Belgium benefit from a distinct prospectus exemption under the Prospectus Act. Most crowdfunded RES Projects in Belgium are structured through a cooperative company.

To benefit from that exemption, the cooperative must register with the National Counsel of Cooperatives, which requires fulfilling certain strict conditions.

The offer of securities from these registered cooperatives is exempted from the prospectus obligation provided the total offer is of less than EUR 5.000.000 and for those cooperative companies which aim to offer an economic and social advantage for the private benefit of their shareholders, the offer must be limited so that a shareholder can, as a result of the offer, only hold shares up to a nominal value of maximum EUR 5.000.

RES cooperatives in Belgium have either issued a prospectus or used the above-mentioned exemption. The FSMA has reviewed multiple prospectus files from RES cooperatives and made a special mention and comment in relation thereto in its 2011 annual report. The cooperative exemption regime was further modified by the Act of 25 April 2014. The FSMA issued a communication in respect to these changes and prior review of the exempted nature of these offers.

It is worthwhile to mention, that aside of the exemption of the prospectus requirement some social regulated cooperative companies can provide a tax advantage to investors. Subject to certain conditions such as to pay out a dividend of maximum 6% (art. 6 of the Royal Decree of 8 January 1962), dividends up to EUR 190 per shareholder – are exempted from withholding tax (for Belgian taxpayers).

Moreover, Belgian taxpayers benefit from a 5% reduction of its investment in the cooperative's shares. Conditions for such reduction is that the investment must be of at least EUR 437.50 (in 2015), the tax reduction was capped at EUR 320 in 2015 (for an investment of EUR 6437.50), the shares must be registered and must remain in possession of the investor for a continuous period of at least 5 years (except in case of death).

### 3.3.2 Rewards Model

Unless some rewards would qualify as investment instruments, which is usually not the case, the Prospectus Act does not apply to rewards based Crowdfunding.

## 3.4 AIFMD regime

### 3.4.1 Definition of AIF

Belgium implemented the European Alternative Investment Fund Managers Directive (“AIFMD”), by the Act on Alternative Investment Funds Managers of 19 April 2014 (*Wet betreffende de Alternatieve Instellingen voor Collectieve belegging en hun beheerders* – “the “AIFM Act”) following its approval by the Parliament on 3 April 2014.

The AIFM Act came into force on 27 June 2014. The AIFM Act mostly implements the directive. However, it imposes more stringent rules on the managers of alternative investment funds marketed to the public.

An AIF (alternative undertaking for collective investment (“*alternatieve instelling voor collectieve belegging*” / “*organismes de placement collectif alternatif*”) is defined as an undertaking for collective investment, including investment compartments thereof, which (i) raises capital from a number of investors with a view to investing it in accordance with a defined investment policy and (ii) is not subject to the UCITS legislation implementing Directive 2009/65/EC.

### 3.4.2 Scope

The AIFM Act applies to all Belgian funds which qualify as AIFs, such as:

- **Real estate closed-ended investment funds (*sicafis* / *vastgoedbevaks*):**  
Pursuant to the Act of 12 May 2014, Belgian real estate closed-ended investment funds (which are subject to the Act of 3 August 2012) had the possibility to remain outside the scope of the AIFM Act if they opted for the status of regulated real estate company (*société immobilière réglementée* / *gereguleerde vastgoedvennootschap*). However, the regulated real estate company is not an investment fund but a listed company available for retail investors with a long-term corporate strategy. To fill this gap, a solid but flexible, legal, regulatory and tax framework for institutional real estate investment funds was set up by the Programme Act (II) of 3 August 2016 which introduced a new Belgian Real Estate Investment Fund (“**REIF**” - “*Fonds d’investissement immobilier spécialisé*” - “*FIIS*” / “*gespecialiseerd vastgoedbeleggingsfonds*” – “*GVBF*”). The Royal Decree implementing the REIF regime has been published in the Belgian Official Gazette of 18 November 2016 and has entered into force on 28 November 2016.

The FIIS regime is optional and only applies to AIFs which have opted for the status of FIIS and which are organised in accordance with the FIIS Royal Decree.

- **Public closed-end private equity investment companies (*publieke privak /pricaf publique*):** A new Royal Decree on alternative investment funds investing in non-listed companies and growth businesses has been published in the Belgian State Gazette on 4 August 2016 and has entered into force on 14 August 2016. Its main objective is a new start for investment companies with fixed capital investing in non-listed companies and growth businesses (**PublicPrivaks**) (*“Pricaf Publique” / “Publieke Privak”*). The Royal Decree aims at providing easier means of financing for alternative investment funds investing in non-listed companies and growth businesses. Despite their high potential, these investment funds previously had difficulties in gaining access to finance, slowing down the further development of their businesses. In addition, the provisions imposed intend to contribute to maintaining and furthering the creation of employment.
- Funds which do not raise funds from the public but are registered as institutional or private collective investment undertakings and which were previously unregulated.
- All AIFs which do not raise capital through private placements and which are not yet subject to the Act of 3 August 2012.

Accordingly, the AIFM Act applies to the managers of these funds which solicit capital from investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors. The AIFM Act excludes certain types of funds from its scope and provides for certain exemptions which may be helpful for managers of smaller or of certain specific funds. As such, holding companies, institutions for occupational retirement provisions, employee participation schemes/employee saving schemes, securitisation SPVs, family office vehicles, joint ventures, supranational institutions, national central banks and governments are excluded from its scope of application.

In addition to these exclusions, Belgium has opted to implement less stringent rules for “small” AIFM’s. As a result, the following AIFMs benefit from a lighter regime:

- AIFMs managing AIFs with total assets under their management of a value of less than EUR 100 million; or
- AIFMs managing AIFs with total assets under their management of a value of less than EUR 500 million (if the AIFs portfolios are unlevered and no redemption rights exist during a period of five years following the date of initial investment in each AIF).

The Crowdfunding Platform Act specifies that Financing Vehicles cannot be undertakings for collective investments and may not have a defined investment policy as the investor is free to decide in which project he participates through the Financing Vehicles. Thus, Financing Vehicles as defined under the Crowdfunding Platform Act will fall out of scope of the AIFMD.

If one uses an investment vehicle that does not comply with the restriction of the Crowdfunding Platform Act, then that vehicle might qualify as an AIF if it has a defined

investment policy. However, it may benefit either benefit from exemptions under AIFMD or, in worst case, from the “lighter regime”.

### **3.4.3 Equity Model**

#### **3.4.3.1 Operating Company seeking funds**

Pursuant to the Belgian AIFM legislation, an Operating Company seeking funding with the purpose of generating profit to its shareholders should not qualify as an AI, as the characteristics of AIF are not met. Usually such company does not have a defined investment policy for the benefit of the investors.

#### **3.4.3.2 Project Company seeking funds**

With regard to a Project Company seeking funding, the Act does not apply to business in which collective investments are not conducted in the form of an AIF. Financing Vehicles under the Crowdfunding Platform Act cannot take the form of an Undertaking for Collective Investment.

However, it cannot be ruled out that an investment vehicle (other than a Financing Vehicle defined by the Crowdfunding Platform Act) would constitute an AIF in the event that the investment vehicle has a collective investment policy. However, these AIF will either benefit from the holding exemption or the lighter regime for small AIF.

### **3.4.4 Lending Model**

Investments by means of debt or placement instruments are generally non-AIF investments since the investors do not share liability for losses.

### **3.4.5 Donations or Rewards Model**

RES Projects can be structured so as not to offer any kind of revenue but instead nonfinancial rewards in return. If the promised reward is electricity at a reduced price it can be argued that the funds are not invested for the benefit of investors. The fund therefore is not a collective investment undertaking.

### **3.4.6 Cooperatives**

Most crowdfunded RES Projects in Belgium are organized through a cooperative company. The AIFM Act does not exclude cooperatives from its scope. Two cooperatives, with activities relating to alternative (micro-) financing, have already registered as AIF with the FSMA (Alterfin and CCP-Icofin). The FSMA has not yet clarified whether it considers that cooperatives can be considered as pursuing a defined investment policy. It is likely they can.

### **3.4.7 Crowdfunding Platforms**

Licensed Crowdfunding Platforms fall outside the scope of AIFM as they need to use Financing Vehicles to bundle investments by the crowd.

### 3.5 Payment Services Directive

Any transfer of funds through a Crowdfunding Platform or payment operations executed by a Crowdfunding Platform will generally constitute money remittance services within the meaning of the Payment Service Act (Payment services are regulated by Book 7 of the Code of Economic Law and the Belgian Payments Services Act of 21 December 2009). These activities are normally restricted to banks and payment establishments licensed by the Belgian National Bank that have been granted the status of Payment Institutions (section 6 of the Act).

The Crowdfunding Platform Act specifies that licensed Crowdfunding Platforms may not provide payment services as they may not hold funds from the investors.

However, Financing Vehicles could qualify as providing payment services if they provide money remittance services. Most Belgian Platforms avoid the cost of a payment services provider by having the funds wired directly by the investor into the funded company's account. Cooperatives funding RES Projects work with an online subscription form. Payment of the units follows then by way of a direct wire into the cooperatives bank account.

Financing Vehicles will probably not be able to rely on the "sales agent" exemption provided for in section 4(1°) of schedule II to the Payment Services Act ("payment transactions from the payer to the payee through a commercial agent authorized to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee"), as the chance is that, in the absence of steady relations with the funded company, they will be deemed to be acting as a broker rather than an agent.

### 3.6 Possible additional regulations

Other common regulations to which the operator of a Crowdfunding Platform may be subject include:

- Book VI Market Practices and Consumer Protection of the Code of Economic Law (formerly The Act on Market Practices and Consumer Protection);
- Money Laundering Provisions (Act of 11 January 1993 as amended);
- Privacy legislation (Mainly Act of 8 December 1992);
- The Consumer Credit Legislation (Now Book VII of the Code of Economic Law)

## 4 Regulatory barriers for Crowdfunding crossing borders in Belgium

The new Crowdfunding Platform Act addresses the question of intra-EEA activities and provides for a licensing regime for foreign actors. Many French and Dutch Crowdfunding initiatives are actively looking and have already contacted the FSMA to enter the Belgian market. Also, the major Belgian Platforms are already active abroad, mainly in France.

## 4.1 Applicable law

Belgian law takes a marketing approach regarding foreign offers. The offering of placement instruments in Belgium may trigger prospectus requirements, the offering of financial services may trigger licensing as an investment firm.

An offer is public where there is a communication, on the Belgian territory, in any way whatsoever and using any means whatsoever, which presents sufficient information on the conditions of an offer enabling an investor to decide to invest in investment instruments, which is made by the bidder, or by someone acting in concert with such bidder. Any means of publicity whether by internet or not can be considered as an offer.

## 4.2 Inbound

This concerns the situation where a Crowdfunding Platform from another EU country addresses investors in Belgium.

### 4.2.1 Foreign Crowdfunding Platform or company / project addresses Belgian investors

Belgian regulatory law can apply to the:

- A. Crowdfunding Platform (mainly license, information and compliance obligations)
- B. and/or the
- C. Company / project seeking funding (mainly prospectus and information obligations)

The FSMA will look into communication addressed in Belgian and these may include foreign websites allowing Belgian investors to subscribe to offers of foreign investment instruments.

#### 4.2.1.1 Crowdfunding Platform

##### (1) Licensing obligations

The Crowdfunding Platform Act specifies that Crowdfunding Platforms cannot provide investment services, with the exception of providing investment advice and receiving and passing on investment orders. As a result, the Crowdfunding Platform Act and licensed Crowdfunding Platforms fall out of the scope of MiFID (exemption in article of the MIFID Directive).

It is within that framework that the Crowdfunding Platform Act sets out further rules applicable to EEA foreigners.

Persons from another member state of the EEA can provide Alternative Finance Services in Belgium if they are licensed in their Member State to provide “similar services”. Prior to acting in Belgium, they must be licensed by the FSMA which will enter in contact with the controlling authority of the member state from which they originate. The management must

not be located in Belgium. However, if a branch is opened in Belgium the management of the branch must meet the fit and proper requirements. The foreign alternative services provider must abide by the obligations set out in the Crowdfunding Platform Act.

Passported foreign licensed investment firms and credit institutions are exempted from control by the FSMA and may directly offer Alternative Finance Services in Belgium.

Obviously, if a foreign Platform does not benefit from a MIFID license to provide financial services and it is not licensed in an EEA country to provide services similar Alternative Financial Services, then the Platform will only be entitled to make offers in Belgium if it registers as a Belgian Platform (and thus establishes itself in Belgium).

Depending on the nature of the investment instruments offered and the services the other regulations detailed above may apply.

#### **4.2.1.2 Foreign Company or Projects seeking funds from Belgian Investors**

##### **(1) Prospectus regulation**

A foreign company seeking funds will fall within the scope of the Prospectus Act if it offers investment instruments in Belgium.

The foreign company may benefit from some exemption:

- when an offer of investment instruments does not qualify as a public offer, if:
  - it is addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors; or
  - the total consideration per investor and per offer is more than EUR 100.000, calculated over a period of 12 months.
- Under the Crowdfunding Exemption which provides that the following operations do not qualify as a public offer of investment instruments, if they are offers:
  - for a total consideration of less than EUR 300.000;
  - with a maximum investment of EUR 1.000 per person and per project.

However, to benefit from the higher thresholds of EUR 5.000 per investor under Crowdfunding Platform Exemption the foreign company / project will need to make its offer through a licensed Platform (for licensing of foreign Platforms see above).

##### **(2) Other financial regulations**

As a general rule and assuming the foreign company is not offering (traded) securities to the Belgian public, no other financial regulations will apply.

However, if a foreign Platform offers a project or company through a Financing Vehicle in Belgium, the provisions of the Crowdfunding Platform Act regulating Financial Vehicles

apply. As stated above the Vehicle must be managed in the interest of the crowd. The crowd must be informed of the links existing between the Platform and the Financing Vehicle and of potential conflicts of interests. The Financing Vehicle annually discloses costs related to its use. Special compartmented accounting per project must be put in place.

#### **4.2.2 Foreign Crowdfunding Platform markets Belgian companies / projects (abroad)**

Belgian regulatory law can apply to the

- Crowdfunding Platform (mainly license and information obligations)
- and/or
- the company / project intending to be funded on the Crowdfunding Platform (mainly prospectus and information obligations).

Given the marketing approach used by the FSMA it is unlikely that the sole fact that a Belgian company or project is marketed through a foreign Platform triggers the application of Belgian financial regulation.

##### **4.2.2.1 Crowdfunding Platform**

###### **(1) Licensing obligations**

The foreign Platform does in this scenario / hypothesis not approach Belgian investors and thus no licensing will be required.

###### **(2) Other financial regulations**

For all practical purposes, Belgian companies have, up to now, not emitted “securities” through foreign Crowdfunding Platforms. Only if such issue would result in trading of securities on a regulated market (stock exchange or similar) would this trigger information requirement for the Platform and the company.

The issue of investment instruments other than “securities” through a foreign Platform does not trigger the application of Belgian financial regulations to that Platform.

##### **4.2.2.2 Belgian Company or Projects seeking funds (abroad) through a foreign Platform**

###### **(1) Prospectus regulation**

As the offer is not addressed to Belgian investors, the Belgian prospectus regulation will not apply.

###### **(2) Other financial regulations**

Normally no other financial regulations will apply to the Belgian company or project, save in the unlikely case that the offer concerns securities traded on a regulated market, in which case information obligations do apply.

## 4.3 Outbound

In this situation a Belgian Crowdfunding Platform enters a foreign (European) markets and addresses foreign investors.

### 4.3.1 Belgian Crowdfunding Platform addresses Foreign (EU) investors

Belgian licensed Platforms remain subject to the same information obligations and safeguards (as detailed above) when they approach foreign investors. The FSMA can scrutinize these.

### 4.3.2 Crowdfunding Platform

#### (1) Licensing obligations

As mentioned above, the regulatory framework governing licensed Platforms remains applicable when they approach foreign investors.

Moreover pursuant to the Crowdfunding Platform Act, a Belgian Platform which intends to operate abroad must inform the FSMA of its intention (and thus do so prior to addressing foreign investors). The information provided to the FSMA must detail the considered foreign activities, their financial impact and the consequences of these activities on the organization of the Platform. The FSMA can oppose within 60 days of receipt of a complete file to this project if it is of the opinion that it will have negative consequences for the Platform.

#### (2) Other financial regulations

As licensed Belgian Crowdfunding Platforms can only offer a limited range of financial services i.e., they are limited to providing investment advice and receiving and passing on investment orders, there is only a very limited range of financial regulations that can apply. However, they remain subject to the mini MiFID regime set out by the Crowdfunding Platform Act and other regulations which may apply as they are active in Belgium.

#### 4.3.2.1 Company / project

##### (1) Prospectus regulation

Assuming that the offer in this hypothesis is not addressed to Belgian investors, the Belgian prospectus regulation will not apply.

To avoid any discussion, the Platform will specify that the offer is not accessible to Belgian investors and will have to make sure they cannot subscribe from Belgium

##### (2) Other financial regulations

As a general rule, no specific financial regulations will apply to the companies or projects offered abroad.

### **4.3.3 Belgian Crowdfunding Platform addresses foreign companies or projects**

As under this scenario Belgian investors are approached with an offer relating to the foreign company or project, Belgian regulations do apply.

#### **4.3.3.1 Crowdfunding Platform**

##### **(1) Licensing obligations**

The Belgian Platform is subject to the Crowdfunding Platform Act and requires the licensing described above if it approaches Belgian investors. The fact that a foreign project or company is offered does not alter in itself the situation.

##### **(2) Other financial regulation**

Licensed Crowdfunding Platforms can only offer a limited range of financial services, i.e., they are limited to providing investment advice and receiving and passing on investment orders. The Mini MiFID obligations (see above) imposed by the Crowdfunding Platform Act remain in place.

#### **4.3.3.2 Company / project**

##### **(1) Prospectus regulation**

The foreign company or project promoted by the Belgian Platform is subject to the Belgian Prospectus Act when the offer is made to Belgian investors. This will be assumed if the offer is made through a Belgian licensed Platform. As a reminder the Prospectus Act regulates offers of investment instruments (and not only of tradeable securities).

The foreign company or project offered through a licensed Belgian Platform may benefit from the Crowdfunding Platform Exemption under the Prospectus Act as defined above. Without the intervention of a Belgian Platform, the foreign company or project may still benefit from the more restrictive Crowdfunding Exemption (as defined above).

Moreover, the foreign company / project might face (local) prospectus requirements pursuant to regulation in its home (EU) country. We cannot assess whether a (local) prospectus requirement exists if the Belgian Crowdfunding Platform presents foreign companies / projects in a campaign to Belgian investors. However, it may be that the foreign (EU) country / the respective financial regulation authority might not follow the marketing focused approach but another approach (e. g. simply connected to the seat / place of residence of the foreign (EU) country). Here, a double regulation cannot be excluded.

##### **(2) Other financial regulation**

With the possible exception of traded securities, foreign companies or projects offered on a Belgian Crowdfunding Platform are not subject to other Belgian financial regulations.

However, if the foreign project or company is a Financing Vehicle (as defined above) the special provisions of the Crowdfunding Platform Act apply if participation through that Vehicle is offered in Belgium. As stated above the Financing Vehicle must be managed in the interest of the crowd. The crowd must be informed of the links existing between the Platform and the Financing Vehicles and potential conflicts of interests. The Financing Vehicle annually discloses costs of its usage. Special compartmented accounting per project must be put in place.

#### **4.4 Impact of EU Regulation**

##### **4.4.1 Prospectus regime**

The Belgian Prospectus Act has a broader scope than the Prospectus Directive as it regulates (1) the offer of investment instruments (and not only transferable securities) but also (2) the offer of securities under the Prospectus Directive threshold. Thus, only a very limited (to nonexistent) part of the Belgian Crowdfunding market is regulated by the harmonized European legislation implemented into Belgian law.

Almost all Crowdfunding campaigns in Belgium have fallen outside the scope of the European prospectus regulation and are solely regulated by the Belgian Prospectus Act.

##### **4.4.2 AIFM-Directive**

Financing Vehicles as defined under the Crowdfunding Platform Act will not have a defined investment policy (as investors decide directly in which project they invest). Thus, the AIFMD Directive will have a limited impact on the Belgian Crowdfunding market.

Only if an investment vehicle used falls outside the scope of the Crowdfunding Platform Act e.g. it has a defined investment policy then this vehicle can be subject to the harmonized part of the AIFM Directive.

Obviously if an investment in such a vehicle is offered outside Belgium, it may come in conflict with local interpretation of the AIF Directive.

##### **4.4.3 MiFID / MiFID II**

The Belgian Crowdfunding market mainly uses non-tradeable debt investment instruments and only exceptionally tradeable securities. In consequence, MiFID (II) has a very limited potential application to the Belgian Crowdfunding market. This was further secured by the fact that the Crowdfunding Platform Act strictly limits the number of investment services a licensed Platform can offer.

Only for MiFID licensed firms acting cross border will MiFID regulation have an impact. This is rather the exception than the rule

#### 4.4.4 PSD / PSD II

The Crowdfunding Platform Act specifies that licensed Crowdfunding Platforms may not provide payment services as they may not hold funds from the investors.

However, investment vehicles could qualify as providing payment services if they would provide money remittance services. Most Belgian Platforms avoid the cost of a payment services provider by having the funds wired directly by the investor into the funded company's account. Cooperatives funding RES Projects work with an online subscription form. Payment of the units follows then by way of a direct wire into the cooperatives bank account.

This said to the extent Financing Vehicles, companies or projects use Payment Services Providers, it is obvious that the Payment Service Directive has an impact on the financing of Crowdfunding projects.

#### 4.5 Summary

Belgium has implemented a quite open and progressive Act regulating Crowdfunding Platform. Other countries also have started to implement own Crowdfunding legislation. These laws are not harmonized and “passporting” not obvious (although anticipated to some degree under the Belgian legislation). There is a clear field of friction between all these local regulations.

Especially the following can be pointed out as barriers hindering cross border activities:

- Foreign Platforms benefiting from a similar license regime abroad can apply for licensing under the Belgian Crowdfunding Platform Act. However, the other way round is not obvious and it is not clear to what extent Belgian Platforms will not be hindered by foreign licensing obligations. The Belgian license and Crowdfunding activity is not passportable. The hindrance is somewhat limited by the fact that Belgian licensed Platforms are allowed to offer only limited financial services. Hence, they limit (but do not totally avoid) friction with foreign regulations regarding the provision of financial services. This said, the provision of Alternative Financing Services abroad (even without any financial service) remains a potential source of friction.
- It is not evident that the Platforms which benefit from a MiFID license and can offer financial services abroad can also passport their Crowdfunding activities as most of these activities fall out of the scope of MiFID.
- Foreign Crowdfunding Platforms will still need to license in Belgium and follow Belgian rules which may be more stringent than local requirements.
- Almost all offers in Belgium fall out of the scope of the harmonized part of the Prospectus regulation. This because the instruments offered are usually not tradeable securities but investment instruments. In consequence, they cannot opt-in to benefit from the advantages of the prospectus regulation on EU level.

- Foreign companies / projects may face different or double prospectus regimes if they offer investment instruments in Belgium and in their home country.

## 5 Lessons learned from the Belgian regulator for a possible European Crowdfunding Regulation

### 5.1 Role Model ("dos")

Belgium took a lead role (together with France and others) in establishing a clear framework for Crowdfunding Platforms. Additionally it made a timid but notable opening on related tax advantages. The latter may not be usable for EU harmonization.

Belgium thus recognizes the importance of Crowdfunding and also provides related (limited) tax benefits.

Belgium also made a first opening to foreign Crowdfunding Platforms in indicating that they can be licensed in Belgium and that contacts will/can be taken with the local authority to coordinate the file. Belgium does recognize the European dimension of Crowdfunding.

For a possible harmonized European Crowdfunding regulation the following aspects of the Belgian approach can be useful:

- The licensing of Platforms under a light regime has been enacted. The act strikes a balance between light regulation and providing protection to investors;
- Private investors may invest up to EUR 5.000;
- Specific Crowdfunding and Crowdfunding Platforms exemptions have been introduced in the Prospectus legislation;
- Additionally offers to professional investors or offers to a limited group also falls out of the scope of the Prospectus Act;
- The provision of financial services by non MiFID licensed Platforms has been allowed when MiFID provided for exemptions. Other financial services such as the placement of financial instruments have received a clearer definition allowing for the activities of Platform to fall out of the scope of these regulated services;
- An open approach to the banking monopoly has allowed Platforms and other vehicles to collect funds from the public, which are returned if the project is not fully funded. Adequate and adapted safeguards have been put in place;
- The FSMA took a clear lead role in explaining Crowdfunding regulations to the public. It already published detailed fact sheets as early as in 2012. The FSMA has also published several memorandum to clarify the Crowdfunding Platform Act;
- The FMSA acknowledges the EU aspect of Crowdfunding. It is currently looking into licensing Foreign Crowdfunding Platforms in Belgium. It has already permitted the activities of Belgian Platforms abroad (mainly in France);
- Investment by the crowd in combination with professionals is allowed.

## 5.2 Aspects that should be avoided ("don'ts")

- Due to the existing EU financial framework (and especially MIFID) Crowdfunding offers related to “securities” cannot be offered through most Platforms, except those that benefit from a MiFID license. As a consequence, pure equity Crowdfunding (other than by MiFID licensed Platforms) is almost nonexistent in Belgium.
- Limitations under the Prospectus Act of the amount invested do not take investors wealth into account. Prospectus investment caps could be further increased for informed investors.
- Approval of a prospectus is needed below EUR 5.000.000. The Belgian exemptions are low EUR 100.000 or EUR 300.000. Above a prospectus can be required.

## 6 Conclusion

Belgium is now on the forefront of the Crowdfunding legislation. It has opened its market to some extent to foreign Platforms and allows and regulates cross border activities from Belgian Platforms.

This said, the potential of cross border activity is limited by the fragmentation of local regulations. This is the case of regulation organizing the licensing of Crowdfunding Platforms. Conflicting local interpretation of EU driven financial terms is also a potential hurdle to cross border activity.

The following measures on a European legislative / administrative level should be taken in order to create a level playing field around the EU from a Belgian perspective:

- Opening of Crowdfunding to all type of financial instruments including tradeable securities;
- In consequence, allowing of exemptions to regulated financial services for Crowdfunding purposes;
- Agreeing on harmonized prospectus exemptions for Crowdfunding purposes below the harmonized thresholds of the Prospectus Directive;
- Clarification that MiFID (II) license (and the EU Passport) covers all financial instrument covered by national legislation in the host EU member state when crossing border;
- Consistent definitions of terms based on European legislation (e. g. collective investment undertaking, financial instruments) by means of European authorities.

## 7 Summary – Crowdfunding regulation

| Country  | Belgium   |
|--|---|
| <p><b>Summary</b></p> <p><b>Recent developments in Crowdfunding regulation</b></p> | <ul style="list-style-type: none"> <li>• <b>2014:</b> first Crowdfunding legislative initiative (the “Crowdfunding Act”) increasing the threshold of the “prospectus exemption” to EUR 300.000 and EUR 1.000 per investor.</li> <li>• <b>2015:</b> the Belgian Government introduced tax incentives in favor of Crowdfunding.</li> <li>• <b>End 2016:</b> the Crowdfunding Platform Act comprehensively regulates the licensing of Crowdfunding Platforms and the use of Financing Vehicles. It further increases the thresholds of the Crowdfunding exemption for licensed Crowdfunding Platforms in the Prospectus law to EUR 300.000 per project and EUR 5.000 per investor.</li> </ul>  |
| <p><b>Current / planned Crowdfunding regulation</b></p>                            |   |
| <p><b>General regulation</b></p>   | <p><u>Licensing:</u></p> <ul style="list-style-type: none"> <li>• Licensed Platforms may not provide regulated investments services, except for providing investment advice and receiving and passing on investment orders.</li> <li>• The definition of placement services has been narrowed to emphasis the fact that a placement service entails assisting the client during the entire process, including managing financial flows. This allows differentiation with permitted services such as receiving and transmitting orders.</li> <li>• The Prospectus Act (article 56) now specifies that Platforms may commercialize investment instruments.</li> <li>• Licensed Platforms will act out of the scope of MiFID. Otherwise they will require MiFID licensing. This is the case for the offering of not exempted financial services regarding tradeable securities (e.g for pure equity Crowdfunding).</li> <li>• Most Platforms will only require licensing as an Alternative Service Provider (the light regime put in place by Belgium) and thus avoid MiFID licensing.</li> </ul> <p><u>Banking monopoly:</u></p> <ul style="list-style-type: none"> <li>• Only credit institutions (and the like) are authorized to collect deposits and other repayable funds from the public in Belgium. Crowdfunding Platforms may not receive or hold monies, financial products from their clients or be indebted to their clients (article 17).</li> <li>• Funds must be collected by either the issuer or payment institutions licensed to manage payments. Adequate protection must be put in place to guarantee that the collected funds cannot be used for any other purpose than either reimbursing the investor (if the fundraising venture fails) or investing in the project (in case of success).</li> </ul> |

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| <p><b>Prospectus requirement</b></p>        | <p>Applies to offers of investment instruments (= broader than financial instruments).</p> <p><b>General Exemption:</b></p> <ul style="list-style-type: none"> <li>• offers below EUR 100.000.</li> <li>• offers addressed to fewer than 150 natural or legal persons other than qualified investors;</li> <li>• total consideration per investor and per offer is more than EUR 100.000, calculated over a period of 12 months.</li> </ul> <p><b>Crowdfunding Exemption:</b></p> <ul style="list-style-type: none"> <li>• for a total consideration of less than EUR 300.000;</li> <li>• with a maximum investment of EUR 1.000 per person and per project.</li> </ul> <p><b>Crowdfunding Platform Exemption:</b></p> <ul style="list-style-type: none"> <li>• Licensed Platform or investment firm do not require a prospectus for offers for a total consideration of less than EUR 300.000, with a maximum investment of EUR 5.000 per person and per project.</li> <li>• Cooperatives in Belgium benefit from a distinct prospectus exemption.</li> </ul> |
| <p><b>AIFMD-regulation</b></p>              | <ul style="list-style-type: none"> <li>• Usually not applicable to average start-up.</li> <li>• Operating companies are no AIF. Project companies (financing vehicles) may be AIF.</li> <li>• However, the Crowdfunding Platform Act specifies that Financing Vehicles cannot be undertakings for collective investments and may not have a defined investment policy. Financing Vehicles as defined under the Crowdfunding Platform Act will fall out of scope of the AIFMD.</li> <li>• In addition Belgium has opted to implement less stringent rules for “small” AIFM’s.</li> <li>• If one uses an investment vehicle that does not comply with the restriction of the Crowdfunding Platform Act, then that vehicle might qualify as an AIF if it has a defined investment policy. However, it may benefit either benefit from exemptions under AIFMD or, in worst case, from the “lighter regime”.</li> </ul>   |
| <p><b>Payment service regulation</b></p>    | <ul style="list-style-type: none"> <li>• Transfer of funds through a Crowdfunding Platform constitutes money remittance services. License required from the Belgian National Bank.</li> <li>• The Crowdfunding Platform Act specifies that licensed Crowdfunding Platforms may not provide payment services as they may not hold funds from investors.</li> <li>• However, Financing Vehicles could qualify as providing payment services if they provide money remittance services. Cooperation with payment service provider required. Most Belgian Platforms avoid the cost of a payment services provider by having the funds wired directly by the investor into the funded company’s account.</li> </ul>   |
| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• Book VI Market Practices and Consumer Protection of the Code of Economic Law (formerly The Act on Market Practices and Consumer Protection);</li> <li>• Money Laundering Provisions (Act of 11 January 1993 as amended);</li> </ul>   |

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|                            | <ul style="list-style-type: none"> <li>• Privacy legislation (Mainly Act of 8 December 1992);</li> <li>• Consumer Credit Legislation (Now Book VII of the Code of Economic Law).</li> </ul>  |
| <b>Regulatory barriers</b> |  |
| <b>Inbound</b>             | <p><b>Foreign Crowdfunding platform addresses Belgian investors</b></p> <p>Belgian investors are approached, thus the Belgian regulatory framework applies.</p> <p><u>Crowdfunding platform:</u></p> <ul style="list-style-type: none"> <li>• Licensing obligations</li> <li>• Persons from another member state of the EEA may provide Alternative Finance Services in Belgium if they are licensed in their Member State to provide “similar services”. Prior to acting in Belgium, they must be licensed by the FSMA which will enter in contact with the controlling authority of the member state from which they originate.</li> <li>• Passported foreign licensed investment firms and credit institutions are exempted from control by the FSMA and may directly offer Alternative Finance Services in Belgium.</li> <li>• If a foreign Platform does not benefit from a MiFID license to provide financial services and it is not licensed in an EEA country to provide services similar Alternative Financial Services, then the Platform will only be entitled to make offers in Belgium if it registers as a Belgian Platform (and thus establishes itself in Belgium).</li> </ul> <p><u>Foreign Company / project:</u></p> <p>Prospectus regulation</p> <p>A foreign company seeking funds will fall within the scope of the Prospectus Act if it offers investment instruments in Belgium.</p> <p>The foreign company may benefit from some exemption:</p> <ul style="list-style-type: none"> <li>• If the offer qualifies as non-public (addressed to fewer than 150 persons or the total consideration per investor and per offer is more than EUR 100.000, calculated over a period of 12 months);</li> <li>• Under the Crowdfunding Exemption, if the offer is for a total consideration of less than EUR 300.000; with a maximum investment of EUR 1.000 per person and per project. Under the Crowdfunding Platform Exemption if the offer is made through a licensed Platform, then higher thresholds of EUR 5.000 per investor.</li> </ul> <p>Other financial regulations</p> <ul style="list-style-type: none"> <li>• If a foreign Platform offers a project or company through a Financing Vehicle in Belgium, the provisions of the Crowdfunding Platform Act regulating Financial Vehicles apply.</li> </ul> <p><b>Foreign Crowdfunding platform markets Belgian companies / projects (abroad)</b></p> |

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|                        | <p>Given the marketing approach, it is unlikely that the fact that a Belgian company or project is marketed through a foreign Platform triggers the application of Belgian financial regulation.</p> <p><u>Crowdfunding Platform:</u></p> <ul style="list-style-type: none"> <li>• No licensing will be required. No application of Belgian financial regulations to that Platform.</li> <li>• <u>Belgian Company or Projects seeking funds</u> (abroad) through a foreign Platform:</li> <li>• As the offer is not addressed to Belgian investors, the Belgian prospectus regulation will not apply. Normally no other financial regulations will apply to the Belgian company or project.</li> </ul>  |
| <p><b>Outbound</b></p> | <p><b>Belgian Crowdfunding platform addresses foreign investors</b></p> <p>Here, only foreign investors (e.g. a Belgian platform addresses French investors) are addressed.</p> <p><u>Crowdfunding Platform:</u></p> <ul style="list-style-type: none"> <li>• Belgian licensed Platforms remain subject to the same information obligations and safeguards when they approach foreign investors.</li> <li>• Licensing obligations</li> <li>• The regulatory framework governing licensed Platforms remains applicable when they approach foreign investors.</li> <li>• Moreover a Belgian Platform which intends to operate abroad must inform the FSMA of its intention (and thus do so prior to addressing foreign investors).</li> </ul> <p>Other financial regulations</p> <ul style="list-style-type: none"> <li>• As licensed Belgian Crowdfunding Platforms can only offer a limited range of financial services i.e., they are limited to providing investment advice and receiving and passing on investment orders, there is only a very limited range of financial regulations that can apply. However, they remain subject to the mini MiFID regime set out by the Crowdfunding Platform Act and other regulations which may apply as they are active in Belgium.</li> </ul> <p><u>Company or Projects:</u></p> <p>Prospectus regulation</p> <ul style="list-style-type: none"> <li>• Assuming that the offer in this hypothesis is not addressed to Belgian investors, the Belgian prospectus regulation will not apply.</li> <li>• Other financial regulations</li> <li>• As a general rule, no specific financial regulations will apply to the companies or projects offered abroad.</li> </ul> <p><b>Belgian Crowdfunding platform markets foreign companies / projects</b></p> <p>Under this scenario, Belgian investors are approached with an offer relating to the foreign company or project -&gt; Belgian regulations do apply .</p> |

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|                                | <p><u>Crowdfunding Platform:</u></p> <ul style="list-style-type: none"> <li>• Licensing obligations</li> <li>• The Belgian Platform is subject to the Crowdfunding Platform Act and requires licensing if it approaches Belgian investors.</li> <li>• Other financial regulations</li> <li>• Licensed Crowdfunding Platforms can only offer a limited range of financial services, i.e., they are limited to providing investment advice and receiving and passing on investment orders.</li> </ul> <p><u>Company or Projects:</u></p> <p>Prospectus regulation</p> <ul style="list-style-type: none"> <li>• The foreign company or project promoted by the Belgian Platform is subject to the Belgian Prospectus Act if investment instruments are offered to Belgian investors. This will be assumed if the offer is made through a Belgian licensed Platform.</li> <li>• The Crowdfunding Platform Exemption (or Crowdfunding Exemption) may be available.</li> <li>• Moreover, the foreign company / project might face (local) prospectus requirements pursuant to regulation in its home (EU) country.</li> </ul> <p>Other financial regulations</p> <ul style="list-style-type: none"> <li>• With the possible exception of traded securities, foreign companies or projects offered on a Belgian Crowdfunding Platform are not subject to other Belgian financial regulations.</li> <li>• However, if the foreign project or company is a Financing Vehicle (as defined) the special protective provisions of the Crowdfunding Platform Act apply if participation through that Vehicle is offered in Belgium.</li> </ul> |
| <b>Impact of EU Regulation</b> |   |
| <b>Prospectus regulation</b>   | <ul style="list-style-type: none"> <li>• The Belgian Prospectus Act has a broader scope than the Prospectus Directive as it regulates (1) the offer of investment instruments (and not only transferable securities) but also (2) the offer of securities under the Prospectus Directive threshold. Thus, only a very limited (to nonexistent) part of the Belgian Crowdfunding market is regulated by the harmonized European legislation implemented into Belgian law.</li> </ul>   |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• The AIFMD Directive will have a limited impact on the Belgian Crowdfunding market as Financing Vehicles as defined under the Crowdfunding Platform Act will not have a defined investment policy and thus fall out of scope.</li> <li>• Only if an investment vehicle used falls outside the scope of the Crowdfunding Platform Act e.g. it has a defined investment policy then this vehicle can be subject to the harmonized part of the AIFM Directive.</li> <li>• Obviously if an investment in such a vehicle is offered outside Belgium, it may come in conflict with local interpretation of the AIF Directive.</li> </ul>  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• The Belgian Crowdfunding market mainly uses debt investment instruments and only exceptionally tradeable securities. In consequence, MiFID and MiFID II have a very limited potential application to the</li> </ul>  |

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|                     | <p>Belgian Crowdfunding market. This was further secured by the fact that the Crowdfunding Platform Act strictly limits the number of investment services a licensed Platform can offer.</p> <ul style="list-style-type: none"> <li>• Only for MiFID licensed firms acting cross border will MiFID regulation have an impact. This is rather the exception than the rule.</li> </ul>  |
| <b>PSD / PSD II</b> | <ul style="list-style-type: none"> <li>• The Crowdfunding Platform Act specifies that licensed Crowdfunding Platforms may not provide payment services as they may not hold funds from investors.</li> <li>• However, investment vehicles could qualify as providing payment services if they would provide money remittance services. Most Belgian Platforms avoid the cost of a payment services provider by having the funds wired directly by the investor into the funded company's account.</li> <li>• To the extent Financing Vehicles, companies or projects use Payment Services Providers, it is obvious that the Payment Service Directive has an impact on the financing of Crowdfunding projects.</li> </ul> |

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# Bulgaria

## 1 Recent developments in the market of Crowdfunding in Bulgaria

During the last 12 months there were the following more significant developments in Bulgaria regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

According to figures from the Bulgarian National Bank foreign direct investment in the field of equity and investment fund shares for 2016 are EUR 30,488.3 million.

Nowadays regarding Crowdfunding equity model, in Bulgaria is popular the so-called *Amundi Fund*. The latter is organized as a "*Societe d'Investissement a Capital Variable*" ("SICAV") under the laws of the Grand Duchy of Luxembourg, incorporated on 18<sup>th</sup> July 1985. The current name of the fund was changed on 2<sup>nd</sup> March 2010.

Instead of focusing on one particular investment objective, *Amundi Fund* has divided its assets into sub-funds of assets, each with a separate investment objective and asset portfolio. This combination provides to the customers an access to global selection of markets through a range of diversified and internationally invested sub-funds.

Investment in *Amundi Fund* shares is suitable for a wide range of customers – individual, corporate, institutional. No matter if the customers are an experienced investor or just a beginner, *Amundi Fund* gives the opportunity to choose between 18 sub-funds in Bulgaria, according to geographic preferences, risk profile, investment horizons and many other criteria.

The advantages of the fund:

- **Profitability** – Opportunity to obtain high rates of return in investments. The value of the shares and income thereof can rise and drop: there is no guarantee for profit and for full return of the initially invested amount of funds.
- **Accessibility and variety of investment opportunities** – Gives access to a wide variety of financial markets in terms of assets (equities, bonds, money market instruments) and geographic exposure (USA, Europe, Asia, MENA, Emerging Countries and others) which are difficult to reach and to trade on individually;
- **Attractive transactions fees** and no minimal initial or subsequent in-vestment's requirements;
- **Liquidity and flexibility** – in order to optimize investments and obtain maximum yield, customers may buy, convert or redeem shares at any time among the different sub-funds and classes. Redemptions are made without any fee. Presently, the conversion is also for free but in the future fees are possible up to 1 %;

- **Professional active asset management** – *Amundi* is an Investment Manager driven by professionalism, quality and reactivity;
- **Diversification** – through investment in various types of securities, spreading out the risk by country and sector, in order to optimize customer re-turn;
- **Transparency, information to investors and simplicity** – Possibility to estimate the value of customer investments at any moment through a daily net asset value (NAV = the price at which clients can buy, convert and redeem your shares).

The steps for becoming an investor in *Amundi Funds* are:

- Visit one of the branches and offices of *Societe Generale Expressbank AD*, listed in the "General Information for Bulgarian investor in Amundi Funds";
- Fulfil an application for the purchase of shares and sign an agreement with the Bank;
- Pay the necessary amount including the subscription fee;
- In 5 working days after the customer placed the order, *Societe Generale Expressbank AD* will inform the clients for the number and the Net Asset Value of the subscribed shares, as of the day of the purchase order

Return on the customer investments can be gained by redeeming shares to *Amundi Funds* at a suitable moment. The offered shares in Amundi sub-funds in Bulgaria do not distribute dividends: the latter are capitalized, thus increasing their value.

## 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

During the last couple of years, several platforms related to Peer-to-Peer (P2P) have been developed in Bulgaria. One of them is *Iuvo*. At present, the platform uses only one originator; this is one of the largest non-bank credit companies "*Easy credit*". The notion "Crowdfunding originator" means an institution which lends money to natural and/or legal persons under pre-arranged conditions. The platform expects that there will be two more investing companies in the next year. *Iuvo* offers a new type of financing on the Bulgarian market. The originator is obliged to pay the remaining principal amount to the investor in arrears over 60 days. There are no fees for account maintenance. In case of selling loans in the secondary market the investor has to pay a fee of 1%. The loans, which can be invested, can be compared by maturity, number of payments and ratings. Users of the platform have invested almost BGN 420 000 month from June 2016 until now. The yield is between 5% and 12%, while the primary market has more than 1,300 credit proposals and at the time they are all consumer and without collateral.

The other platform is *Klear* which launched in November 2016. The difference in this platform is that a company will lend money, following this will seek the funding. Creator of *Klear* is Loic Le Pishu, who was CEO of "BNP Paribas Personal Finance" in Bulgaria several

years ago and who has experience in non-bank lending. The platform now allows applying for loans, where those borrowers with the lowest risk profile would pay the APR (annual percentage rate) of about 6% in comparison to an average of 11% for bank loans. There will be no buy back options, however after 120 days of delay in repayment of the loan, the debt will be transferred to a Collectors company and the money shall be paid back to the investor. *Klear* will target prime customers with a lower risk profile and the profitability will be expected to be around 6%. Loans shall be compared on the basis of age, affiliation and address of the borrower, data from the Central Credit Register and payment history. The investment into the platform is currently EUR 1 million.

The other P2P platform, popular in Bulgaria, is *Mintos*. The platform has 14 originators, mainly non-bank lenders from Lithuania, Latvia and Estonia. The investment is realized through payment transactions into a Latvian bank. On the primary market are listed nearly 2,000 loans, 90% of which are from the Latvian company *Mogo*. There are loans to companies with relevant information about the financial performance of the lending company. The yield is from 5.5% to 15%, but less than 1% of the announced primary market loans. More significant, however, is the secondary market, where there are over 25 000 credits. Since last year through the platform have been funded loans for over EUR 73 million.

There is another popular platform on the Bulgarian market known as *Twino*. Since November 2015, there are over EUR 60 million invested in the system and more than EUR 850,000 return paid to investors. Nearly three-quarters of the credits are short term ones: 1 to 3 months, which average yield is 11%. Loans, which repayment is delayed are around 18% of all the loans. There are no fees for withdrawal of funds from the account. The majority of the loans have a buy-back option in case of delay of more than 30 days, and relevant interest is due for the period. The Originators are credit companies from Poland, Georgia, Latvia and Denmark.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

The last two years showed a trend for the development of donor platforms in Bulgaria. Scholarship Fund "*Go, learn and come back*" exists to support talented youth to obtain quality education abroad and to be successful in Bulgaria upon return. The fund was created in 2016 by "*Here and There*"- an Association of Bulgarians studying abroad who have returned to the country to share and provide their knowledge and skills in Bulgaria.

The purpose of the platform is to give scholarships from Bulgarians to Bulgarians every year. Once they acquire education abroad they should apply their knowledge in practice in Bulgaria.

Last year, the association collected BGN 11,000 from donors who then support three people in their MBA abroad that are studying at Harvard, Cambridge and Marburg at the moment.

The aim of the second edition is to collect and distribute scholarships to a second group of young people who should complete MBA abroad in 2017 / 2018. At present, there have been collected about BGN 20,000.

#### 1.4 Real Estate Crowdfunding in Bulgaria

*Property Club Bulgaria* is the first platform for shared financing of real estate in Southeast Europe. The headquarters of the company is in Sofia. Property Club was founded in 2015 as a "professional for everyone" platform and for the first time introduced the possibility for shared financing of real estate transactions in the region.

Property Club is an online platform that enables its clients to finance real estate investment deals. The process is based on the increasingly popular approach for shared financing in which a group of people together finance a project and benefit from it if the same one is successful.

The participants are the following:

- Operators select and prepare projects to be proposed in the platform as opportunities for shared funding;
  - People who co-finance the projects;
  - Project Managers who propose and manage the projects to be funded.

The investment process is accomplished in 5 steps:

(1) signing up, (2) reviewing the projects for co-financing, (3) selecting a project and participating with the selected amount, then waiting for full financing of the project, (4) preparing the documents and after the successful completion (5) making a profit.

#### 1.5 Renewable Energy Sources Crowdfunding

A short-term program for promotion of using renewable energy and biofuels in Radnevo municipality was launched in 2016. The program is scheduled for the period 2016 – 2019 and was developed on the basis of Art. 10, Para. 1 and para. 2 of the Renewable Energy Act and of the Energy Act in accordance with the National Energy Action Plan of renewable resources and guidelines of the Agency for Sustainable Energy development. The program is consistent with:

- the planned development of the area;
- characteristics and the potential of the municipality;
- as well as the current energy efficiency strategy.

The main goal of the program is to promote the use of renewable energy for the needs in municipal and private buildings. The initial implementation of renewable energy sources in municipal buildings and the presentation of the results to the population of the municipality will serve as a benchmark for achieving of savings. Taking into account the steadily rising cost of electricity, with the implementation of energy-efficient measures and the implementation

of the renewable energy sources it will reduce the energy consumption of the transmission network, which will decrease the cost of the municipality at all. Savings can be redirected to other areas that could improve the quality of life and the business environment in the municipality. In this way Radnevo municipality will be more competitive and attractive for investment. The challenge is to put an end to the excessively high energy consumption without reducing the quality of life and the comfort of housing. This can be achieved by: improving the energy management of the territory of the municipality; changing the fuel base for local heating systems with renewable sources; introducing local sources of renewable energy (solar collectors, photovoltaic and geothermal sources, use of biomass, waste treatment); changes in the behaviour of energy consumers.

In determining the sources of funding to implement the objectives of the short - term municipal program to promote the use of energy by renewable sources and biofuels of the municipality of Radnevo have been taken into account:

- the possibilities for securing own funds from the municipal budget;
- attracting external resources according to the available at the moment of Planning financial instruments;
- developing new forms of Investment partnerships;
- and the benefits of successful combinations of two or more sources of funding.

One of the main sources of the program is that it will be funded by the stakeholders' own resources.

## **2 Recent developments regarding Crowdfunding regulation in Bulgaria**

The current Bulgarian legislation does not provide any explicit regulations for Crowdfunding. In 2017 a special report of the European Union was drawn up, namely Report from the Commission to the Council and the European parliament – Accelerating the capital markets union: addressing national barriers to capital flows. This document outlines the different national approaches to group funding. According to information available to the Commission, such requirements exist in a limited number of Member States and could be found in legislation or in supervisory practice. They may apply to all types of financial services or only to some, such as insurance, banks or fund managers established in these countries. One of the main potential obstacles to cross-border activity is the lack of regulations on Crowdfunding, as well as the different legal framework between countries. Overcoming these obstacles will help to gain access to foreign markets from national platforms without requiring them to be registered in foreign territory. As a result, the Commission has the task of constantly monitoring the group finance platforms.

There have been changes in the laws that apply to Crowdfunding by analogy like the Credit Institutions Act, the Law on Payment Services and Payment Systems, the Public Offering of Securities Act, the Markets in Financial Instruments Act, the Law on the activities

of collective investment schemes and other collective investment undertakings, the Law on Measures against Money Laundering and Currency Act. However, without any particular effect on Crowdfunding. We are mentioning some of these in section 3 below.

### **3 Current Regulation of Crowdfunding in Bulgaria**

After reviewing the current applicable Bulgarian legislation (up to now) and the available public information provided by the competent state authorities in this regard, we can confirm that there are no explicit regulations in the field of Crowdfunding financing being adopted yet.

Notwithstanding the above, upon development of this legal institute in Bulgaria, the following legal framework could be applied in future to the already existing types of crowdfunding:

#### **3.1 Licence under the Law on the Bulgarian National Bank**

##### **3.1.1 Law on Credit Institutions & Law on Payment Services and Payment Systems**

In general pursuant to Art. 2 and 3 of the Law on Credit Institutions a legal entity is treated as a credit or a financial institution in any case it provides to the public financial services including payment services within the meaning of the Law on Payment Services and Payment Systems.

Financial institutions which are not subject to license under another special legal act are required to register in the Financial Institutions Register maintained by the Bulgarian National Bank (BNB) – the institution, supervising their activity. BNB shall be also competent to exercise control to payment service providers as defined in the Law on Payment Services and Payment Systems.

In summary, notwithstanding the type of the Crowdfunding platform, the operator of the platform shall be required to meet the prerequisites of at least one of the abovementioned legal acts.

Since 2016, the scope of the Law on Payment Services and Payment Systems has been broadened by regulating conditions for facilitating consumers in the cross-border opening of payment accounts within the European Union.

##### **3.1.2 Public Offering of Securities Act & Markets in Financial Instruments Act**

In case the Crowdfunding platform offers an equity model it could fall within the legal framework of the Public Offering of Securities Act or the Markets in Financial Instruments Act.

Legal entities providing public offering of securities shall be required to register as a public joint-stock company and to comply with the requirements for those companies under the Law.

Legal entities facilitating public offering of securities or investment products could have been required to register as an investment intermediary under the Markets in Financial

Instruments Act. According to the latest amendments as of 2016 of the Markets in Financial Instruments Act the enforcement and establishment of collateral on the cash and financial instruments of clients for the obligations of the investment intermediary is not allowed.

### 3.2 Prospectus requirements

The companies which publicly offer securities to investors are generally subject to a prospectus requirement as per Art 78 of the Public Offering of Securities Act. These rules do not apply to the following types of offering:

- the securities are offered solely to qualified investors;
- the securities are offered to fewer than 150 natural or legal persons in each individual Member State who are not qualified investors;
- the minimum amount for which the offered securities can be acquired is the BGN equivalent of EUR 100,000 per investor for each individual offering;
- unit nominal value of the securities offered is at least the equivalent of EUR 100,000;
- the total value of the securities offered within the European Union is less than the BGN 100,000 equivalent, which threshold is calculated over a period of 12 months

The Financial Supervision Commission is responsible to supervise the public offering of securities and to exercise controlling activities in order to prevent and terminate legal violations in view to ensure protection of the interests of investors. Other applicable laws related to the activities of the crowd-funding platforms might be the Commerce Act, the Law on Measures against Money Laundering and the Currency Act, in regard to the bank transfers regulations, as well as the different lending models, including between related parties.

In case of suspicion of money laundering or of criminal assets involved, the persons are obliged to notify immediately the Directorate "Financial Intelligence" of the State Agency "National Security".

According to the amendments of the Law on Measures against Money Laundering as of 2016 notification may also take place electronically with qualified electronic signature or issued by the State Agency for National Security an access certificate.

In 2016 the Currency Act was changed in the section "Gathering information for the needs of the statistics". The change rescinds the obligation to file a report within 30 days of receipt of funds from abroad. This change is a good prerequisite for the cash flows that characterize the activity of Crowdfunding.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

With regard to the management of the alternative investment funds (AIFs) a new chapter has been adopted in the Law on Collective Investment Schemes and Other Undertakings for Collective Investments which provides for detailed regulation of the activity of the fund

managers, including their registration/licensing, requirements for their organization, terms and conditions in case of trans-border management. The competent body which shall regulate and supervise the activities of AIFs and their managers shall be the Financial Supervision Commission. Nevertheless, pursuant to the Law on Collective Investment Schemes and Other Undertakings for Collective Investments, the Crowdfunding financing does not fall within the scope of its application. The latest amendments of Law on Collective Investment Schemes and Other Undertakings for Collective Investments from 2016 do not affect the phenomenon of Crowdfunding. It shall apply to closed-end investment companies, as far as the special investment purposes companies are excluded of the scope of application of the Directive.

### 3.4 Regulation of Renewables Crowdfunding

The most developed Crowdfunding projects are in connection with RES projects therefore we hereby briefly outline the legal framework.

In 2010 Bulgaria adopted new legislation about the RES projects, changing the conditions for the support of the sector in terms of preferential prices, terms and introduction of guarantee payments. The explanation of this policy could be seen in the Ministry of Energy report. The evaluation of Ministry of Energy is that the introduced with the 2007 law support measures for the RES – preferential prices, compulsory buying, long term contract, etc. led to very high interest about the production of RES based electricity. This causes several problems such as: the announcement of too much investment intentions for solar and wind parks, not in compliance with the capacity of the energy system of the country; the cases of RES projects in preserved or other sensitive areas without the necessary authorizations, the need to change the statute of agricultural lands and the fact that many potential investors were not prepared to fully support their investment.

According to the experts of the RES-Integration project, “The new RES Act now abolishes the priority access to the grid for RES producers completely. The law places renewable energy behind all other kinds of energy. The law envisages stopping the application of the support mechanism after the indicative target for Bulgaria is achieved. This measure is in direct violation of EU directives. Another serious barrier is the fact that RES investors will find out the price at which they will be selling their energy only after the construction of their power generating facilities is completed”.

In 2011 the Parliament adopted a new, rather restrictive Renewable Energy Sources Act (RES Act) in response to the significant rise of the percentage of the energy, produced via renewable sources. The eligibility period for FiTs for wind and solar photovoltaic (PV) was reduced. The main reason for this legislative direction was the prognosis for sharp increase of the cost of renewable support systems and grid development, and the falling cost of renewables, especially solar. Following this tendency after 2012 the new legislative measures brought the RES sector to a significant decrease of the support for RES. These developments led to certain protests from investors against the newly adopted rules, the lack of transparency in the energy sector and the lack of predictability for their investment.

From 2015 onwards there is no amendment to the Law on Renewable Energy, as well as adopted bills in the National Assembly to amend this Law.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject to include:

- Commercial Law;
- Law on Measures against Money Laundering, and
- the Currency Act.

## 4 Regulatory barriers for Crowdfunding crossing borders

Given that in Bulgaria there is no directly applicable law on Crowdfunding the referred to above laws will apply by analogy. In this respect, in the case of the equity model Crowdfunding, compliance with the prospectus requirements set out in Section II of the Public Offering of Securities Act will be required. Currently, an obvious example of the equity model Crowdfunding in Bulgaria is the *Amundi Fund Bulgaria* platform. Despite the fact that the shares offered on the Bulgarian market by *Amundi Fund Bulgaria*, there is no requirement to publish a prospectus. The reason for this is Art. 79, para. 5, item 8 of the Public Offering of Securities Act according to which a prospectus is not published if the securities are already admitted to trading on another regulated market. As *Amundi Fund Bulgaria* is a sub-fund of a parent company domiciled in an EU Member State, the requirement for a prospectus is the responsibility of that parent company.

### 4.1 Applicable law

Unlike the equity model Crowdfunding, which does not require the involvement of an investment firm, all other models (for example Lending Model) are very likely to resort to the participation of investment firms. According to Art. 6 of the Markets in Financial Instruments Act providing investment services and investment activities on a professional basis can perform only a joint-stock company or a limited liability company with a registered office in the territory of the Republic of Bulgaria, having obtained a license for an investment intermediary by the Financial Supervision Commission.

In case the Crowdfunding platform requires payments in foreign currency, the investment firm shall be licensed under Art. 7, para 2 of the Markets in Financial Instruments Act.

### 4.2 Inbound

Crowdfunding platforms that shall operate on the Bulgarian market are obliged to fulfil certain requirements under the relevant Bulgarian legislation.

#### 4.2.1 Foreign Crowdfunding platform which addresses Bulgarian investors

As Crowdfunding platforms outside Bulgaria appear to be "foreign", and in view of the application of the Markets in Financial Instruments Act, by analogy, they have to identify

their clients and the transactions executed for their account with the Financial Supervision Commission within a certain period of time.

#### **4.2.1.1 Crowdfunding platform**

The EU rules on financial instruments is aimed at enhancing the integration, competitiveness and efficiency of financial markets within the Union which has an impact on Bulgaria to some extent, the two legislative instruments are closely related – Regulation (EU) No 600/2014 (MiFIR) and Directive 2014/65 / EC (MiFID II).

Under the approach agreed with the European Parliament:

- the deadline for Member States to transpose MiFID II into national law will be 3 July 2017;
- the date of application of both MiFID II and MiFIR will be 3 January 2018.

The new rules seek to simplify the administrative obligations related to the publication of prospectuses.

The question that arises is whether the new rules will push more Bulgarian companies to the Bulgarian Stock Exchange (BSE). Given the fact that banks are the main sources of funding in Bulgaria, the new rules appear to be favourable for small and medium-sized enterprises. The new rules provide for a number of reliefs for smaller public offerings, with the main purpose of making changes to ease the administrative and financial burden of the process that has so far fuelled smaller companies to seek financing through the stock exchange.

While these changes have the potential to popularize BSE – Sofia among issuers and investors, it is yet to be seen how and within what timeframes they will be trans-posed into the new rules in the Bulgarian legal framework.

It is important to note that certain steps have already been taken in Bulgaria to implement these measures to some extent. In Bulgaria, since the end of 2016 there is a Capital Markets council which purpose is to implement the guidelines of the European Commission.

#### **(1) Licence obligations**

The Markets in Financial Instruments Act supplements the MiFID II with respect to the requirements for the persons who manage and control the activities of investment firms and regulated markets in financial instruments as well as for persons who have a qualifying holding in the said companies. In addition, the Markets in Financial Instruments Act regulates state oversight to ensure compliance with this law.

The legal regime established through the Markets in Financial Instruments Act prevents the carrying out of activities in the territory of Bulgaria without a license granted under to referred to law.

#### **(2) Other financial regulation**

In all cases, the activities of Crowdfunding platforms are covered by analogy with laws such as the Currency Act, the Law on Measures against Money Laundering, the Commerce Act.

#### **4.2.1.2 Company / project**

##### **(1) Bulgarian prospectus regulation**

The requirements for the publication of a prospectus are set out in Chapter VI, Section II of the Public Offering of Securities Act. The same law regulates also in detail the cases which exclude the publication of a prospectus. They are the following, but not limited to - offering securities to fewer persons than is prescribed by law; The nominal value of the securities is below the BGN equivalent of EUR 100.000; there has been already published prospectus; resale of securities or final placement of securities through investment intermediaries as long as a valid prospectus is available; securities offered in connection with a takeover by means of an exchange offer, provided that a document is made available to the persons containing information which is regarded by the Financial Supervision Commission as being equivalent to the information contained in the prospectus.

##### **(2) Other financial regulation**

Another law applicable to Crowdfunding is the Law on Measures against Money Laundering activities which include disclosure of information on the handling and management of money, securities or other financial assets.

#### **4.2.2 Foreign Crowdfunding platform which addresses Bulgarian companies**

The Public Offering of Securities Act does not allow the possibility to apply pro-visions of foreign laws and another different legal order other than the Bulgarian one.

Whereas the prospectus is not in Bulgarian language, the issuer, the offeror or the person asking for the admission of the securities to trading on the market shall be obliged to make it available in Bulgarian language.

##### **4.2.2.1 Crowdfunding platform**

###### **(1) Licence obligations**

Under Bulgarian law, any foreign person offering securities on the Bulgarian market should be listed in the Register of Public Companies and Other Issuers of Securities.

###### **(2) Other financial regulation**

Foreign legal entities offering securities must be registered in a special register under the terms of Order № 22 of 29.07.2005 on the terms and procedure for entry and deletion of public companies, other issuers of securities and securities issues in the register of the Financial Supervision Commission.

#### **4.2.2.2 Company / project**

##### **(1) Prospectus regulation**

Please see above the requirements of the Public Offering of Securities Act for the publication of the prospectus in Bulgarian and for the registration of the respective foreign legal entity in a special register.

##### **(2) Other financial regulation**

Subsidiary application will also find the Currency Act, The Law on Measures against Money Laundering, The Commerce Act.

#### **4.3 Outbound**

In cases when Bulgarian Crowdfunding platforms direct their activity outside the country the following regulations should apply:

The persons under Art. 3, para. 2 and 3 of Law on Measures against Money Laundering shall be obliged to ensure the application of the measures under this Act and regulation regarding its branches and subsidiaries in which they have a majority stake abroad to the extent that the relevant foreign legislation permits.

##### **4.3.1 Bulgarian Crowdfunding platform addresses foreign (EU) investors**

Despite the general rule that the prospectus must be prepared in Bulgarian language the Public Offering of Securities Act allows certain exceptions. Where an offer to the public is made or admission to trading on a regulated market is sought in one or more Member States excluding Bulgaria and the Member State of origin is the Republic of Bulgaria, the prospectus shall be drawn up either in a language accepted by the competent authorities of those Member States or in a language customary in the sphere of international finance, at the choice of the issuer, offeror or person asking for admission of the securities to trading on a regulated market. For the purposes of confirmation of the prospectus by the Commission, the prospectus shall be drawn up in the Bulgarian or the English language, at the choice of the issuer, offeror or person asking for admission of the securities to trading on a regulated market.

###### **4.3.1.1 Crowdfunding platform**

##### **(1) Licence obligation**

There is no requirement for registration of a Bulgarian issuer in a foreign country, according to the Public Offering of Securities Act. The issuer must meet the legislative requirements in that other State.

##### **(2) Other financial regulation**

Bulgarian Crowdfunding platforms should be subject to the foreign regulations when operating outside the country.

#### **4.3.1.2 Company / project**

##### **(1) Prospectus regulation**

The Public Offering of Securities Act shall apply only when the Crowdfunding activity takes place on the territory of Bulgaria.

##### **(2) Other financial regulation**

Art. 3b of the Law on Measures Against Money Laundering forbids banks to establish on the territory of the Republic of Bulgaria and foreign banks operating on the territory of the country through a branch to enter into correspondent (bank) relations with banks in jurisdictions, where the said banks do not have a physical presence and do not belong to a regulated financial group. On the other hand, there is no obstacle for other legal entities which are not banks to enter into such correspondence relations. This means there is no obstacle for Bulgarian Crowdfunding platforms to raise funds in Bulgaria for activities in other countries.

#### **4.3.2 Bulgarian Crowdfunding platform addresses foreign companies / projects**

The Public Offering of Securities Act is to be applied as far as the activity is to be performed in Bulgaria.

##### **4.3.2.1 Crowdfunding platform**

###### **(1) Licence obligation**

In cases where a Bulgarian Crowdfunding platform presents foreign companies / projects the rules of art. 126h of the Public Offering of Securities Act should be applied one of which is that any parties to the contract, who are non-resident persons, shall be obligated to name a representative and an address in Bulgaria.

###### **(2) Other financial regulation**

By analogy, all other relevant regulations should be applied as above.

##### **4.3.2.2 Company / project**

###### **(1) Prospectus regulation**

MiFID II has not yet been implemented in Bulgaria.

###### **(2) Other financial regulation**

Pursuant to Ordinance № 22 of 29.07.2005 on the conditions and procedure for entry and deletion of public companies, other issuers of securities and issues of securities at the Register of the Financial Supervision Commission, foreign issuers have to submit additional documents from the country of origin.

## 4.4 Impact of EU regulation

### 4.4.1 Prospectus rule / regimes

No or almost no impact on Crowdfunding in Bulgaria.

### 4.4.2 AIFM-Directive

No or almost no impact on Crowdfunding in Bulgaria.

### 4.4.3 MiFID / MiFID II

No or almost no impact on Crowdfunding in Bulgaria.

### 4.4.4 PSD / PSD II

May be applicable to platform operators in Bulgaria.

## 4.5 Summary

We consider that the following regulatory and factual barriers hinder crossborder activities of Crowdfunding platforms from a Bulgarian perspective:

- The lack of an explicit legal framework for Crowdfunding;
- Even in the light of the applicable by analogy laws like The Credit Institutions Act; The Law on Payment Services and Payment Systems; The Public Offering of Securities Act; Markets in Financial Instruments Act; The Law on the activities of collective investment schemes and other collective investment undertakings; The Law on Measures against Money Laundering and Currency Act, it is not possible to ascertain general criteria applicable to legal organizational form of Crowdfunding platforms;
- In the absence of legal regulation and intensive practice at European level about Crowdfunding it requires the drafting of model contracts and standardized templates of documents between participants in the Crowdfunding platforms;
- There are no risk allocation rules among participants in the Crowdfunding platforms;
- There are significant problems for the acquisition of intellectual property rights related to some products of Crowdfunding platforms;
- Lack of mechanism for control by specially authorized state bodies over the Crowdfunding platforms;
- As there is no legal regulation for Crowdfunding in Bulgaria, this creates difficulties in obtaining local passport licenses;
- Lack of clear rules on applicable law.

## 5 Lessons learned from Bulgaria regulation for a possible harmonized European Crowdfunding regulation

Considering the aim of most of the Bulgarian regulations to protect investors from risky investments it will be good if the Bulgarian legislator recognises the importance of Crowdfunding as a new kind of funding and is willing to grant Crowdfunding the possibility to be established in the market through exception of Crowdfunding from most regulatory requirements (in particular prospectus requirement), but also the Law on Payment Services and Payment Systems which applies to payment transactions related to the collection or delivery of cash, performed in a non-commercial manner in the framework of a charitable or other non-profit-making activity and is an obstacle for the model of Donation Crowdfunding. The same refers to the Currency Act as well.

The referred to above obstacles should be taken into consideration in the preparation of the future harmonised legislation on an European level.

### 5.1 Role model ("dos")

The adoption of a special law for Crowdfunding will create a legal framework for a new phenomenon which already exists in the Bulgarian reality. Adoption of explicit legal regulation of Crowdfunding in Bulgaria shall set clear and simple rules and procedures. This includes also measures for protection of the investors in Crowdfunding projects. On the other hand measures for increase of people's trust in Crowdfunding projects should be taken having in mind the impact of the financial pyramid schemes which have caused substantial turbulence in Bulgaria and in the other Balkan countries in the 90s.

### 5.2 Aspects that should be avoided ("don'ts")

The adoption of a special law for Crowdfunding should comply with the effective regulations that may be and are applied to Crowdfunding at present and should avoid an eventual collision in this respect with other effective legislation closely related to Crowdfunding. In case of adoption of legal framework for Crowdfunding in Bulgaria it should provide clear rules about the protection of intellectual property over the Crowdfunding projects exposed in Bulgarian platforms, clear contractual rules between the platforms and the investors. In this connection should decrease of the administrative burden for the investors and the business, including licensing exemption in certain cases.

## 6 Conclusion

The development of Crowdfunding in the Bulgarian legislation creates the necessity for a specific law on Crowdfunding.

In view of future developments in the referred to sector, it should be pointed out that there is a need to rely on the market mechanisms and to ensure that support measures are transparent and equal for the potential investors. There is also a need to simplify the complex administrative procedures, especially for any projects connected to Crowdfunding.

Therefore, through reasonable legislative mechanisms and proper quality and financial control in the sector, there are good future perspectives for the development of the Crowdfunding platforms at all. The latter have not been utilized essentially as of this date. It is important that this type of funding mechanism finds finally a regulatory base in Bulgaria and later on to be included in the harmonisation process of renewable electricity policies within the European Union.

## 7 Summary – Crowdfunding regulation

|   |  |
|---|--|
| <b>Country</b>  | <b>Bulgaria</b>  |
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <p>In recent years several platforms of the type Peer-to-Peer (P2P) have been developed in Bulgaria. The most famous of them are: Iuvo; Klear; Mintos and Twino. These platforms use different types of funding and a different pattern of action. For example, some of them use originators - ie financing by borrowers from a non-banking sector like Iuvo, Mintos and Twino. The other types of platforms are characterized by lending money first and then looking for projects through which to repay the money.</p>  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• There are no explicit legal regulations for Crowdfunding. As a result, some of the current legislation should be applied by analogy, namely - Credit Institutions Act; Law on Payment Services and Payment Systems; Public Offering of Securities Act; Markets in Financial Instruments Act; Law on the activities of collective investment schemes and other collective investment undertakings; Commercial Law; Law on Measures against Money Laundering; Currency Act.</li> <li>• The operator of the platform may be required to be licensed / registered either as a financial or a credit institution by the Bulgarian National Bank in accordance with the Law on Credit Institutions, respectively with the Law on Payment Services and Payment Systems.</li> <li>• Further to the change in 2016 of the Public Offering of Securities Act, it is stipulated that the same one shall not apply to commercial offers for securities issued by companies whose purpose is the collective investment of funds raised through a public offering of securities which operates on the principle of risk spreading. This means that provided such conditions are agreed in the case of Crowdfunding, the Public Offering of Securities Act will not be applied for Crowdfunding, which again highlights the need to introduce special legislation in the field of Crowdfunding in Bulgaria.</li> <li>• Not allowed enforcement and establishment of collateral on the cash and financial instruments of clients for the obligations of the investment intermediary according to The Markets in Financial Instruments Act.</li> <li>• According to the Law on Measures against Money Laundering notification related to suspicion of money laundering or of the presence of criminal assets may also take place electronically with qualified electronic signature or issued by the State Agency for National Security an access certificate.</li> <li>• The provisions of the Commercial Law can be applied to the Crowdfunding as regards the legal form of the companies; the governing bodies; the distribution of profits and many others.</li> <li>• According to The Currency Act there is no obligation to file a report within 30 days of receipt of funds from abroad (as it was before)</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for companies which publicly offer securities to investors.</li> </ul>   |

|                                      |  |
|--------------------------------------|--|
|                                      | <ul style="list-style-type: none"> <li>• Threshold: EUR 100.000 per issuer within 12 months.</li> </ul>  |
| <b>AIFMD-regulation</b>              | <ul style="list-style-type: none"> <li>• With regard to the management of the alternative investment funds (AIFs) a chapter was adopted in the Law on Collective Investment Schemes and Other Undertakings for Collective Investments in 2013 which provides for detailed regulation of the activity of the fund managers, including their registration/licensing, requirements for their organization, terms and conditions in case of trans-border management. The competent body which shall regulate and supervise the activities of AIFs and their managers shall be the Financial Supervision Commission.</li> <li>• From 2016 Individuals who manage venture capital funds or social entrepreneurship funds and wish to use the EuSEEC or EuSEF designation for alternative investment schemes managed by them are registered by the Commission pursuant to Art. 14 of Regulation (EU) No 345/2013, respectively Art. 15 of Regulation (EU) No 346/2013.</li> <li>• Pursuant to the Law on Collective Investment Schemes and Other Undertakings for Collective Investments, the Crowdfunding financing shall not fall within the scope of its application.</li> <li>• It shall apply to closed-end investment companies only, as far as the special investment purposes companies are excluded from the scope of application of the Directive.</li> </ul> |
| <b>Payment service regulation</b>    | <ul style="list-style-type: none"> <li>• Transfer of funds through operator may constitute money remittance service – in future, the operator of the platform may be required to be licensed / registered either as a financial or a credit institution by the Bulgarian National Bank in accordance with the Law on Credit Institutions, respectively with the Law on Payment Services and Payment Systems.</li> </ul>  |
| <b>Consumer credit regulation</b>    | <ul style="list-style-type: none"> <li>• At present, lending agreements, including between related parties or between a local and foreign entities are subject to a registration under the Currency Act in a special register at the Bulgarian National Bank.</li> </ul>   |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• The Commerce Act</li> <li>• The Law on Measures against Money Laundering</li> <li>• The Currency Act</li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addressing Bulgarian investors</b></p> <p>→ identify their clients and the transactions executed for their account with the Financial Supervision Commission</p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- If the platform has a foreign MiFID licence it can generally conduct business in Bulgaria without a local licence</li> <li>- If the platform has no such licence, it must obtain a local one</li> </ul> <p><i>Foreign company / project</i></p> <p>→ Public Offering of Securities Act applicable for prospectus requirements</p> <p><b>Foreign Crowdfunding platform addressing Bulgarian companies</b></p>   |

|                                |  |
|--------------------------------|--|
|                                | <p>→ any foreign person offering securities on the Bulgarian market should be listed in the Register of Public Companies and Other Issuers of Securities</p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- Needs to be listed in Register of Public Companies and Other Issuers of Securities</li> <li>- other Bulgarian regulations may be applicable (see above)</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>- Public Offering of Securities Act applies for the publication of the prospectus in Bulgarian and for the registration of the respective foreign legal entity</li> </ul>  |
| <b>Outbound</b>                | <p><b>Bulgarian Crowdfunding platform addresses foreign (EU) investor</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- no requirement for registration of a Bulgarian issuer in a foreign country, according to the Public Offering of Securities Act</li> <li>- The issuer must meet the legislative requirements in that other State</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>- Public Offering of Securities Act shall apply only when the Crowdfunding activity takes place on the territory of Bulgaria</li> </ul> <p><b>Bulgarian Crowdfunding platform addresses foreign companies / projects</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- The Public Offering of Securities Act is to be applied as far as the activity is to be performed in Bulgaria</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>- Bulgarian law does not apply; MiFID II has not yet been implemented in Bulgaria</li> </ul> |
| <b>Impact of EU Regulation</b> |  |
| <b>Prospectus regulation</b>   | No or almost no impact on Crowdfunding in Bulgaria.  |
| <b>AIFM-Directive</b>          | No or almost no impact on Crowdfunding in Bulgaria.  |
| <b>MiFID / MiFID II</b>        | No or almost no impact on Crowdfunding in Bulgaria.  |
| <b>PSD / PSD II</b>            | May be applicable to platform operators in Bulgaria.   |

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# Croatia

## 1 Recent developments in the market of Crowdfunding in Croatia

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

There have been no recent developments in the use of the Equity Model in Croatia. There still appears to be little or no Crowdfunding in Croatia based on the Equity model.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There have been no recent developments in the use of the Lending Model in Croatia. There still appears to be little or no Crowdfunding in Croatia based on the Lending model.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

Crowdfunding in Croatia is based almost exclusively on the Donations or Rewards model. The past two years have seen a significant drop in the total funds raised in Crowdfunding campaigns in the country. While in 2015 the amount of funds collected for Croatia based Crowdfunding projects was USD 750.000,00, in 2016 the amount was only USD 300.000,00. Approximately two thirds of that revenue was collected by a single project (*Vitastiq*).

All or almost all Crowdfunding activity in Croatia is operated through international platforms. The most frequently used platform is *Indiegogo*. Other well-known platforms, such as *Kickstarter*, are either less commonly used or are unavailable in Croatia.

Croatia appears to be too small a market to develop significant platforms of its own. Croinvest.eu, a platform developed in 2014 for the use of equity, lending and donation based Crowdfunding, appears to host little, if any, new funding activity. Other projects for local platforms, such as *Doniratica*, have not taken off.

While the use of Crowdfunding is currently in decline, public awareness about Crowdfunding in the country appears to be growing. *Crowdfunding akademija*, a UNDP backed project, promotes Crowdfunding in Croatia and in the surrounding region and organises education for groups and individuals interested in launching Crowdfunding campaigns. There have also been other attempts to promote Crowdfunding among NGO's, start-ups and communities.

### 1.4 Real Estate Crowdfunding / Renewables Crowdfunding

There has been no known use of Crowdfunding in real estate financing in Croatia. Renewable Crowdfunding has been used but very infrequently. In a few projects, all of them donations based, Crowdfunding was used to finance the use of solar energy in public buildings, such as schools.

## 1.5 International approach

As already mentioned, all or almost all Crowdfunding activity in Croatia is conducted through platforms located abroad. In our view, harmonisation of the regulation of Crowdfunding would allow more predictability for Croatian investors and campaigners and would allow the Croatian market to benefit from the experience of larger jurisdictions.

## 2 Recent developments regarding Crowdfunding regulation in Croatia

Over the past period there have been no significant developments in Croatia with respect to the regulatory framework relating to the use of Crowdfunding in Croatia.

## 3 Current Regulation of Crowdfunding in Croatia

### 3.1 Licence under the Capital Market Act and Open-Ended Investment Funds Act

#### 3.1.1 Equity Model

Under the Croatian Capital Market Act, anyone intending to provide “investment services” and conduct “investment activities” in Croatia requires a written licence from the domestic Financial Services Supervisory Authority (*Hrvatska agencija za nadzor financijskih usluga* – “HANFA”), or from Croatian National Bank (“CNB”) if a credit institution is at hand.

The “investment services and activities” are defined as (inter alia) the brokering of business involving the purchase and sale of financial instruments (investment brokering), the purchase and sale of financial instruments in the name of and for the account of others (contract brokering), the placement of financial instruments without commitment to take up those instruments (placement of financial instruments), portfolio management, investment counselling, safeguarding and administering investments (including custodial services).

“Financial instruments” within the meaning of the Capital Market Act notably include transferable securities, units in collective investment funds, money market instruments options, futures, swaps, forward rate agreements and other derivative instruments linked to securities, currency, interest rates or returns.

“Transferable securities” are those types of securities which are transferable on capital markets, including, inter alia, (a) stock corporation shares and other equivalent securities representing shares in the capital or in membership rights within companies, and share deposit certificates; (b) bonds and other forms of securitized debt, including certificates of deposit relating to such securities; (c) any other security which permits the purchase or sale of securities described in the preceding paragraphs; d) any other security based on which a cash payment may be made as determined with reference to securities, currency, interest rates, returns, commodities, indices or measures.

Depending on the Crowdfunding model used, there is the possibility that the fund seeker or the platform could in fact be considered as operating an open-ended public collective

investment fund (scheme). This interpretation could arise taking into account that the “investment fund” can refer to a body corporate or a collection of assets and that typically the investors would not have day-to-day oversight of management decisions. In such case, the applicable rules mandate both obtaining requisite approval from HANFA and registering with the relevant registry.

On the other hand, where a campaign would seek finance only through stakes not transferable on capital markets (e.g. shares in private limited liability companies, or stakes in a cooperative or silent partnership stakes) such regime would fall outside Croatian capital markets regulation, and no licence from securities regulator would be required.

However, it should be noted that due to complete lack of Crowdfunding activity in Croatia until very recently, no settled practice on licencing issues has yet been developed. There is currently no available information on whether the Croatian legislation will change in a way where Crowdfunding would be separately regulated.

### **3.1.2 Lending Model**

To the extent that the platform would entail dealing in bonds or others transferable debt securities (to the extent these are deemed “transferable securities” in terms of Capital Market Act), an appropriate licence would have to be obtained from HANFA and/or CNB, similarly as with the Equity Model. On the other hand, if the loans would not be transferable nor otherwise be structured in a way qualifying as transferable securities, no such licence would be necessary.

Furthermore, to the extent that commercial lenders would use Crowdfunding to borrow to individual borrowers (consumers), the Croatian Consumer Credit Act would generally apply and a proper licence from the Ministry of Finance or CNB would generally be required for certain types of lending activity. There will also be implications for the form and content of the lending agreement.

### **3.1.3 Donations or Rewards Model**

Crowdfunding projects involving donations from the general public do not qualify as investment services or activities. Platforms and projects operating Donations or Rewards Model are therefore not caught by Croatian financial services regulations.

The same should apply, in our view, to rewards-based Crowdfunding projects given that in such projects the reward is non-monetary and is not intended to create profit for the donor. It is conceivable however that, in certain scenarios, rewards-based projects are characterised by the competent Croatian authorities as subject to financial services regulations.

### **3.1.4 Prospectus requirements**

Under the Capital Market Act, a prospectus is mandated for a public offering of securities on the territory of Republic of Croatia. However, as a rule this refers only to offering of “transferable securities” (those transferable on capital markets), such as stock corporation

shares. Therefore, if an Equity Model campaign would offer only stakes not transferable on capital markets (e.g. shares in private limited liability company, stakes in a cooperative or silent partnership stakes), it appears that there would be no prospectus requirement.

Likewise, the Lending Model of Crowdfunding could generally be subject to the rules on prospectus obligations only in cases where the lending involves bonds or other debt securities transferable on capital markets. For the Donations and Rewards Model it appears that the prospectus requirements will not be applicable.

Finally, even with “transferable securities”, there are a number of exceptions to the prospectus requirement, notably for offers worth less than EUR 5 million in the EU, calculated for a 12- month period.

### 3.2 Regulation of Crowdfunding under the AIFMD regime

In Croatia the Alternative Investment Fund Managers Directive (2011/61/EU) (“AIFMD”) has been implemented via the Alternative Investment Funds Act 2013 (“AIFA”) which applies as of 1 July 2013 (the day of Croatia’s accession to the EU) and relevant bylaws.

AIFA governs, inter alia, the terms for establishment and operation of AIFs and AIF management entities (“AIFMs”). AIF is defined as an investment fund established for the purpose of: (i) raising assets through public or private offer; (ii) investing these assets into different types of property in accordance with a strategy and investment targets defined upfront; and (iii) exclusively for the benefit of investors in such AIF.

AIFs can be open-ended (generally only a collection of assets without legal personality, managed by AIFM) or closed-ended (a company formed as stock corporation or a private limited liability company, managed by AIFM). Open-ended AIFs are not the public open-ended investment funds regulated by the Open-Ended Investment Funds Act, and they are not subject to the licence requirements prescribed therein. Shares in AIFs can generally be offered both publicly and privately.

A Crowdfunding scheme where a non-standard profit sharing arrangement is provided might be construed as involving an investment fund in form of AIF. Furthermore, AIFA does not offer conclusive guidance on whether an operating company seeking funding by way of Crowdfunding might be considered as an AIF. It could be argued that the typical start-up seeking funding for its general commercial business is not AIF as (i) such company does not invest the received capital “in accordance with an upfront business strategy” (but only to finance its operations), and/or that (ii) the assets are not used “exclusively” for the benefit of the investors (as the fund-seeker is typically utilizing the majority or at least a small part of funds for its own business benefit).

Finally, Crowdfunding platform operators do not qualify as AIF’s given that they do not raise capital from investors themselves but only provide a technical facility for capital-raising by the fund-seeker.

### 3.3 Licence under the Payment Services Act

The transmission of funds between the investor and the crowd-funded business via the Crowdfunding platform may involve the platform operator providing "money remittance" services as defined under the Croatian Payment Services Act ("PSA"). Money remittance services generally require authorization from CNB.

However, money remittance services under PSA do not extend to payments made by "commercial agents" authorized to negotiate or conclude contracts on behalf of the payer and payee. Therefore, depending on the overall structure, the platform operators would likely be able to invoke this exception and avoid the licencing obligation.

### 3.4 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Croatian Act on Prevention of Money Laundering and Financing of Terrorism
- Croatian Act on Protection of Personal Data
- Croatian Companies Act.

## 4 Regulatory barriers for Crowdfunding crossing borders

As already mentioned, almost all Crowdfunding in Croatia is made by means of donations or rewards based models. The issues concerning cross-border regulation of equity or lending based Crowdfunding are therefore less relevant for the practice, as matters currently stand. One should hope that EU wide regulatory activity could bring about more predictability and encourage the wider use of Crowdfunding in Croatia beyond the donations/rewards model. The analysis below takes into account the fact that currently no active Crowdfunding platform exists in Croatia and that almost all Crowdfunding is donations/rewards based and is conducted via platforms based abroad.

### 4.1 Applicable law

Croatian securities legislation and other capital market laws and regulations do not apply only to financial services providers established in Croatia, but also those established abroad provided that they target the Croatian market, for example by specifically soliciting investments via email or internet. HANFA or CNB, as appropriate, may therefore request foreign based providers to obtain appropriate licences or comply with other requirements under Croatian law.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addressing Croatian investors

To the extent that Crowdfunding platforms may qualify as financial service providers, Croatian capital markets laws and regulations can apply when foreign based platforms target investors based or resident in Croatia. Mere availability to a Croatian investor of an

international platform would not be sufficient to trigger the application of Croatian regulatory law. What would be required, in our view, is intentional solicitation of business in Croatia indicated by, for example, the use of Croatian language, availability of Croatian phone lines or presence of agents operating in Croatia. Unfortunately, there has been no guidance from HANFA or CNB as to when specifically Croatian regulatory law would have extraterritorial application in the context of Crowdfunding.

#### **4.2.1.1 Crowdfunding platform**

The applicability of Croatian regulatory law to a Crowdfunding platform depends on whether the platform has a MiFID licence from another Member State.

If the platform is in the possession of such a licence, it is permitted to operate in Croatia according to the equity model involving transferrable securities, without having a presence in Croatia so long as it makes the required notification under Croatian law. Such an “EU Passport” would presumably also allow the platform to provide financial services relating to shares or other rights not covered by the licence, such as soliciting investments into shares in a Croatian limited liability company or loan based arrangements.

If the platform does not own such a licence, it would have to obtain a Croatian licence from HANFA or CNB.

#### **4.2.1.2 Company / project**

Financial regulations that are applicable to Croatian companies or projects apply also to those companies or projects which use foreign based Crowdfunding platforms to attract investors in Croatia.

### **4.2.2 Foreign Crowdfunding platform addressing Croatian companies**

If a foreign Crowdfunding platform seeks to attract fund-seekers from Croatia (e.g. Croatian companies) to use the platform to attract funds, the platform does not provide financial services as it does not intend to make any public offers or provide other regulated services in the Croatian territory. Therefore, for such activity, in our view, the platform does not have to obtain a licence from HANFA or CNB or own an EU passport.

#### **4.2.2.1 Crowdfunding platform**

In this scenario the platform does not target investors in Croatia, so that no licencing requirements apply. Other financial regulations may be applicable, but only to the extent that they would involve issuing by the platform of transferrable securities, such as bonds. In such a case regulation concerning prospectuses and other matters relating to public issuance of securities may apply.

#### **4.2.2.2 Company / project**

Financial regulations that are applicable to Croatian companies or projects apply also to those companies or projects which use foreign based Crowdfunding platforms to attract investors in Croatia.

### **4.3 Outbound**

Currently there appear to be no active local platforms in Croatia. Even if one were to be successfully established in the near future, it appears difficult to imagine that it would successfully target also other EU markets. If this were to occur, the following questions would theoretically occur: how such platform would be regulated to the extent that it addresses foreign (EU) investors (4.3.1) and how it would be regulated to the extent that it addresses foreign (EU) companies or projects (4.3.2).

#### **4.3.1 Croatian Crowdfunding platform addresses foreign (EU) investor**

In this scenario, a Croatian platform attracts investment into a Croatian company or other project only from investors located in another Member State.

##### **4.3.1.1 Crowdfunding platform**

Because in this scenario no investment from Croatia is being attracted, Croatian financial regulatory law does not apply. We note that, depending on the circumstances, it may be difficult for the platform to demonstrate to the regulators (HANFA or CBA) that only foreign, and not Croatian investors are targeted by the platform.

If this is indeed the case, the platform is not subject to Croatian licencing requirements or is it subject, as a matter of principle, to other regulatory requirements under Croatian law.

##### **4.3.1.2 Company / project**

Because Croatian investors are not aimed by the platform, the company or project seeking funds via the platform are not subject to Croatian prospectus and other regulatory requirements, in this scenario.

#### **4.3.2 Croatian Crowdfunding platform addresses foreign companies / projects**

In this fact pattern, a Croatian platform solicits investment into a foreign company from Croatian investors.

##### **4.3.2.1 Crowdfunding platform**

Because, in this scenario, investment is sought from Croatian investors, all the licencing and other requirements concerning the platform apply. In terms of applicability, this fact pattern is no different from the situation where the platform seeks investment into a Croatian company or project (see above under 3).

#### 4.3.2.2 Company / project

If the investment sought by the platform relates to rights in relation to shares in a limited liability company or loans or other rights that are not publically traded, Croatian regulatory law does not apply. If the investment is into tradable financial instruments, the company or the project will normally be subject to prospectus requirements and other requirements of its home Member States regulatory law. If the company or the project is not adequately regulated in its home country, Croatian regulatory authorities shall require the platform to discontinue seeking investment for the company/project in Croatia.

### 4.4 Impact of EU regulation

#### 4.4.1 Prospectus rule / regimes

The EU Prospectus Directive has been transposed into Croatian law, primarily through the Capital Markets Act. Its relevance for Crowdfunding is very limited because, as mentioned earlier, there has been no significant use of any equity or loan based Crowdfunding models in Croatia.

#### 4.4.2 AIFM Directive

The AIFM Directive has also been transposed into Croatian law by the enactment of the Alternative Investment Funds Act. The use of alternative investment funds in Croatia has been relatively limited. There has been no experience in Croatia with the application of alternative investment models in the context of Crowdfunding.

#### 4.4.3 MiFID / MiFID II

For the reasons indicated above capital market directives, including MiFID, have had no impact on the Crowdfunding market in Croatia.

#### 4.4.4 PSD / PSD II

The Payment Services Directive was implemented in Croatia by the adoption of the Payment System Act (*Zakon o platnom prometu*) in 2011. Crowdfunding platforms would presumably be entitled to rely on the exception provided for commercial agents, but there has been no published guidance by the regulators on this issue. The more conservative option for the platforms appears to be to use banks or other licenced payment service providers for the transmission of funds from their funders to fund seekers.

### 4.5 Summary

For the market of its size, facilitation of cross-border Crowdfunding would be essential for future development of Crowdfunding in Croatia. More legal certainty as to whether and to which extent a campaign financed across borders can be regulated by various Member States involved could encourage the use of Crowdfunding which has been used very scarcely, beyond the donations/rewards model.

## 5 Lessons learned from Croatia's regulation for a possible harmonized European Crowdfunding regulation

### 5.1 Role model (“dos”)

Given the lack of experience with Crowdfunding as well as the absence of any attempts by the legislator to adjust the financial regulation specifically to the needs of the Crowdfunding market, it appears that there are no rules or practices in Croatia which may serve as a model for any future EU wide Crowdfunding regulation.

### 5.2 Aspects that should be avoided (“don’ts”)

For the same reasons, we see no cautionary tales from Croatia that we could point to.

## 6 Conclusion

Croatia has had very limited experience with Crowdfunding, particularly with equity or lending based models. Almost all Crowdfunding activity focuses on international donations or rewards based platforms.

There have been no attempts by the legislator or the regulators to address the needs of the Crowdfunding industry in particular. Depending on the model used, Crowdfunding may be applicable to some Croatian financial regulations, but because of the lack of demand, there has been no experience in applying those regulations to Crowdfunding specifically.

In our view, harmonisation of the regulation of Crowdfunding would allow more predictability for Croatian investors and campaigners and would allow the Croatian market to benefit from the experience of larger jurisdictions.

## 7 Summary – Crowdfunding regulation

| Country   | Croatia  |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• No legislative or other regulatory developments affecting the regulation of Crowdfunding.</li> <li>• No active local Crowdfunding platforms</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• No regulatory practice</li> <li>•</li> <li>• Certain types of Equity Model and Lending Model are potentially subject to a regulated regime under local securities and investment funds laws.<br/>→ HANFA and/or CNB authorisation and registration required</li> <li>• Depending on the structure, Donations/Rewards Model is not subject to financial services regulation</li> </ul>   |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for offering of securities transferable on capital markets.</li> <li>• Threshold: EUR 5 million EU-wide per issuer within 12 months</li> </ul>   |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Legislation only recently implemented and no regulatory practice</li> <li>• Typical start-up company seeking funding for regular operations should generally not constitute an AIF</li> <li>• Crowdfunding structure could constitute an AIF if it includes profit share arrangements otherwise than in a commercial company</li> <li>• Depending on the structure, funding by non-transferable loans or contributions under Donations/Rewards Model should not entail an AIF<br/>→ Crowdfunding platforms are likely not AIFM</li> </ul> |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Transfer of funds through operator may constitute money remittance service<br/>→ Ministry of Finance / CNB authorisation required</li> <li>• Exemption for "commercial agents" likely to apply to operators of Crowdfunding platforms</li> </ul>  |
| <b>Consumer credit regulation</b>                     | <p>If consumer borrowers are permitted on a platform (Lending Model) a consumer credit licence is generally required</p> <p>→ implications for the form and content of the lending agreements</p>  |

|                                      |  |
|--------------------------------------|--|
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Croatian Act on Prevention of Money Laundering and Financing of Terrorism</li> <li>• Croatian Act on Protection of Personal Data</li> <li>• Croatian Companies Act</li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addressing Croatian investors</b></p> <p>→ Croatian law generally applicable</p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- If the platform has a foreign MiFID licence it can generally conduct business in Croatia without a local licence</li> <li>- If the platform has no such licence, it must obtain a local one</li> </ul> <p><i>Foreign company / project</i></p> <p>→ Croatian law generally applicable</p> <p><b>Foreign Crowdfunding platform addressing Croatian companies</b></p> <p>→ Croatian law generally does not apply</p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- Croatian licencing requirements not applicable</li> <li>- other Croatian regulations may be applicable, but only in relation transferrable securities</li> </ul> <p><i>Company / project</i></p> <p>→ Croatian prospectus and other requirements apply</p> |
| <b>Outbound</b>                      | <p><b>Croatian Crowdfunding platform addresses foreign (EU) investor</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- Croatian financial regulatory law does not apply</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>- company or project not subject to Croatian prospectus and other regulatory requirements</li> </ul> <p><b>Croatian Crowdfunding platform addresses foreign companies / projects</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>- Croatian licencing and other requirements concerning the platform apply</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>- Croatian law does not apply</li> </ul>  |
| <b>Impact of EU Regulation</b>       |  |
| <b>Prospectus regulation</b>         | No or almost no impact on Crowdfunding in Croatia.   |

|                         |   |
|-------------------------|---|
| <b>AIFM-Directive</b>   | No or almost no impact on Crowdfunding in Croatia.  |
| <b>MiFID / MiFID II</b> | No or almost no impact on Crowdfunding in Croatia.  |
| <b>PSD / PSD II</b>     | May be applicable to platform operators in Croatia. |

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# Cyprus

## 1 Recent developments in the market of Crowdfunding in Cyprus

There have been no significant developments in Cyprus regarding the Crowdfunding, as the market and remains largely under-developed and no Crowdfunding specific legislation has been put in place to expressly provide for and regulate the relevant matters.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

No Crowdfunding platforms exist in Cyprus under the Equity Model.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

No Crowdfunding platforms exist in Cyprus under the Lending Model.

### 1.3 The Donations or Rewards Model

There are very few Crowdfunding platforms in Cyprus based on the donations or rewards - based Crowdfunding Model which present campaigns supporting charitable causes or the promotion of innovative ideas.

### 1.4 Real Estate Crowdfunding/Renewable Crowdfunding

There are no Crowdfunding projects in Cyprus purporting to finance real estate and/or renewable energy projects.

### 1.5 International approach

We are not aware of any foreign Crowdfunding platforms wishing to enter the Cyprus market; however, we understand that there are certain foreign platforms presenting campaigns relating to charitable causes in Cyprus.

## 2 Recent developments regarding Crowdfunding regulation in Cyprus

Cyprus has yet to enact specific legislation regulating Crowdfunding and instead, it is the applicable European Union (EU) legislation (either in the form of directly applicable regulations or directives transposed into national law) that sets out the regulatory framework and provides the necessary guidance for regulating the lending-based and investment-based Crowdfunding models in Cyprus.

## 3 Current Regulation of Crowdfunding in Cyprus

### 3.1 License under MiFID Law or the Business of Credit Institutions Law

#### 3.1.1 Equity Model/Lending Model

##### (1) General Rule

The provision of investment services and/or the performance of investment activities in connection with financial instruments in Cyprus falls within the scope of and is regulated by the Investment Services and Activities and Regulated Markets Law, Law 144(I)/2007 (“MiFID Law”), transposing in Cyprus the Markets in Financial Instruments Directive 2004/39/EC (“MiFID Directive”).

According to the MiFID Law, and in line with the MiFID Directive, investment services or activities include the reception and transmission of orders in relation to one or more financial instruments, the execution of orders on behalf of clients, the provision of investment advice, engagement in portfolio management, the operation of a multilateral trading facility, dealing on own account, the placing of financial instruments without a firm commitment basis and the underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis.

As regards financial instruments, these include transferable securities (i.e. securities which are negotiable on the capital market), money-market instruments, units in collective investment undertakings, derivative instruments for the transfer of credit risk, as well as options, futures, swaps and forwards which may be settled physically or in cash. However, subordinated or profit-participation loans to companies – which we understand may be common products for Crowdfunding platforms in other European countries – are not, as a general rule, regarded per se as investment products. Nevertheless, notwithstanding that they may not expressly be caught by the MiFID Law, a case-by-case assessment should be performed to determine whether these loans could potentially trigger any regulatory licensing requirement, either by the Cyprus Securities and Exchange Commission (“CySEC”), i.e. the competent regulator for the provision of investment services or by the Central Bank of Cyprus (“CBC”), i.e. the competent regulator for the provision of any banking services, for the entity accepting such loans as its main activity.

It is likely that a Crowdfunding platform wishing to engage in investment-based Crowdfunding will offer services tantamount to investment services and activities provided for in the MiFID Law. Accordingly, the platform could be receiving orders from investors and transmitting them to the issuer or another third party intermediary, thus performing the activity of reception and transmission of orders, or could be acting on behalf of investors to conclude agreements to buy or sell one or more financial instruments, thus effectively executing orders on behalf of clients within the scope of the MiFID Law.

In view of the above, where a Crowdfunding platform is carrying out business within the scope of the MiFID Law, and to the extent there is no applicable exemption from the application of the MiFID Law, such platform would have to obtain a license from the competent authority in Cyprus, being CySEC, or would have to be a credit institution that has an existing authorization to also provide MiFID regulated services and/or activities under its banking license, or act as the tied agent of an investment firm or credit institution.

Note is made that with regard to the lending model in particular, the Business of Credit Institutions Law 66/1997 (the “Business of Credit Institutions Law”) may be of more relevance. Under the said law it is prohibited for any person, other than a licensed credit institution, to engage in the business of taking deposits or other repayable funds from the public unless it has been previously authorized by CBC. The definition of “credit institution” in Cyprus follows that of Regulation (EU) No 575/2013 (the “CRD IV”) which clarifies that a credit institution is an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account. In view of the above, it would seem unlikely for a Crowdfunding platform, having adopted the lending model, to fall into the above definition that would trigger a banking licensing requirement by the CBC, if the platform does not hold money for own account and therefore does not perform the activity of holding deposits and simultaneously granting credit to others for own account.

## **(2) Exemptions from licensing requirement**

Although the MiFID Law does not entail any exemption specific to Crowdfunding, it does provide several exemptions from its scope, including:

- persons who do not provide any investment services or activities other than dealing on own account unless they are market makers or deal on own account outside a regulated market or an MTF on an organised, frequent and systematic basis by providing a system accessible to third parties in order to engage in dealings with them; or
- persons providing investment advice in the course of providing another professional activity not governed by the MiFID Law, provided that the provision of such advice is not specifically remunerated; or
- persons providing an investment service where that service is provided in an incidental manner in the course of a professional activity and that activity is regulated by legal or regulatory provisions or a code of ethics governing the profession which do not exclude the provision of that service etc.

## **(3) Additional regulatory requirements pursuant to MiFID Law**

Where applicable, the MiFID Law imposes a variety of capital, organizational and conduct of business requirements, aimed at ensuring that client assets are protected, conflicts of interests are avoided, and that the platform acts in the interests of the clients or investors. More specifically, an investment firm licensed under the MiFID Law must have a specified initial capital varying in case the investment firm in question does not deal in any financial instruments for its own account or underwrite issues of financial instruments on a firm commitment basis, but holds client money or securities and engages in the reception and transmission of investors' orders for financial instruments and/or the execution of investors' orders for financial instruments and/or the management of individual portfolios of investments in financial instruments. In the event that an investment firm is active in any or all of the above-named services or activities, but is not authorized to hold client money or

securities, to deal for its own account, or to underwrite issues or on a firm commitment basis, the initial share capital required is significantly lower.

Furthermore, in case of a Crowdfunding platform offering investments through equity and hybrid instruments, solely in the primary market where there are no frequent opportunities to realize and/or dispose of the investment at publicly available market prices, the platform offering such investments would have to carry out an appropriateness assessment regarding its clients. Additionally, platforms remunerated by both projects and investors would have to take measures to ensure that they are acting in the best interests of clients.

It is noted that in accordance with the MiFID Law (and in line with the requirements of the Directive on investor-compensation schemes – Directive 97/9/EC), investment firms licensed under the MiFID Law and credit institutions authorized in Cyprus are not allowed to provide investment services without participating in the respective investment compensation funds, providing investors with access to compensation up to a specified amount where the investment firm is no longer financially able to meet its obligations. As a result of the above, a Crowdfunding platform authorized under the MiFID Law would have to comply with the above requirement as well.

### **3.1.2 Donations or Rewards Model**

Donations-based or reward-based Crowdfunding is not expressly regulated in Cyprus and no investment or banking licensing requirements would be applicable in this type of Crowdfunding.

## **3.2 Prospectus requirements**

### **3.2.1 Equity/Lending Model**

Entities seeking Crowdfunding which involve either the issuing of securities or, in general, offerings of investment products to investors may be required to observe the provisions of the Public Offer and Prospectus Law, Law 114(I) of 2005 (“Prospectus Law”), which implements the provisions of the Prospectus Directive, namely Directive 2003/71/EC.

Under the Prospectus Law a “public offer” means a communication to persons in any form and by any means, presenting sufficient information on the terms of the offer and the securities to be offered, so as to enable an investor to decide to purchase or subscribe to these securities and includes:

- A. the collection of money from the public for the participation in any kind of investment in securities • and
- B. the placing and the offer of securities through investment firms pursuant to the MiFID Law.

The Prospectus Law requires the publication of a prospectus by any entity which offers its securities to the public prior to any such offer of securities or to the admission to trading of such securities on a regulated market, except where certain exclusions or exemptions apply.

The prospectus cannot be published unless approved by the CySEC. Nonetheless, the Prospectus Law applies only where instruments are transferable securities within the definition of MiFID Law, transposing the MiFID Directive.

Furthermore, the Prospectus Law does not apply to the following, inter alia:

- securities included in an offer where the total consideration of the offer in the European Union is less than EUR 5 million calculated over a period of 12 months;
- an offer of securities addressed solely to qualified investors (as defined in the MiFID Law);
- an offer of securities addressed to fewer than 150 natural or legal persons per member state, which are not qualified investors;
- an offer of securities with total consideration in the European Union of less than EUR 100,000, which value shall be calculated over a period of 12 months as to the securities offered during this period.

### **(1) Content of the prospectus**

As regards the content of the prospectus, the Prospectus Law provides that the prospectus must contain all information which according to the specific nature of the issuer and the securities being object of the public offer or admission to trading on a regulated market, is necessary in order to enable investors to evaluate comprehensively the assets, liabilities, financial position, profits and losses and prospects of the issuer and of any guarantor, and of the rights attaching to such securities.

Upon its approval, the prospectus is valid for 12 months, provided that every time there is a substantial amendment to it that may potentially influence the evaluation by investors of the offered securities, a supplementary prospectus must be published, which must be approved by CySEC.

Lastly, it is noted that the prospectus must be accompanied by a summary note drafted in a concise manner and summarizing the content of the prospectus and containing basic information on the offered securities, to aid investors when considering whether to invest in such securities. The summary note should also contain a warning, stipulating, inter alia, that it should be read as an introduction to the prospectus and that the investor should base any decision to invest in the securities on consideration of the prospectus as a whole.

### **(2) Advertisement**

The Prospectus Law provides that (subject to the provisions of Article 34 of Regulation 809/2004) any type of advertisements relating to an offer to the public of securities or to an admission to trading on the Cyprus Stock Exchange (CSE) or on another regulated market that takes place in Cyprus, shall be clearly distinguishable and recognizable and shall state that a prospectus has been or shall be published and indicate the location where investors are able to obtain it, or how investors shall be able to have access to its full text. Furthermore, the

information contained in an advertisement may not be inaccurate or misleading, but consistent and without any conflict or discrepancy with the information contained in the prospectus, and any type of announcement by which a public offer or admission to trading on the CSE or on another regulated market is announced, shall be previously submitted to CySEC.

### 3.2.2 Donations or Rewards Model

As above, donations-based or reward-based Crowdfunding is not expressly regulated in Cyprus, and prospectus requirements will not be applicable for this type of Crowdfunding.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

The Cyprus Alternative Investment Fund Managers Law 56(I)/2013 (the “AIFM Law”) could be applicable to a Crowdfunding platform which manages or markets a collective investment undertaking (other than in the form of Undertakings for Collective Investments in Transferable Securities - UCITS) which raises capital from a number of investors with the aim of investing it in accordance with a “defined investment policy”. In the latter scenario, the investment vehicle itself could form an alternative investment fund (“AIF”), which would have to be authorized by CySEC if established in Cyprus. However, if the investment vehicle constitutes an operating company, it is unlikely that the application of the AIFM Law would be triggered; instead the general provisions of the Companies Law would be applicable to it if it operates as a limited company established under Cyprus law.

In accordance with the Alternative Investment Funds Law, Law 131(I)/2014 (“AIF Law”), an AIF is any collective investment undertaking (other than UCITS) including the investment compartments thereof, which, collectively:

- A. raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and
- B. does not require authorisation pursuant under the Open-ended Undertakings for Collective Investments Law of 2012, Law 78(I)/2012 or pursuant to the legislation of another Member State which harmonises the article 5 of the Directive 2009/65/EC (the “UCITS IV Directive”).

The AIFM Law contains various exclusions from its scope, including:

- A. Holding companies, defined as “a company with shareholdings in one or more other companies, the commercial purpose of which is to carry out a business strategy or strategies through its subsidiaries, associated companies or participants in order to contribute to their long-term value, and which is either a company:
  - Operating on its own account and whose shares are admitted to trading on a regulated market in the Union; or

- is not established for the main purpose of generating returns for its investors by means of divestment of its subsidiaries or associated companies, as evidenced in its annual report or other official documents”.

B. Securitisation special purpose entities defined as “entities whose sole purpose is to carry on a securitisation or securitisations within the meaning of Article 1(2) of Regulation (EC) No 24/2009 of the European Central Bank of 19 December 2008 concerning statistics on the assets and liabilities of financial vehicle corporations engaged in securitisation transactions (ECB/2008/30) and other activities which are appropriate to accomplish that purpose”.

In the event that the AIFM Law applies, a manager of the AIF (or the AIF itself in case it is a self-managed AIF) would have to be appointed, which itself would be subject to organizational and capital requirements. Where the AIF is internally managed (i.e. the AIF manages itself), the initial capital required is EUR 300,000. In case the AIF is externally managed, the external manager would have to have an initial capital of EUR 125,000. Other requirements that would have to be complied with include risk management, asset valuation, disclosure requirements, addressing of conflicts of interest, remuneration practices and management of the AIF’s liquidity. Additionally, a depositary would have to be appointed for the AIF, which can only be either an authorised credit institution, investment firm or other eligible firm but may not be the AIFM.

AIFs may be marketed to professional and retail investors, subject to the observance of further requirements.

In the above context, if the Crowdfunding platform qualifies as an external AIFM, apart from the services of managing and marketing AIFs, it may also be authorized by CySEC to provide other non-core services, such as investment advice, safe-keeping and administration in relation to shares or units of collective investment undertakings and reception and transmission of orders in relation to financial instruments.

### **3.3.1 Project Company seeking funding**

#### **(1) Equity Model**

Project companies might qualify as AIFs within the meaning of the AIFM Law if they seek funding from investors in return for a share in the profits or revenue generated by the project as in the Equity Model.

#### **(2) Lending Model**

As far as investments by means of subordinated loans (or other debt-based investments) are concerned, these may be structured as non-AIF investments for the reason that the investors do not share liability for any losses.

#### **(3) Donations or Rewards Model**

This type of Crowdfunding does not offer any kind of revenue but instead non-financial rewards (usually tickets etc.). Therefore, the funds are not invested for the benefit of the investors and the funding contains no collective investment undertaking such as an AIF.

### 3.3.2 Crowdfunding Platform

Assuming the operator of the Crowdfunding platform will not raise capital from investors for its own business it will not qualify as an AIF. Equally, as it will most probably not manage the relevant company or project being the underlying investment, it will not qualify as an AIFM either.

## 3.4 Regulation under the Payment Services Directive

The money-handling aspect may be of relevance in all types of Crowdfunding. Whether adopting the equity, lending or donations-rewards model, Crowdfunding platforms could be said to be providing the following services as defined in the Payment Services Law, Law 128(I)/2009 (“PS Law”):

- services enabling cash to be placed in, or withdrawn from, a payment account and the operations required for operating a payment account;
- the execution of payment transactions, including transfers of funds on a payment account with the users’ payment service provider or with another payment service provider;
- issuing and/or acquiring payment instruments; or
- money remittance.

In cases where Crowdfunding platforms intend to provide directly the above-listed services they could be regarded as payment service providers (“PSPs”), and as such, unless they are credit-institutions or e-money institutions, must be authorised by the Central Bank of Cyprus.

The PS Law provides different thresholds of initial capital requirements for payment institutions ranging from EUR 20,000 for those offering money remittance services to EUR 125,000 if different services are offered. PSPs must also adhere to requirements relating to own funds, appropriate governance arrangements and internal control mechanisms, transparency requirements and provisions as regards the consequences of non-execution or defective execution of a payment order, including restoration of the amount of the payment transaction.

Note is made however that the PS Law excludes from its scope certain services which could be of relevance for Crowdfunding activities, i.e.:

- payment transactions from the payer to the payee through a commercial agent authorised to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee;
- services provided by technical service providers, which support the provision of payment services, without them entering at any time into possession of the funds

to be transferred, including processing and storage of data, trust and privacy protection services, data and entity authentication, information technology (IT) and communication network provision, provision and maintenance of terminals and devices used for payment services;

- services based on instruments that can be used to acquire goods or services only in the premises used by the issuer or under a commercial agreement with the issuer either within a limited network of service providers or for a limited range of goods or services.

Importantly, the law makes clear that any funds received by payment institutions from payment service users with a view to the provision of payment services shall not constitute a deposit or other repayable funds (as those terms are used for the purposes of the Business of Credit Institutions Law as well as the E-money Law, Law 81(I)/2012). This is of particular importance, when the Crowdfunding platform is operating under the lending model.

### 3.5 Possible additional regulations

Other regulations which may be applicable to a Crowdfunding platform include:

- The E-money Law, Law 81(I)/2012;
- The Distance Marketing of Financial Services Law, Law 242(I)/2004;
- The Consumer Credit Law, Law 106(I)/2010;
- The Prevention and Suppression of Money Laundering Activities Law, Law 188(I)/2007;
- The Processing of Personal Data (Protection of Individuals) Law 138(I) 2001;

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

Cyprus financial regulation will generally apply either in the case where investors domiciled in Cyprus are approached by foreign financial actors (e.g. investment firms or issuers of financial instruments etc.) or in case Cyprus financial actors conduct cross-border investment or banking activities whether in other EU member states or in third countries.

In particular, the MiFID Law applies to the provision of investment and ancillary services, as well as the performance of investment activities on a professional basis in Cyprus, where the provision of investment and ancillary services in Cyprus includes, inter alia:

- A. any provision or offer for the provision of investment and ancillary services, made from a place outside Cyprus to persons within, or resident or domiciled in Cyprus, provided the above provision or offer reaches such persons when they are within or resident or domiciled in Cyprus or where the relevant transaction is concluded within Cyprus;

- B. any provision or offer for the provision of investment and ancillary services, which comes from inside Cyprus or from a person within, resident or domiciled in Cyprus, to persons that are within, resident or domiciled in Cyprus or outside Cyprus;

Nevertheless, the criteria determining how an offer for the provision of services reaches investors resident or domiciled in Cyprus are not expressly set out in any secondary legislation by the competent regulator. This may be important in the case of a Crowdfunding platform established under the laws of another EU member state, as the determination of whether the MiFID Law would be applicable may not be as straightforward.

## 4.2 Inbound

The question is whether the Crowdfunding platform addresses investors in the Republic of Cyprus or accommodates Cyprus companies or projects on its platforms.

### 4.2.1 Foreign Crowdfunding platform addresses Cypriot investors

The Cyprus regulatory framework may be applicable to the:

- Crowdfunding platform; and/or
- Company or project seeking funding

#### 4.2.1.1 Crowdfunding platform

##### (1) License obligations

The applicable regulatory framework will depend on whether the Crowdfunding platform holds, or not, a MiFID license (and therefore a passport) in any other EU member state.

##### (a) The platform holds a MiFID license in another EU member state

##### *Scope of MiFID Law*

As stated further above, the MiFID Law, transposing the respective MiFID Directive, applies to the provision of investment services or activities (i.e. the reception and transmission of orders, the execution of orders on behalf of clients, the provision of investment advice, the engagement in portfolio management, the operation of a multilateral trading facility, the dealing on own account, the placing of financial instruments with or without a firm commitment basis) relating to financial instruments caught within MiFID scope. Such financial instruments include transferable securities, money-market instruments, units in collective investment undertakings, derivative instruments for the transfer of credit risk, as well as options, futures, swaps, forwards which may be settled physically or in cash, etc.

Whereas it is likely that an EU-based Crowdfunding platform may engage in investment-based Crowdfunding addressing Cyprus resident or domiciled investors, in order for the MiFID Law to be applicable, such services shall need to relate to financial instruments as defined in the said Law. By way of example, if the EU-based Crowdfunding platform acts on behalf of Cyprus investors to conclude agreements to buy or sell shares in a private company

(in such case being the project company seeking funding), the MiFID Law will not be applicable. Similarly, Crowdfunding conducted in the form of subordinated and/or profit-participation loans, will also fall outside MiFID as such products are also not regarded as financial instruments. It is not clear whether a specific license may be required for Crowdfunding platforms addressing financial instruments or other investment products not falling within MiFID; CySEC or the CBC (as the case may be) may examine this on a case by case basis when (or if) assessing their specific characteristics.

### ***EU passport***

The MiFID Law provides that an investment firm (“IF”) authorised and supervised by a competent authority of another member state, and therefore a Crowdfunding platform authorized as such, may freely provide investment and ancillary services and/or perform investment activities within the territory of Cyprus, without obtaining a relevant license from CySEC and without establishing a presence in Cyprus, provided that such services and/or activities are covered by its authorisation.

The IF may begin providing services and/or performing activities freely in the territory of Cyprus, when the notification from the competent authority of the home member state is communicated to CySEC, stating the program of operations that the IF intends to apply in Cyprus and in particular the investment services or activities and ancillary services it intends to provide, as well as whether it intends to use tied agents in Cyprus.

In the event that the Crowdfunding platform holds a MiFID License and intends to approach Cyprus investors, it is not clear whether the MiFID license will suffice also for providing financial services relating to financial instruments or products not covered by the MiFID license – e. g. shares in a private company or subordinated profit-participating loans.

#### **(b) The platform has no MiFID license**

As already mentioned, if the Crowdfunding platform intends to address investors resident or domiciled in Cyprus, local regulation will be applicable. Therefore, the Crowdfunding platform must in principle – apply for a license under MiFID provided that it intends to offer investment services or activities in financial instruments falling within MiFID scope.

### **(2) Other financial regulation**

Other financial regulation may be applicable depending on the activities conducted by the EU Crowdfunding platform seeking to provide services in Cyprus, e.g. the Payment Services Law, the E-Money Law, the Business of Credit Institutions Law etc., with relevant passport provisions also being applicable. The foreign platform will also be considered an obliged person under the Cyprus Anti-Money Laundering legislation to the extent that it provides services in Cyprus through a branch.

#### **4.2.1.2 Foreign company / project**

##### **(1) Cyprus prospectus regulation**

In principle, a foreign company (which would be the company seeking funding through a Crowdfunding platform) purporting to offer transferable securities (within the meaning of MiFID) to the public in Cyprus, would have to adhere to relevant provisions of the Cyprus Prospectus Law. Assuming such company already has a prospectus approved by the competent authority of its home member state, prospectus passport provisions would be applicable. In particular, the Cyprus Prospectus Law, provides that where an offer to the public or admission to trading on the Cyprus Stock Exchange or on another regulated market operating in Cyprus takes place, if the home member state is not Cyprus, the prospectus and any supplement to the prospectus approved by the competent authority of the home member state shall be valid, provided that CySEC and ESMA are notified accordingly.

Notably, where the host member state of an EU-based company is the Republic of Cyprus and CySEC finds irregularities or any breaches of the law committed by the issuer, it shall refer these findings to the competent authority of the home member state and to ESMA. Furthermore, where despite the measures taken by the competent authority of the home member state or due to the non-taking of measures by the latter or due to such measures prove inappropriate or inadequate, the issuer persists in breaching the relevant legal or regulatory provisions, CySEC, after informing the competent authority of the home member state, shall take all appropriate measures in order to protect investors, notifying those to the European Commission and ESMA at the earliest possible.

##### **(2) Other regulation**

Depending on whether the foreign company purports to admit its securities to trading on the Cyprus Stock Exchange, additional listing requirements pursuant to the Cyprus Securities and Stock Exchange Law, Law 14(I)/1993 may be applicable. In the event that the foreign company issues subordinated profit-participating loans, these will not in principle be regulated in Cyprus. Finally, foreign companies issuing securities or profit-participating loans will not constitute obliged persons within the meaning of the Anti-money laundering law.

#### **4.2.2 Foreign Crowdfunding platform addresses Cyprus companies**

As above, Cyprus regulation may apply to:

- The Crowdfunding platform; and/or
- The company or project intending to be funded on the Crowdfunding platform

As stated above, Cyprus financial services regulation will be applicable where investors, who are resident or are domiciled in Cyprus, are provided or are offered to be provided with investment services and activities or ancillary services by an investment firm either established in Cyprus or abroad. However, in the event that such investors are not approached, Cyprus regulation may not be applicable. Nevertheless, the Cyprus company

seeking funding shall in any case need to observe the requirements of the Cyprus Companies Law.

#### **4.2.2.1 Crowdfunding platform**

##### **(1) License obligations**

As stated above, to the extent services are not being offered in Cyprus and Cyprus investors are not approached, Cyprus regulation will not apply and the Crowdfunding platform need not adhere to Cyprus licensing requirements.

##### **(2) Other financial regulation**

In case the foreign Crowdfunding platform does not purport to offer any services in Cyprus, no additional Cyprus financial regulation will be applicable.

#### **4.2.2.2 Company / project**

##### **(1) Prospectus regulation**

To the extent that the Cyprus company seeking funding through a foreign Crowdfunding platform purports to issue securities to the public in Cyprus, the Cyprus Prospectus Law will be applicable. Therefore, if such securities are not purported to be issued in Cyprus, the Cyprus Prospectus Law will not be applicable.

##### **(2) Other financial regulation**

The Cyprus Companies Law, Cap. 113 (the “Companies Law”) sets out several requirements in relation to the issue of shares and debentures of a Cyprus company, including that only public companies (i.e. non-private companies with more than 7 members) can offer shares and/or debentures to the public. Therefore, companies offering such securities to the public through Crowdfunding platforms have to take the form of a public company in accordance with the provisions of the Companies Law.

If the securities being issued by the Cyprus company are listed on the Cyprus Stock Exchange, additional listing requirements pursuant to the Cyprus Securities and Stock Exchange Law, Law 14(I)/1993 and the Market Abuse Regulation (Regulation (EU) No 596/2014) may be applicable. It is highly unlikely, however, that the securities of a Cyprus company seeking funding through a Crowdfunding platform will be admitted to trading on a regulated market. Furthermore, with regard to MAR in particular, as the company seeking funding will act through a Crowdfunding platform, and therefore the offering and/or dealing of securities will be performed through the platform, MAR will not be applicable as the requirements of the regulated market and of trading on such market are not met.

If the Cyprus company uses subordinated profit-participating loans, these will not in principle be regulated in Cyprus. Finally, such company will not constitute an obliged entity under the Cyprus Anti-money laundering legislation.

### 4.3 Outbound

In this scenario a Cyprus Crowdfunding platform enters foreign (European) markets and therefore addresses foreign investors.

In this situation, two different alternatives must be considered:

- Cyprus Crowdfunding platform approaches foreign (EU) investors or
- Cyprus Crowdfunding platform approaches Cyprus investors and presents a company or project from another EU member state on its platform

#### 4.3.1 Cyprus Crowdfunding platform addresses foreign (EU) investors

Cyprus financial regulation will be applicable to the extent that the provision of financial services comes from within Cyprus, irrespective of whether such services are being offered to persons outside Cyprus. That being said, insofar as the Crowdfunding platform is domiciled in Cyprus, Cyprus financial regulation may be applicable.

##### 4.3.1.1 Crowdfunding platform

###### (1) License obligation

As stated further above, the MiFID Law applies to the provision of investment and ancillary services and the performance of investment activities on a professional basis in Cyprus where the provision of investment and ancillary services in Cyprus any provision or offer for the provision of investment and ancillary services, which comes from inside Cyprus or from a person within, resident or domiciled in Cyprus, to persons that are within, resident or domiciled in Cyprus or outside Cyprus. Therefore, although Cyprus investors may not be approached, the fact that the provision of investment services comes from within Cyprus, could mean that the Cyprus Crowdfunding platform offering investment services within MiFID scope to investors abroad, would be subject to MiFID Law requirements.

###### (2) Other financial regulation

Insofar as the Cyprus Crowdfunding platform offers investment services under the MiFID Law, it would also be subject to the Cyprus Anti-money laundering legislation. Furthermore, requirements arising from the Cyprus Companies Law will also be applicable, since the Crowdfunding platform is a Cyprus company.

##### 4.3.1.2 Company / project

###### (1) Prospectus regulation

The Prospectus Law will be applicable in the event that securities are being offered to the public in Cyprus. That being said, in case that the company seeking funding only addresses foreign investors, it shall not have to comply with the above law.

###### (2) Other financial regulation

Assuming that the company seeking funding is not a Cyprus company and assuming further that its securities are not listed on a regulated market in Cyprus, no local financial services regulation will be applicable (including the Cyprus anti-money laundering regulation).

### **4.3.2 Cyprus Crowdfunding platform addresses foreign companies / projects**

To the extent that Cyprus investors are being approached, appropriate licenses shall need to be obtained if investment services or other regulated activities are purported to be provided.

#### **4.3.2.1 Crowdfunding platform**

##### **(1) License obligation**

In case the Cyprus Crowdfunding platform approaches Cyprus investors presenting foreign companies or projects, and provided that it provides the MiFID investment services or activities in relation to financial instruments, the MiFID Law will be applicable.

##### **(2) Other financial regulation**

Other financial regulation may be applicable depending on the activities conducted by the EU Crowdfunding platform seeking to provide services in Cyprus, e.g. the Payment Services Law, the E-Money Law, the Business of Credit Institutions Law etc. Depending on whether the above regulation is applicable, the platform will also be considered an obliged entity under the Cyprus Anti-Money Laundering legislation.

#### **4.3.2.2 Company / project**

##### **(1) Prospectus regulation**

In principle, a foreign company (which would be the company seeking funding through a Crowdfunding platform) purporting to offer transferable securities (within the meaning of MiFID) to the public in Cyprus would have to adhere to relevant provisions of the Cyprus Prospectus Law. Assuming such company already has a prospectus approved by the competent authority of its home member state, prospectus passport provisions would be applicable.

##### **(2) Other financial regulation**

Foreign companies or projects that issue securities might be subject to additional compliance obligations (e.g. listing and transparency requirements), in the event for instance that such securities are traded on a regulated market in Cyprus. In the event that such foreign companies or projects issue subordinated profit-participating loans, these will not in principle be regulated in Cyprus. Finally, foreign companies issuing securities or profit-participating loans will not constitute obliged persons within the meaning of the Anti-money laundering law.

## 4.4 Impact of EU regulation

### 4.4.1 Prospectus rule / regimes

As stated above, the Prospectus Law transposes into national law the Prospectus Directive. Furthermore, the Companies Law also requires Cyprus companies intending to invite persons to subscribe for shares in or debentures of in such company to issue a prospectus and lists certain requirements in respect of its content. Nevertheless, the Companies Law explicitly provides that Companies Law provisions shall not apply in relation to shares or debentures to which the Prospectus Law applies. As the Prospectus Law applies to transferable securities which are negotiable on the capital market, the provisions of the Companies Law will catch shares or debentures issued by a public Cyprus company that are non-negotiable on the capital market. Furthermore, the Prospectus Law has a broader scope applying to both Cyprus and foreign companies seeking to offer securities to the public in Cyprus, whereas the Companies Law only applies to Cyprus companies. Therefore, EU legislation is most influential in setting the prospectus regime in Cyprus.

### 4.4.2 AIFM-Directive

As stated above, the Cyprus AIFM Law, which transposes into national law the provisions of the AIFMD, could be of relevance to a Crowdfunding platform where the latter manages or markets a collective investment undertaking (other than in the form of Undertakings for Collective Investments in Transferable Securities- UCITS) which raises capital from a number of investors with the aim of investing it in accordance with a “defined investment policy”. In such case, the company or project seeking funding could form an AIF, which would have to be authorized by CySEC if established in Cyprus. However, if the company seeking funding constitutes an operating company, it is unlikely that the application of the AIFM Law would be triggered, however this made be determined by the respective competent authority.

In view of the above, and given that the interpretation of whether there exists a collective investment undertaking (and therefore an AIF) remains with the respective local authorities, it cannot be excluded that there may be a cross-border barrier, in the sense that a local supervisory authority may consider an investment vehicle to be an AIF, whereas one other will not deem it as such. Furthermore, given that there is no harmonized EU framework with regard to the marketing of AIF units to retail investors, additional and more burdensome regulation may be imposed on such an AIF depending on the jurisdiction where the AIF intends to market its units.

### 4.4.3 MiFID / MiFID II

Both MiFID I and MiFID II apply to transferable securities which are negotiable on the capital market. As it may be unlikely that Crowdfunding platforms will address companies issuing such securities, the application of MiFID may be very limited to the Cyprus Crowdfunding market. In fact and as stated further above, at the moment there are no Cyprus Crowdfunding platforms operating either through the equity or lending models.

Nevertheless, MiFID's passporting provisions may defeat to a certain extent regulatory barriers pertaining to the provision of services from one EU country to another.

#### 4.4.4 PSD / PSD II

The PS Law implementing the Payment Services Directive may be crucial to the operation of a Crowdfunding platform, whether under the lending, equity or donations or rewards models. The PSD II which aims to improve the existing rules is expected to be implemented by January 2018.

Although PSD is a full harmonization Directive intended to provide clear and harmonised rules across Europe, it has provided some leeway in the implementation of certain provisions. Additionally, the competent authorities appointed by Member States to supervise implementation of the PSD also have a degree of flexibility in the interpretation of certain provisions, including the money remittance services.

Nevertheless, it is understood that as far as the PS Law is concerned, any transfer of funds through the operator of a Crowdfunding platform would generally constitute money remittance services within the meaning of the PS Law. Such transfer of funds could occur if the investors pay their investment amounts to the Crowdfunding platform which then passes the funds to the company or project seeking funding.

In view of the above, the PSD and PSD II directives have a great impact for Crowdfunding with regard in particular to the conclusion of transactions.

#### 4.5 Summary

While a number of European countries have already implemented regulation specific to Crowdfunding, the lack of relevant market practice in Cyprus may be the main reason a similar legislative initiative has yet to be introduced in the country. In view of the above, guidance with regard to the regulation of Crowdfunding is sought in the applicable European financial services regulatory framework. Nevertheless, given the leeway member states possess in the transposition of EU directives, it is understood that certain regulatory barriers may arise in the cross-border activities of Crowdfunding platforms. From a Cyprus perspective, the following requirements arising from the applicable financial services regulation may impact the cross-border provision of services by Crowdfunding platforms:

- Wide scope of the MiFID Law, which applies, inter alia, to any provision or offer for the provision of investment services to investors who are resident or are domiciled in Cyprus;
- Inbound as well as outbound: passport is only available to MiFID licensed investment firms or other EU licensed service providers (e.g. Credit institutions, PSPs, E-money institutions). Therefore Crowdfunding platforms addressing companies issuing securities not falling within MiFID scope or subordinated profit-participating loans are excluded from the possibilities of the European passport regime and shall adhere to local requirements on each occasion;

## 5 Lessons learned from Cyprus regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model ("dos")

As Cyprus has not adopted Crowdfunding-specific legislation, it may not be considered as a role model for a possible harmonized European Crowdfunding regulation.

### 5.2 Aspects that should be avoided ("don'ts")

As above, Cyprus has not adopted Crowdfunding-specific legislation, which could be problematic to a possible harmonization of the European Crowdfunding regulation.

## 6 Conclusion

Although an increasing number of EU member states have taken the initiative to regulate the Crowdfunding business as a method of financing, Cyprus has yet to follow this example. In view of the lack of specific regulation, any barriers from a Cyprus law perspective to cross-border Crowdfunding stem from the lack of regulation which may cause some uncertainty as to the applicable requirements. That being said, we would suggest that the following measures shall need to be taken on a European legislative or administrative level in order to safeguard full harmonisation across the EU:

- regulation of all types of financial and other instruments that may be potentially used in Crowdfunding (especially non-negotiable transferable securities) and subordinated profit-participating loans;
- clarification that the MiFID II license (and by extension the EU Passport) shall extend to all financial instruments covered by national legislation in the host EU member state;
- harmonised definitions of the terms deriving from relevant European legislation (e. g. financial instruments).

## 7 Summary – Crowdfunding regulation

| Country   | Cyprus  |
|---|---|
| <b>Summary</b>  |   |
| <b>Recent developments in Crowdfunding regulation</b> | There have been no developments in Cyprus regarding Crowdfunding regulation, which remains largely under-developed.   |
| <b>Current / planned Crowdfunding regulation</b>      |   |
| <b>General regulation</b>                             | <p><b>Equity Model/Lending Model</b></p> <ul style="list-style-type: none"> <li>• If investment services are offered or investment activities are performed by the Crowdfunding platform as regards financial instruments (e.g. shares, units in collective investments etc) an investment license must be granted following the prior authorization of the Cyprus Securities and Exchange Commission (CySEC);</li> <li>• Financial instruments under MiFID include transferable securities (i.e. securities which are negotiable on the capital market), money-market instruments, units in collective investment undertakings, derivative instruments for the transfer of credit risk, as well as options, futures, swaps, forwards which may be settled physically or in cash, etc. Subordinated or profit-participation loans to companies are not, as a general rule, regarded per se as investment products.</li> <li>• MiFID Law does not include a specific Crowdfunding exemption from its scope, but it does provide several other exemptions.</li> <li>• Where applicable, the MiFID Law imposes a variety of capital, organizational and conduct of business requirements, purporting to ensure that client assets are protected, conflicts of interests are avoided, and that the platform acts in the interests of the clients or investors.</li> <li>• With regard to the lending model in particular, the Business of Credit Institutions Law 66/1997 may be of more relevance. <ul style="list-style-type: none"> <li>- Under the Business of Credit Institutions Law, it is prohibited for any person, other than a licensed credit institution, to engage in the business of taking deposits or other repayable funds from the public unless it has been previously authorized by CBC.</li> <li>- It would seem unlikely for a Crowdfunding platform, having adopted the lending model, to fall into the above definition that would trigger a banking licensing requirement by the CBC, if the platform does not hold money for own account and therefore does not perform the activity of holding deposits and simultaneously granting credit to others for own account.</li> </ul> </li> </ul> <p><b>Donations or Rewards Model</b></p> |

|                                      |   |
|--------------------------------------|---|
|                                      | <ul style="list-style-type: none"> <li>• No investment or banking licensing requirements would be applicable to this type of Crowdfunding.</li> </ul>   |
| <p><b>Prospectus requirement</b></p> | <ul style="list-style-type: none"> <li>• Equity/Lending Model</li> <li>• A requirement for the issuance of a prospectus applies for the offering of securities to the public. The scope, application and exemptions follows those of the relevant EU Prospectus Directive;</li> <li>• The prospectus cannot be published unless approved by the CySEC.</li> <li>• Prospectus Law applies only where instruments are transferable securities within the definition of the MiFID Law, transposing the MiFID Directive.</li> <li>• Prospectus Law shall not be apply, inter alia, to:             <ul style="list-style-type: none"> <li>• securities included in an offer where the total consideration of the offer in the European Union is less than EUR 5,000,000, calculated over a period of 12 months;</li> <li>• an offer of securities addressed solely to qualified investors (as defined in the MiFID Law);</li> <li>• an offer of securities addressed to fewer than 150 natural or legal persons per member state, which are not qualified investors;</li> <li>• an offer of securities with total consideration in the European Union of less than EUR 100,000, which value shall be calculated over a period of 12 months as to the securities offered during this period.</li> </ul> </li> <li>• Prospectus shall contain all information which according to the specific nature of the issuer and the securities being offered, is necessary in order to enable investors to evaluate comprehensively the assets, liabilities, financial position, profits and losses and prospects of the issuer and of any guarantor, and of the rights attaching to such securities.</li> <li>• Any type of advertisements relating to an offer to the public of securities or to an admission to trading on the Cyprus Stock Exchange (CSE) or on another regulated market, that takes place in Cyprus, shall, inter alia, state that a prospectus has been or shall be published and indicate the location where investors are able to obtain it, or how investors shall be able to have access to its full text.</li> <li>• Donations or Rewards Model</li> <li>• Prospectus requirements will not be applicable for this type of Crowdfunding.</li> </ul> |
| <p><b>AIFMD-regulation</b></p>       | <ul style="list-style-type: none"> <li>• In case a Crowdfunding platform constitutes an AIFM operating an AIF, such AIFM and/or the AIF must be licensed by CySEC under the AIFMD.</li> <li>• Operating companies are unlikely to be considered as falling under the scope of the relevant legislation.</li> <li>• an AIF is any collective investment undertaking (other than UCITS) including the investment compartments thereof, which, collectively:             <ul style="list-style-type: none"> <li>• raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and</li> </ul> </li> </ul>   |

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|   | <ul style="list-style-type: none"> <li>• does not require authorisation pursuant under the Open-ended Undertakings for Collective Investments Law of 2012, Law 78(I)/2012 or pursuant to the legislation of another Member State which harmonises the article 5 of the Directive 2009/65/EC (the “UCITS IV Directive”).</li> <li>• Where the AIF is internally managed the initial capital required is EUR 300,000.</li> <li>• Where the AIF is externally managed, the external manager would have to have an initial capital of EUR 125,000.</li> <li>• AIFs may be marketed to professional and retail investors, subject to the observance of further requirements.</li> </ul> <p>Project Company seeking funding:</p> <p>Equity Model</p> <ul style="list-style-type: none"> <li>• Project companies might qualify as AIFs if they seek funding from investors in return for a share in the profits or revenue generated by the project as in the Equity Model.</li> </ul> <p>Lending Model</p> <ul style="list-style-type: none"> <li>• Investments by means of subordinated loans, or other debt-based investments, may be structured as non-AIF investments for the reason that the investors do not share liability for any losses.</li> </ul> <p>Donations or Rewards Model</p> <ul style="list-style-type: none"> <li>• This type of Crowdfunding contains no collective investment undertaking such as an AIF.</li> </ul> <p>Crowdfunding platform:</p> <ul style="list-style-type: none"> <li>• If the platform does not raise capital from the public for its own business it will not qualify as an AIF.</li> <li>• If the platform does not manage the relevant company or project being the underlying investment, it will not qualify as an AIFM.</li> </ul> |
| <p><b>Payment service regulation</b></p>    | <ul style="list-style-type: none"> <li>• The transfer of funds through a Crowdfunding platform could constitute a money remittance service which would trigger the obligation for licensing by the Central Bank of Cyprus.</li> <li>• Thresholds of initial capital range from EUR 20,000 to EUR 125,000 depending on the services being offered.</li> <li>• PS Law excludes from scope, inter alia, payment transactions from the payer to the payee through a commercial agent authorised to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee.</li> </ul>   |
| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• The E-money Law, Law 81(I)/2012;</li> <li>• The Distance Marketing of Financial Services Law, Law 242(I)/2004;</li> <li>• The Consumer Credit Law, Law 106(I)/2010;</li> <li>• The Prevention and Suppression of Money Laundering Activities Law, Law 188(I)/2007;</li> <li>• The Processing of Personal Data (Protection of Individuals) Law 138(I) 2001;</li> </ul>   |
| <p><b>Regulatory barriers</b></p>           |  |

**Inbound**

**Foreign Crowdfunding platform addresses Cyprus investors**

- Crowdfunding platform

*The platform holds a MiFID license in another EU member state*

- The applicable regulatory framework will depend on whether the Crowdfunding platform holds, or not, a MiFID license (and therefore a passport) in any other EU member state.
- The MiFID Law will be applicable to an EU-based Crowdfunding platform addressing Cyprus resident or domiciled investors if it engages in investment-based Crowdfunding relating to financial instruments as defined in the said Law.
- EU passport will be applicable to a Crowdfunding platform holding a MiFID license.
- It is unclear whether a MiFID license held by a foreign Crowdfunding platform will suffice also for providing financial services relating to financial instruments or products not covered by the MiFID license – e. g. shares in a private company or subordinated profit-participating loans.

*The platform has no MiFID license*

- If the Crowdfunding platform intends to address investors resident or domiciled in Cyprus, local regulation will be applicable.
- Other financial regulation may be applicable depending on the activities conducted by the EU Crowdfunding platform seeking to provide services in Cyprus (e.g. the Payment Services Law, the E-Money Law, the Business of Credit Institutions Law etc.), with relevant passport provisions also being applicable.

- Foreign Company/project

- A foreign company (which would be the company seeking funding through a Crowdfunding platform) purporting to offer transferable securities (within the meaning of MiFID) to the public in Cyprus, would have to adhere to relevant provisions of the Cyprus Prospectus Law.
- Assuming the foreign company already has a prospectus approved by the competent authority of its home member state, prospectus passport provisions would be applicable.
- The Cyprus Securities and Stock Exchange Law, Law 14(I)/1993 may be applicable depending on whether the foreign company purports to admit its securities to trading on the CSE.
- The Anti-money laundering law will not be applicable.

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|------------------------|--|
|                        | <p><b>Foreign Crowdfunding platform addresses Cyprus companies</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform <ul style="list-style-type: none"> <li>- To the extent services are not being offered in Cyprus and Cyprus investors are not approached, Cyprus regulation will not apply and the Crowdfunding platform need not adhere to Cyprus licensing requirements.</li> <li>- In case the foreign Crowdfunding platform does not purport to offer any services in Cyprus, no additional Cyprus financial regulation shall be applicable.</li> </ul> </li> <li>• Cyprus Company/project <ul style="list-style-type: none"> <li>- To the extent that the Cyprus company seeking funding through a foreign Crowdfunding platform purports to issue securities to the public in Cyprus, the Cyprus Prospectus Law will be applicable. Therefore, if such securities are not purported to be issued in Cyprus, the Cyprus Prospectus Law will not be applicable.</li> <li>- Cyprus companies seeking funding through Crowdfunding platforms should comply with the Cyprus Companies Law, Cap. 113, which sets out several requirements in relation to the issue of shares and debentures of a Cyprus Company, including that only public companies (i.e. non-private companies with more than 7 members) can offer shares and/or debentures to the public.</li> <li>- Where the securities being issued by the Cyprus company are listed on the Cyprus Stock Exchange, additional listing requirements pursuant to the Cyprus Securities and Stock Exchange Law, Law 14(I)/1993, as well as the Market Abuse Regulation (Regulation (EU) No 596/2014) may be applicable.</li> <li>- It is highly unlikely that the securities of a Cyprus company seeking funding through a Crowdfunding platform will be admitted to trading on a regulated market.</li> <li>- The company will not constitute an obliged entity under the Cyprus Anti-money laundering legislation.</li> </ul> </li> </ul> |
| <p><b>Outbound</b></p> | <p><b>Cyprus Crowdfunding platform addresses foreign (EU) investors</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform <ul style="list-style-type: none"> <li>- Although Cyprus investors may not be approached, the fact that the provision of investment services comes from within Cyprus, could mean that the Cyprus Crowdfunding platform offering investment services within MiFID scope to investors abroad, would be subject to the MiFID Law requirements.</li> </ul> </li> </ul>   |

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|  | <ul style="list-style-type: none"> <li>- Insofar as the Cyprus Crowdfunding platform offers investment services under the MiFID Law, it would also be subject to the Cyprus Anti-money laundering legislation.</li> <li>- Requirements arising from the Cyprus Companies Law will also be applicable, since the Crowdfunding platform is a Cyprus company.</li> </ul> <ul style="list-style-type: none"> <li>• Company/project <ul style="list-style-type: none"> <li>- The Prospectus Law will be applicable in the event that securities are being offered to the public in Cyprus.</li> </ul> </li> </ul> <p><b>Cyprus Crowdfunding platform addresses foreign companies/projects</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform <ul style="list-style-type: none"> <li>- In case the Cyprus Crowdfunding platform approaches Cyprus investors presenting foreign companies or projects, and provided that it provides the MiFID investment services or activities in relation to financial instruments, the MiFID Law will be applicable.</li> <li>- Other financial regulation may be applicable depending on the activities conducted by the EU Crowdfunding platform seeking to provide services in Cyprus, e.g. the Payment Services Law, the E-Money Law, the Business of Credit Institutions Law etc. Depending on whether the above regulation is applicable, the platform will also be considered an obliged entity under the Cyprus Anti-Money Laundering legislation.</li> </ul> </li> <li>• Company/project <ul style="list-style-type: none"> <li>- In principle, a foreign company (which would be the company seeking funding through a Crowdfunding platform) purporting to offer transferable securities (within the meaning of MiFID) to the public in Cyprus, would have to adhere to relevant provisions of the Cyprus Prospectus Law.</li> <li>- Assuming such company already has a prospectus approved by the competent authority of its home member state, prospectus passport provisions would be applicable.</li> </ul> </li> <li>• Foreign companies or projects that issue securities might be subject to additional compliance obligations (e.g. listing and transparency requirements), in the event for instance that such securities are traded on a regulated market in Cyprus.</li> <li>• In the event that foreign companies or projects issue subordinated profit-participating loans, these will not in principle be regulated in Cyprus.</li> </ul> |
|--|--|

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>Foreign companies issuing securities or profit-participating loans will not constitute obliged persons within the meaning of the Anti-money laundering law.</li> </ul>  |
| <b>Impact of EU Regulation</b> |  |
| <b>Prospectus regulation</b>   | <ul style="list-style-type: none"> <li>Prospectus Law transposes into national law the respective Prospectus Directive.</li> <li>Companies Law also requires Cyprus companies intending to invite persons to subscribe for shares in or debentures of in such company, to issue a prospectus and lists certain requirements in respect of its content. Nevertheless, the Companies Law explicitly provides that Companies Law provisions shall not apply in relation to shares or debentures, to which the Prospectus Law applies.</li> </ul>  |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>Cyprus AIFM Law, transposes into national law the provisions of the AIFMD, could be of relevance to a Crowdfunding platform where the latter manages or markets a collective investment undertaking (other than in the form of Undertakings for Collective Investments in Transferable Securities- UCITS) which raises capital from a number of investors with the aim of investing it in accordance with a “defined investment policy”.</li> <li>The interpretation of collective investment undertakings (and therefore an AIF) remains with the respective local authorities and therefore it cannot be excluded that there may be a cross-border barrier, in the sense that a local supervisory authority may consider an investment vehicle to be an AIF, whereas one other will not deem it as such.</li> <li>No harmonized EU framework with regard to the marketing of AIF units to retail investors, additional and more burdensome regulation may be imposed on such an AIF depending on the jurisdiction where the AIF intends to market its units.</li> </ul> |
| <b>MiFID / MiFID II</b>        | Both MiFID I and MiFID II apply to transferable securities which are negotiable on the capital market. As it may be unlikely that Crowdfunding platforms will address companies issuing such securities, the application of MiFID may be very limited to the Cyprus Crowdfunding market.   |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>The PS Law implementing the Payment Services Directive may be crucial to the operation of a Crowdfunding platform, whether under the lending, equity or donations or rewards models.</li> <li>The PSD II is expected to be implemented by January 2018.</li> <li>It is understood that as far as PS Law is concerned, any transfer of funds through the operator of a Crowdfunding platform would generally constitute money remittance services within the meaning of the PS Law.</li> </ul>   |

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# Czech Republic

## 1 Recent developments in the market of Crowdfunding in the Czech Republic

During the last years there were the following significant developments in the Czech Republic regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company / project)

Although Crowdfunding is more and more popular in the Czech Republic, there has not been any equity platform until recently. Currently we are aware of two equity platforms offering mostly investments in start-ups and one of these platforms is also offering investments in the form of mini-bonds. This change may be partly attributable to new legislation governing corporations (Act no. 90/2012 Coll., the Corporations Act, which took effect on 1 January 2014). The Corporations Act enables more flexibility in setting up the corporate governance structure of target companies, thereby making equity Crowdfunding projects more viable in the long term. Both existing equity platforms are domestic.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

Perhaps most significant change in respect of the Lending Model is that financial institutions are becoming involved in these platforms. Despite this change peer-to-peer lending is the only currently operative model in practice. Business loans continue to be outnumbered by loans to private individuals. And also as mentioned above one Crowdfunding platform is offering investments in the form of mini-bonds.

Currently there are around 5 platforms based on the Lending Model and all of the platforms are domestic.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

Crowdfunding platforms based on the Rewards Model continue to be the most successful and popular in the Czech Republic. As in the past, social and cultural projects still form a majority of funded ventures, along with a smaller number of start-up companies.

The majority of Crowdfunding platforms in the Czech Republic are based on Rewards Model and the platforms are domestic. Currently there are around 10 rewards platforms in the Czech Republic.

## 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

The real estate projects and the projects dealing with the renewable energy sources are generally popular and attractive in the market, but so far no Crowdfunding platform focused on the real estate or renewable energy sources projects has been established in the Czech Republic and there have been no notable Crowdfunding projects in these areas.

## 1.5 International approach

We understand that some foreign Crowdfunding platforms (mostly US and Canadian) try to reach the local markets in Europe and plan to establish international platforms. We have not seen such trend in the Czech Republic yet.

## 2 Recent developments regarding Crowdfunding regulation in the Czech Republic

In the past year the main regulations relevant to Crowdfunding remained largely stable and unchanged. We understand from unofficial contact with public bodies that the current extent of Crowdfunding regulation is viewed as sufficient and that, therefore, no specific regulatory changes directly affecting Crowdfunding are expected in the near future.

## 3 Current Regulation of Crowdfunding in the Czech Republic

### 3.1 Licence under Act no. 240/2013 Coll., on management companies and investment funds, as amended (the “AMCIF”)

#### 3.1.1 Equity Model

Investing in return for a share in the profits or revenue generated by a company/project is defined by the AMCIF as a form of collective investment.

Such activity corresponds most closely to the definition of an investment fund under the AMCIF. An investment fund is either a joint-stock company with its registered office in the Czech Republic or a mutual fund (which is merely a collection of funds and has no legal personality) that is entitled or the purpose of which is (i) to collect funds from the public by issuing shares/participation certificates and (ii) to perform the collective investment of the collected funds on the basis of a given investment strategy based on the principle of the division of risk for the benefit of the owners of the shares/participation certificates and further (iii) to manage the funds (“Investment Fund”).

An Investment Fund can either (i) be managed by a management company, (ii) exist in the form of an Investment Fund which is entitled to manage itself or (iii) exist in the form of an Investment Fund which is managed by its executive body being a management company. All three possibilities (a management company, a self-managing Investment Fund and an Investment Fund managed by its executive body) are required to obtain a licence from the Czech regulator (i.e. the Czech National Bank).

The capital of an Investment Fund has to reach at least EUR 1,250,000 within six months of the date of the establishment of such Investment Fund.

If a project company or a Crowdfunding platform acting under the Equity Model would intend to provide investment services, it would have to be properly licenced under Act no. 256/2004 Coll., on capital markets, as amended (the “Capital Markets Act”).

Investment services (“Investment Services”) under the Capital Markets Act include in particular:

- A. reception and transmission of orders in relation to investment instruments (i.e. in particular investment securities such as shares or bonds and derivatives – “Investment Instruments”);
- B. execution of orders in relation to Investment Instruments on behalf of a client;
- C. proprietary trading in Investment Instruments;
- D. management of client's assets under a contract with the client if an Investment Instrument is part of such assets;
- E. investment advice concerning Investment Instruments;
- F. underwriting and/or placing of Investment Instruments on a firm commitment basis;
- G. placing of Investment Instruments without a firm commitment basis; and
- H. services of safekeeping and administration of Investment Instruments for the account of clients (including custodianship and related services).

Alternatively, a Crowdfunding platform may position itself as an intermediary for a direct sale of shares in the individual companies to its investors, thereby avoiding the application of collective investment rules. Under this model, the platform would still have to be licenced with the Czech National Bank as an investment firm, in particular providing the Investment Services listed above under letter b), c), f) and h).

However, the application of this method provides for significant administrative constraints, in particular regarding the corporate structure of the target companies (e.g. the economies of the relevant administrative costs effectively rule out target companies structured as limited liability companies). Furthermore, prospectus requirements (as described in section 3.2) must also be respected.

### 3.1.2 Lending Model

Under Czech law, the lending of money by individuals to a company/project in return for repayment of the loan and interest is a non-regulated activity. Despite the fact that the lending of money would occur through an online Crowdfunding platform, there are no regulatory requirements under Act no. 21/1992 Coll, on banking, as amended (the “Banking Act”). However, general civil and commercial rules on lending must be observed.

Most importantly, the Crowdfunding platform is obliged to obtain a trade licence in order to be entitled to organise lending and borrowing.

The provision of money to individuals as consumers is now regulated under the new Act no. 257/2016 Coll., on consumer credit (the “Consumer Credit Act”), which entered into effect on 1 December 2016. Under the Consumer Credit Act, not only consumer loans providers, but also consumer loans intermediaries are required to obtain a licence from the Czech National Bank. The non-banking consumer loans providers and intermediaries now also fall under the supervision of the Czech National Bank.

Should the Crowdfunding platform act as a non-banking consumer credit provider, it must satisfy certain statutory requirements, such as minimum registered capital, establishment of supervisory body, implementation of anti-money laundering rules, etc. The licence for non-banking consumer loans providers is granted for 5 years with possible extension of 60 months.

Crowdfunding platforms may, however, provide consumer loans in the regime of intermediaries acting on behalf of third parties. In that case, the statutory requirements are not as strict, the main requirements being the expertise and credibility. The licence for consumer loans intermediaries is granted for one year and can be extended by 12 months.

### 3.1.3 Donations or Rewards Model

The provision of money by individuals to a company/project for benevolent reasons or for non-monetary reward constitutes an exemption under the AMCIF. Collecting funds or assets that can be valued in money the main purpose of which is the financing of activities that relate to the production or sale of goods, research or the provision of services (other than financial services) and further management of such collected funds or assets that can be valued in money (or assets gained for such funds or assets that can be valued in money) does not constitute collective investment. Such activity is thus not regulated by the AMCIF. However, a Crowdfunding platform which would organise such collection of funds would have to obtain a trade licence for these purposes.

Furthermore, the requirements of Act No. 117/2001 Coll., on public collections, as amended (the “APC”) apply to the Donations Model. The APC applies to any activity by which voluntary donations are being collected from further unspecified members of the public (the “Public Collection”) and imposes several restrictions. In particular, Public Collections may only be held for publicly beneficial purposes, such as humanitarian purposes, charity, education, sport, and protection of cultural items, cultural heritage or the environment. Any Public Collection has to be notified to the relevant Regional Authority (in Czech: “krajský úřad”). The Regional Authority subsequently scrutinizes the application and may reject it for non-compliance with the statutory requirements, in particular if it finds that the purpose of the Public Collection is not publicly beneficial. Furthermore, detailed records of the contributions must be kept and must be submitted to the Regional Authority after the Public Collection has finished.

Due to the aforementioned administrative requirements and the fact that Crowdfunding of certain types of projects (e.g. business start-ups) would rarely satisfy the conditions of public benefit, current Crowdfunding platforms refrain from the use of the Donations model. Instead,

the Rewards model is used where each project typically has to define rewards for contributors and the contribution is structured as a sale of such reward, thus falling out of the scope of the APC.

### 3.2 Prospectus requirements

Under the Capital Markets Act, the general prospectus requirement does not apply where the offering of investment securities (i.e. shares, bonds, securities substituting shares or bonds, securities enabling the acquisition or sale of shares or bonds, certain derivatives, or similar securities) in all member state of the European Union does not exceed EUR 1,000,000 within a time period of 12 months.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

In the Czech Republic, the AIFMD has been implemented by the AMCIF. Under the AMCIF, an alternative investment fund (an “AIF”) constitutes either a special fund or a fund of qualified investors.

A special fund under the AMCIF is defined as an Investment Fund which does not fulfil the requirements stipulated by the law of the European Union and thus is not registered in the relevant register kept by the Czech National Bank.

The AMCIF defines a fund of qualified investors as:

- A. a legal entity (limited partnership, limited liability company, joint stock company, *societas europea* or cooperative) with its registered office in the Czech Republic that is entitled to (i) collect funds or assets that can be valued in money from several qualified investors by issuing participation securities or in a way that such qualified investors be-come its shareholders, and (ii) perform collective investment of the collected funds or assets that can be valued in money on the basis of a given investment strategy for the benefit of such qualified investors, and (iii) to manage such assets; or
- B. a mutual fund the purpose of which is to (i) collect funds or assets that can be valued in money from several qualified investors by issuing participation certificates and (ii) invest the collected funds on the basis of a given investment strategy for the benefit of the owners of the participation certificates and (iii) manage these assets; or
- C. a trust fund (i) the statutes of which identifies several qualified investors as beneficiaries; such beneficiaries are the founder of the given trust fund or the person that in-creased the assets of the given trust fund on the basis of a contract and (ii) which is established for the purpose of investment on the basis of a given strategy for the benefit of its beneficiaries

### 3.3.1 Operating company seeking funding

Assuming that “operating company” means a start-up or developing company seeking funding for its general commercial business by means of a Crowdfunding platform, the operating company falls under an exemption under the AMCIF. Collecting funds or assets that can be valued in money the main purpose of which is the financing of activities that relate to the production or sale of goods, research or the provision of services (other than financial services) and the further management of such collected funds or assets that can be valued in money (or assets gained for such funds or assets that can be valued in money) does not constitute collective investment. Such activity is not regulated by the AMCIF; therefore, an operating company can neither fall under the definition of a special fund nor of a fund of qualified investors under the AMCIF.

Of course, the operating company would have to obtain a relevant trade licence in order to be able to conduct its business.

### 3.3.2 Project Company seeking funding

As long as a project company is acting under the Equity Model (i.e. it invests in return for a share in the profits or revenue generated by such project company), then the provisions in the AMCIF apply to it. An investor in a project company acting under the Equity Model would probably not qualify as a qualified investor (as defined by the AMCIF), so a project company acting under the Equity Model would probably not constitute a fund of qualified investors under the AMCIF. The capital of a special fund has to reach at least EUR 1,250,000 within six months of the date of the establishment of such special fund.

Also, if a project company acting under the Equity Model would intend to provide Investment Services (as defined above), it would have to be properly licenced under the Capital Markets Act.

The AMCIF will not apply to project companies seeking funding via the Lending or Reward Models.

### 3.3.3 Crowdfunding Platform

Should the Crowdfunding platform organise funding for project companies under the Equity Model, it would not constitute a fund of qualified investors under the AMCIF (as an investor of a project company acting under the Equity Model would not qualify as a qualified investor, as defined by the AMCIF). It cannot be ruled out; however, that such Crowdfunding platform could constitute a special fund under the AMCIF (i.e. an AIF under the AMCIF).

The capital of a special fund has to reach at least EUR 1,250,000 within six months of the date of the establishment of such special fund.

Also, should the Crowdfunding platform intend to provide Investment Services (as defined above) when organising funding for project companies under the Equity Model would, it would have to be properly licenced under the Capital Markets Act.

Should the Crowdfunding platform organise funding for project companies under the Lending Model, it would neither constitute a special fund nor a fund of qualified investors, as the AMCIF would not apply due to the fact that organising the lending of money by individuals to a company/project in return for the repayment of the loan plus the payment of interest is a non-regulated activity.

Should the Crowdfunding platform organise funding for project companies under the Donations or Rewards Model, it would neither constitute a special fund nor a fund of qualified investors, as the AMCIF would not apply due to the fact that organising the provision of money by individuals to a company/project for benevolent reasons or for non-monetary reward constitutes an exemption under the AMCIF.

### 3.4 Regulation under the Payment Services Directive

Should the Crowdfunding platform intend to perform payment services itself in the Czech Republic, it would have to be properly licenced. There is the possibility to become either (i) a payment institution, (ii) a small-scale payment service provider, (iii) an electronic money institution or (iv) a small-scale electronic money issuer under the Act no. 284/2009 Coll., on payment services, as amended (the “Payment Services Act”). Becoming a payment institution or an electronic money institution requires a licence granted by the Czech National Bank. Becoming a small-scale payment service provider or a small-scale electronic money issuer requires registration with the Czech National Bank.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Act 455/1991 Coll., on trading, as amended (which regulates trade licences) (the “Trade Licencing Act”);
- the Capital Markets Act; and
- Act 253/2008 Coll., on some measures against the legalisation of proceeds gained from criminal conduct and financing of terrorism (AML provisions) (the “AML Act”).

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable Law

The most important criterion to determine whether or not Czech financial regulation shall apply in the cross-border provision of services is the place where the provision of services occurred. In case of distance provision of financial services, it is deemed that the service is provided in the Czech Republic if the Czech market is targeted, e.g. by addressing potential investors by direct e-mails, calls or by advertisement in national newspapers.

To assess when the financial services provided via the Internet fall under Czech regulation, it must be considered whether the website focuses on Czech investors, the website

and the entire communication is in Czech and whether the financial services are actually being offered to Czech clients.

## 4.2 Inbound

### 4.2.1 Foreign Crowdfunding platforms addresses Czech investors

Czech regulatory law can apply to the

- Crowdfunding platform and/or
- Company/project seeking funding.

#### 4.2.1.1 Crowdfunding platform

The applicable regulatory law depends on whether the platform has a licence granted in an EU country or not. In addition it always depends on the model of Crowdfunding that is offered by the platform.

##### (1) Equity Model

In the case the platform is licenced as an Investment Fund, its licence can be passported into the Czech Republic and the platform can offer the projects to investors in the Czech Republic once the passporting is completed. Similar rules are applicable to AIFs.

In the case the platform holds a MiFID licence for an investment firm such licence can be passported into Czech Republic and after that the platform can offer its projects also to investors in the Czech Republic.

In the case the platform does not hold a passportable licence, the platform can offer the projects to investors in the Czech Republic only in the case it obtains the respective licence in the Czech Republic (or other EU country and passports such licence to the Czech Republic).

##### (2) Lending Model

As mentioned above there is no specific Crowdfunding regulation applicable to the platform operating the Lending Model, the platform in fact acts as an intermediary of a loan and such activity is subject to a trade licence. No further regulatory licence is necessary for the platform, subject to the below.

In the case the loans would be provided to consumers, the platform would act as an intermediary of a consumer loan and in that case it would require a registration as an intermediary with the Czech National Bank.

##### (3) Donations or Rewards Model

There are no specific regulations for foreign platforms, and same rules as for domestic platforms would be applicable.

##### (4) Other financial regulation applicable to all models

Should payment services be connected with Crowdfunding the platform is also required to be licenced as payment institution or electronic money institution, depending on the exact scope of the services provided. In the case it holds the appropriate licence in its home EU country under the PSD (or PSD II) such licence can be passported into the Czech Republic.

#### **4.2.1.2 Project company**

In the case a foreign project/company would be offered in the Equity Model Crowdfunding platform a prospectus rules must be adhered to. As mentioned above there are no specific prospectus rules for offering shares through Crowdfunding platform, so the general prospectus rules (and exemptions) under the Prospectus Directive will apply.

### **4.3 Outbound**

#### **4.3.1 Crowdfunding Platform**

In this case the Czech platform addresses investors outside the Czech Republic. As mentioned above the Czech rules and regulations apply if the services or products are offered in the Czech Republic or if the investors in the Czech Republic and approached or targeted. So in this scenario the Czech rules will not apply since only the investors outside the Czech Republic are targeted.

#### **4.3.2 Project company**

The prospectus requirement under Czech law is applicable only in the case a public offer is addressed to the investors in the Czech Republic. In the case of a public offer of financial products offered outside of the Czech Republic Czech law will not apply.

### **4.4 Impact of EU regulation**

#### **4.4.1 Prospectus rules**

The prospectus requirements in the Czech Republic are governed by the Capital Markets Act implementing the Prospectus Directive. The scope of the securities to which the prospect requirements apply to in case of their public offer as well as relevant exemptions are explained above. The European legislation as implemented into Czech law poses very significant regulatory barrier to the project companies that are part of the Equity Model. The project companies mostly rely on the exemption under the Prospectus Directive since the volume of offered securities is usually below the threshold set by the Prospectus Directive and a prospectus does not have to be produced.

#### **4.4.2 AIFM-Directive**

The AIFM-Directive and the implementing the Czech AMCIF mainly affect equity-based or potentially lending-based Crowdfunding platforms (debt securities). Since there are no Crowdfunding specific exemptions or guidelines issued by the regulator, it remains uncertain whether the Crowdfunding would fall into the scope of AIFM-Directive and the Czech AMCIF.

### 4.4.3 MiFID II

The impact of MiFID II on the Czech Crowdfunding platforms is very similar with the impact of the prospectus rules described in point 4.3.1 above as both MiFID and MiFID II will have been implemented into the same legislation as the Prospectus Directive, i.e. the Capital Markets Act. The main scope of application of MiFID/MiFID II is the possibility to rely on the EU Passport regime both inbound and outbound.

The platform based on the Equity Model might trigger the licencing requirements under MiFID/MiFID II in the case investment services are provided by the platform as explained above.

### 4.4.4 PSD II

The Payment Services Directive has been implemented into the Czech Payment Services Act and it is expected that PSD II will be implemented into a new act that would replace the existing Payment Services Act. The existing Payment Services Act also implements the E-Money Directive. With respect to PSD I / PSD II the money remittance services and necessary licence requirements might be triggered by the Crowdfunding platform if the investor funds are transferred through it. Alternatively, the Crowdfunding platform may decide to co-operate with a li-censed payment services operator. In any case the Crowdfunding platform needs to consider this complex regulation before it commences to operate.

## 4.5 Summary

Current regulatory environment is quite complex for a Crowdfunding platform – which by its nature – should not face the same level of regulation as the established financial institutions, investment firms or investment firms. By its nature – the Crowdfunding should be an easier alternative to the established means of raising money and should be recognised on the EU level in accordance with the aim to establish a European single market. Cross-border flow of the capital facilitated by the less-regulated Crowdfunding within the Union is an important socio-economic factor of the EU integration process.

From a Czech perspective, the Crowdfunding platforms face mainly the following regulatory barriers:

- No relevant exemption from licence requirements or a simplified licence under the Capital Markets Act, and
- No relevant exemption from licence requirements under the AMCIF.

Apart from regulatory barriers, there is almost no official standpoint of the main regulator concerned – the CNB – on position of Crowdfunding platforms (especially based on Equity Model).

## 5 Lessons learned from the Czech Republic's regulation for a possible harmonized European Crowdfunding regulation

To a large extent, the regulatory regime of Crowdfunding is already heavily influenced by harmonized European legal provisions, as they are based on the AIFMD, the Payment Services Directive (PSD) and PSD II, MiFID, MiFID II and others.

### 5.1 Role model ("dos")

With regard to the Lending Model and the Rewards Model, it may be viewed positively that little to no regulatory limitations apply.

### 5.2 Aspects that should be avoided ("don'ts")

No specific Czech regulations currently exist for Crowdfunding; rather the existing regulations were adapted and applied to this emerging phenomenon. As a result, the level of investor protection required by the regulation may limit the viability of smaller investments.

The administrative requirements applied to the Equity Model often require written form with no possibility to complete such steps electronically, which would be most suited to the nature of Crowdfunding. The related costs may render investments in smaller amounts uneconomical.

Regulatory limitations to the Donation Model, such as a requirement to register Public Collections and maintain detailed records of the provided donations, effectively exclude the viability of this model.

## 6 Conclusion

During the past years there has been growing interest in Crowdfunding in the Czech Republic, although this is not necessarily reflected in the amount of existing platforms. Currently, the Rewards Model remains the most popular and successful with the Equity Model attracting start-ups and new investors.

## 7 Summary – Crowdfunding regulation

| Country   | Czech Republic   |
|---|--|
| Summary   |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Under the new Consumer Credit Act, consumer loans providers and intermediaries must obtain a licence from the Czech National Bank</li> <li>• New Corporations Act enables more flexible structure of target companies using Equity Model</li> <li>• No new regulation is expected in the near future</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Project company or Crowdfunding platform acting under Equity Model can be qualified as an Investment Fund under AMCIF → licence from Czech National Bank required</li> <li>• Alternatively, Crowdfunding platform may to a limited extent act as intermediary in direct purchase of shares by investors → licence from the Czech National Bank required</li> <li>• Project company or Crowdfunding platform acting under Lending Model is not a regulated entity → no licence required</li> <li>• Project company or Crowdfunding platform acting under Donations or Rewards Model enjoys an exemption under AMCIF and cannot be qualified as an Investment Fund → no licence required</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• General prospectus requirement for offering of investment securities</li> <li>• Exemptions apply under threshold of EUR 1,000,000 per issuer for investment securities offered in any Member State of EU within 12 months</li> </ul>  |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Operating company like start-up or developing company will not be qualified as AIF under AMCIF → no licence required</li> <li>• A project company/Crowdfunding platform acting under Equity Model could possibly be qualified as AIF under AMCIF → licence from Czech National Bank required</li> <li>• Project company/Crowdfunding platform acting under Lending or Rewards Model will not be qualified as AIF → no licence required</li> </ul>   |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Provision of payment services as defined under Payment Services Act by a project company or a Crowdfunding platform triggers licencing requirements (licence granted by Czech National Bank)</li> </ul>   |
| <b>Consumer credit regulation</b>                     | <ul style="list-style-type: none"> <li>• The Consumer Credit Act only applies to individuals who are consumers. The Consumer Credit Act does not apply to business relationships.</li> </ul>   |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Trade Licencing Act</li> <li>• Capital Markets Act</li> <li>• AML Act</li> </ul>  |
| <b>Regulatory barriers</b>                            |  |
| <b>Inbound</b>  | <ul style="list-style-type: none"> <li>• In case of distant provision of financial services, it is deemed that the service is provided in the Czech Republic if the Czech market is</li> </ul>   |

|                                |  |
|--------------------------------|--|
|                                | <p>targeted, e.g. by addressing potential investors by direct e-mails, calls or by advertisement in national newspapers</p> <ul style="list-style-type: none"> <li>• The financial services provided via the Internet fall under Czech regulation if the website focuses on Czech investors, the website and the entire communication is in Czech and if the financial services are actually being offered to Czech clients</li> <li>• As a general rule a foreign platform that has MiFID/MiFID II or Investment Fund licence can offer its products/services in the Czech Republic on the basis of such licence provided that it has been passported into the Czech Republic</li> <li>• In the case a foreign platform does not hold a passportable licence it needs to obtain the respective regulatory licence in the Czech Republic</li> <li>• The project/company must adhere to the prospectus rules (exemptions) under the Prospectus Directive</li> </ul> |
| <b>Outbound</b>                | <ul style="list-style-type: none"> <li>• In the case solely the investors outside the Czech Republic are targeted either by the Crowdfunding platform or the project/company, Czech law does not apply</li> </ul>  |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | <ul style="list-style-type: none"> <li>• Equity Model in the Czech Republic is made subject to prospectus exemptions under the Prospectus Directive and mostly the exemption in respect of the total volume of shares offered is use</li> </ul>  |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• AIFM Directive and its implementation in the Czech Republic has no impact on Crowdfunding in the Czech Republic</li> </ul>  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• MiFID /MiFID II has a significant impact on the platforms offering the Equity Model – the platform must have an investment firm licence or alternatively, depending on the exact scope of services it must have a local law licence of investment intermediary. The local investment intermediary licence is not passportable</li> </ul>  |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• Any transfer of funds through the operator of a Crowdfunding platform constitutes money remittance service within the meaning of the Payment Services Act, the Czech implementation of PSD/PSD II in Czech law. PSD/PSD II has significant impact regarding the transaction of investments</li> </ul>   |

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# Denmark

## 1 Recent developments in the market of Crowdfunding in Denmark

During the last couple of years the Crowdfunding market in Denmark has become more and more popular and has in some areas experienced a rapid growth. On 25 March 2017 the Danish Growth Fund (in Danish: Vækstfonden) and Danish Crowdfunding Association (in Danish: Dansk Crowdfunding Forening) published a report of the Danish Crowdfunding market in 2016. The report shows that in both 2015 and 2016 Crowdfunding is estimated to have increased with a rate of 250 per cent compared to the year before. Therefore, the Crowdfunding market in Denmark follows the global development.

Below you will find a more detailed description of the recent developments in the different Crowdfunding models: (i) the Equity Model, (ii) the Lending Model and (iii) the Donations or Rewards Model.

### 1.1 Equity Model

The equity-based model continues to be the most complex model from a regulatory perspective (please refer to a more detailed description hereof below in paragraph 3.1). This probably also explains why, despite experiencing the same overall growth as the global market, equity-based Crowdfunding has had no ground in Denmark until just recently. In 2016, Crowdinvest, which is an equity-based Crowdfunding platform, was launched and is the first Danish equity-based Crowdfunding platform.

### 1.2 The Lending Model

Lending-based Crowdfunding is the most common Crowdfunding model in Denmark. It is estimated to represent 52 per cent of total capital raised by Crowdfunding in Denmark. In 2016, the amount of capital raised by lending-based Crowdfunding grew more than twice compared to the year before.

Currently, there are six platforms for lending-based Crowdfunding in Denmark. The lending model distinguishes between (i) platforms where a company is in need of capital and (ii) platforms where private persons lend capital. Five of the lending-based platforms in Denmark only provide capital for companies. It is mainly SMEs operating within the trade and services industry which use the Crowdfunding platforms.

The newest addition to lending-based Crowdfunding platforms is Coop Crowdfunding, which was launched as a pilot project in April 2017 in collaboration with the already established platform Lendino. Coop is a Danish supermarket chain with 1.7 million members. Coop Crowdfunding will create a link between its members and local food manufactures and businesses.

### 1.3 The Donations or Rewards Model

Reward Crowdfunding is much more prevalent in Denmark compared to the global trend. Reward-based Crowdfunding is estimated to make up for 43 per cent of the total Crowdfunding market in Denmark in 2016 compared to 8 per cent on a global plan.

Currently, there is only one Danish reward-based Crowdfunding platform. However, a number of Danish projects can be found on well-known foreign platforms such as Kick-starter and Indiegogo.

Donation-based Crowdfunding is estimated to take up 5 per cent of the total Crowdfunding market in Denmark in 2016. There are two Danish platforms for donation-based Crowdfunding.

### 1.4 Real Estate Crowdfunding

Real Estate Crowdfunding has started to gain ground in Denmark. Recently, a Crowdfunding platform called BrickShare has been launched. The platform enables investors to invest in real estate property. The investor receives its share of the periodic rent income and the profit (if any) by the sale of the property.

### 1.5 Renewable Energy Crowdfunding

According to information available on the websites of the various Danish Crowdfunding platforms only very few and minor renewable energy projects have been financed via Crowdfunding platforms in Denmark.

### 1.6 International approach

Some international Crowdfunding platforms, especially within Reward Crowdfunding have entered the Danish market. However, for the time being, we are yet to see the breakthrough of international Crowdfunding platforms in Denmark.

## 2 Recent development regarding Crowdfunding regulation in Denmark

In May 2015 the Danish Ministry of Industry, Business and Financial Affairs concluded in its report on Crowdfunding in Denmark, that no amendments to existing regulation were necessary to advance the application of Crowdfunding in Denmark. As a consequence hereof, there have been no particular developments regarding the Crowdfunding regulation in Denmark.

However, the Danish Ministry for Industry, Business and Financial Affairs recently announced that the Danish government intends to make it easier for fintech companies to be established in Denmark. The aim is to create a fintech lab within the Danish FSA, which will make it easier for digital start-ups to navigate within the financial regulation. Accordingly, Crowdfunding platforms, which carry out activities within the fintech industry, would therefore also be able to benefit from this fintech lab.

### 3 Current Regulation of Crowdfunding

#### 3.1 Licence requirements under Danish financial regulation

##### 3.1.1 Equity Model

Rendering of investment services in Denmark commercially are regulated activities under Danish law and such activities are subject to a licensing requirement from the Danish FSA according to the Danish Financial Business Act (Consolidated Act No. 174 of 31 January 2017).

For the purpose of Danish law “investment services” are interpreted and based on MiFID and include, inter alia, receipt and arrangement for the account of investors of orders in relation to one or more financial instruments and, execution of orders with one or more financial instruments. Financial instruments within the scope of the Danish Financial Business Act include securities and financial instruments. Securities include shares in companies and other securities equivalent to shares in companies, partnerships and other businesses, and share certificates, bonds and other debt instruments, including certificates for such securities, and any other securities of which securities as mentioned above can be acquired or sold, or give rise to a cash settlement, the amount of which is fixed with securities, currencies, interest rates or returns, commodities indexes and other indexes and targets as reference.

MiFID II, which is to be implemented in Danish law before 3 July 2017 by way of amendments to the Danish Financial Business Act and by a new Act on Capital Markets (in Danish: lov om kapitalmarkeder), will from a Crowdfunding platform point of view not change the scope of applicability in relation to investment services and financial instruments.

If a Crowdfunding platform facilitates the offering of securities or financial instruments, the operator of the platform renders investment services and is therefore subject to the licensing requirement under the Danish Financial Business Act if the Crowdfunding platform facilitates that investors meet public limited companies that are seeking funding with a view to facilitating a transaction in respect of the shares in the limited companies. The Danish FSA has in November 2013 issued guidance on the licensing requirements and the exemptions thereunder.

##### 3.1.2 Lending Model

Any activity in Denmark comprising receiving from the public of deposits or other funds to be repaid requires a license in accordance with the Danish Financial Business Act. If the Crowdfunding model is based on the concept that the Crowdfunding platform provider will repay the deposits provided by the investors this will require a license under Danish law.

##### 3.1.3 Donations or Rewards Model

Each of the Donations and Rewards Model is structured in order not to constitute any form of financial investment or financial return and therefore is not within the scope of the Danish

financial regulation. Accordingly, the provider of a Crowdfunding platform operating this model is not subject to any financial regulation or license requirements.

## **3.2 Prospectus requirements**

### **3.2.1 Equity Model**

The public offering and sale of securities or investment products to investors is subject to a prospectus requirement pursuant to the Danish Securities Trading Act (Consolidated Act no. 251 of 21 March 2017) which for prospectuses above EUR 5,000,000 implements the Prospectus Directive. Currently, Danish law has a special set of national rules in respect of prospectuses for offerings with a value between EUR 1,000,000 and 5,000,000. The Danish Securities Trading Act is expected to be replaced by a new act which has been introduced as “Act on Capital Markets”. In the bill for the new act it is proposed that the special national rules are to be left out. Consequently, the national rules are not expected to be effective from 3 January 2018.

The Danish Crowdfunding offers are very limited, most Crowdfunding offers fall within the exemption for offers worth less than EUR 1,000,000 in a period of 12 months. There are other exemptions that may be applicable if single issues exceed this level such as if the issues are addressed solely to qualified investors or is addressed to fewer than 150 natural or legal persons. However, as the Danish offerings are very limited, and most often subject to the exemptions no prospectus requirement is likely to apply in respect of the types of Crowdfunding which are currently available or will be in the near future in Denmark.

## **3.3 Regulation of Crowdfunding under the AIFMD regime**

### **3.3.1 Equity Model and Lending Model**

A Crowdfunding platform where investors are offered a variety of start-ups, which they are able to invest in in order to receive a return may be subject to the Danish Act on Alternative Investment Fund Managers (Act no. 1074 of 6 July 2016) (the “AIFM Act”), if the platform will qualify as an Alternative Investment Fund. This definition is laid out in the AIFM Act implementing the Alternative Investment Funds Managers Directive (the “AIFMD”) in Danish legislation. If the platform qualifies as an alternative investment fund (an “AIF”), the persons administering the platform will qualify as Fund Managers and thereby be subject to the AIFM Act. Currently, no platforms have been registered as an AIF according to the Danish FSA’s homepage.

## **3.4 Regulation under Payment Services Directive**

### **(1) Lending Model**

If the activity rendered in connection with the Lending Model qualifies as payment services the rendering of such activity will require an authorisation from the Danish FSA pursuant to the Danish Payment Services and Electronic Money Act. The transmission of funds between the potential investor and the project/entity which is being funded may require

the Crowdfunding platform provider providing “money remittance” services under the Danish Payment Services and Electronic Money Act.

The Danish Payment Services and Electronic Money Act is expected to be replaced 1 January 2018 by a new Act on Payments, which will implement the PSD2-directive into Danish law. The bill for the new act was introduced to the Danish Parliament on 15 March 2017. The current form of the bill reflects an implementation, which is close to the wording of the directive. However, in certain areas gold plating of the PSD2-directive is proposed, including areas of consumer protection and the Danish debit card solution, “Dankortet”. Thus, the bill restricts the possibility for any provider to draw up consumer profiles based on data regarding the consumer’s payments. Moreover, the new act will comprise corporate governance obligations in regards to whistle blower-schemes and composition of management which are not included in the directive. This is because of the Danish implementation of Directive 2013/36/EU on Capital Requirements (CRD IV) which have been implemented to cover almost all financial institution in order to ensure uniform standards to financial groups which operates in various fields. Since a Crowdfunding platform based on the Lending Model may conduct activities covered by the Act on Payments such Crowdfunding platforms may be obligated to comply with the Danish requirements on corporate governance.

Furthermore, the new act proposes to implement the exemption as set out in article 32 of the PSD2-directive. Consequently, Crowdfunding platforms may only need a limited li-license provided that the platform does not exceed the threshold as set out in article 32 of the PSD2-directive.

### **3.5 Possible additional regulations**

#### **3.5.1 Equity Model**

Crowdfunding platforms facilitating the offering of securities or financial instruments as outlined above in paragraph 3.1.1 will be subject to the Danish Executive Order on Investor Protection (Executive Order no. 623 of 24 April 2015) and a suitability test will have to be performed on the investor in question. However, the suitability test is not a requirement, if the order is execution only. As a consequence of the MiFID II a revised version of the Executive Order was going out for consultation in March 2017. The revised version of the Executive Order requires also performance of a suitability test except if the order is execution only.

Furthermore, as all Danish investment firms are subject to the Danish Act on Prevention of Money Laundering and Financing of Terrorism (Consolidated Act no. 1022 of 13 August 2013) this will also apply in this situation. The Act on Prevention of Money Laundering and Financing of Terrorism is expected to be replaced by an entirely new Act in June 2017, which will implement EU’s fourth Anti-Money Laundering Directive.

#### **3.5.2 Donations or Rewards Model**

Donation campaigns must be notified to the Danish Fundraising Board and is subjected to the conditions of the Danish Fundraising Act (Act no. 511 of 26 May 2014). A fee of DKK

1,000 must be paid to the Danish Fundraising Board in case of notifications and applications, if the fundraising campaign falls within the scope of the Danish Fundraising Act. Any Crowdfunding platform that engages in donation-based Crowdfunding is governed by general regulations under company law. No other requirements are imposed.

The Danish reward-based Crowdfunding is similar to the donation-based model, however, the two models differ as a potential investor who invests in reward-based Crowdfunding expects to receive something in return and the transaction is therefore fiscally similar to selling a product. Companies who apply rewards-based Crowdfunding are obliged to list the income from such sale in their annual reports together with expenses for production and similar and thereby special attention is to be paid to corporate taxation and VAT declaration.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

A foreign Crowdfunding platform planning to offer its activities into Denmark on a cross border basis, have to overcome the same hurdles and barriers that apply to local Crowdfunding platforms under the existing regulatory framework described above. Thus, if the platform's Crowdfunding model constitutes the conduct of a regulated financial activity, the platform cannot provide such model without obtaining the relevant license or having the relevant passporting rights.

Before obtaining the relevant license, the Crowdfunding platform must determine to what extent Danish law is applicable. There are no specific rules, but a few elements provide for some guidance to this question. Firstly, the Danish licensing requirement is triggered by the marketing of products or services to persons in Denmark. Secondly, the license requirement is triggered when an entity is performing or carrying out financial activities in Denmark. However, the assessment may also include additional elements such as choice of language, registered office etc.

### 4.2 Inbound

The question is whether the foreign Crowdfunding platform addresses Danish investors or if wants to present Danish companies/projects on its platform.

#### 4.2.1 Foreign Crowdfunding platform addresses Danish investors

Danish applicable regulatory law distinguishes between requirements to

- Crowdfunding platform; and
- Company or project seeking funding.

##### 4.2.1.1 Crowdfunding platform

Foreign Crowdfunding platforms intending to address Danish investors must be duly licensed. Thus, any platform intending to carry out regulated financial activities or services must obtain license before commencing such activities. The license required depends on the

type of activity carried out or service performed. As stated above, Crowdfunding platforms based on the Lending-model may need to obtain a banking or payment services license. Equity-based Crowdfunding platforms may be required to obtain investment license.

Crowdfunding platforms from other EU countries are able to conduct financial activities and services in Denmark pursuant to the EU passport rules, which for the main part have been implemented into Danish law by way of the Danish Financial Business Act.

A platform which is duly licensed to conduct financial activities in its home state may passport its right into Denmark. When the Crowdfunding platform has determined that Danish law is applicable, based on the assessment stated above, the platform must first properly notify the competent authority in its home member state in order to carry out activities in Denmark. The cross-bordering Crowdfunding platform may start conducting services in Denmark, when the Danish FSA has received proper notification from the home state competent authority. The platform may also choose to carry out activities through a branch instead. If so, the platform must wait two months after the Danish FSA has received notification from the supervisory authority of the home country.

Moreover, EU/EAA licensed providers of payment services are able to passport their authorisation into Denmark pursuant to the notification procedures described above. However, in case the foreign provider is not duly licensed and wants to obtain license from the Danish FSA, in addition to not exceeding the established thresholds the provider must have its registered office in Denmark in order to obtain the limited license.

Any entity from an EU-country which is not duly licensed in its home member state is not able to benefit from the passport regime. Thus, such entities must apply for authorisation directly with the Danish FSA when the entity offers regulated financial activities.

#### **4.2.1.2 Company / project**

Similar to passporting financial activities under the Danish Financial Business Act, the issuer of a prospectus can passport such prospectus into Denmark. The issuer must advise the home state competent authority, which will then notify the Danish FSA, by submitting the approved prospectus, a certificate of approval, and a Danish translation of the summary. The issuer or arranger should obtain confirmation from the Danish FSA that it has received the documents on launch date minus three days. The Danish FSA will then one day prior to the launch date confirm to the competent authority of the home state that all documents required to the issuer to passport into Denmark have been received.

#### **4.2.2 Crowdfunding platform from another EU country addresses Danish companies/projects**

Danish law distinguishes between requirements to

- The foreign Crowdfunding platform; and
- The company/project intending to be funded on the Crowdfunding platform

#### 4.2.2.1 Crowdfunding platform

Here, the foreign Crowdfunding platform does not approach Danish investors, but Danish companies may use the foreign Crowdfunding platform to seek funding. Danish law does not apply to the platform, provided that (i) the Danish companies or projects make the initial approach and (ii) the services offered by the foreign Crowdfunding platform are not marketed or solicited to the Danish market. Since the regulated activities are not carried out in Denmark and the Crowdfunding platform is not based in Denmark, there are no license requirements under Danish law.

#### 4.2.2.2 Company / project

Danish prospectus regulation applies when the securities are offered to the public. It is thus central to the applicability of Danish law whether the securities are offered to the public of Denmark, as this will trigger the Danish prospectus rules which will then apply to the Danish company.

### 4.3 Outbound

In this situation a Danish Crowdfunding platform enters other European markets and thus addresses foreign investors.

The following distinguishes between

- Danish Crowdfunding platform addressing foreign (EU) investors; and
- Danish Crowdfunding platform addressing Danish investors and presenting a company/project from another EU member state on its platform

#### 4.3.1 Danish Crowdfunding platform addresses foreign (EU) investors

Here, only foreign investors with residence outside Denmark are addressed. However, both the Crowdfunding platform and the company/project are based in Denmark and thus have a Danish reference.

On the one hand, based on the assumption that marketing and financial activities are carried out outside Denmark, the Danish licensing requirements are not triggered.

On the other hand though, as the Crowdfunding platform and company/project are based and established in Denmark, the Danish FSA may come to the conclusion that Danish law is applicable as the registered office is included in the overall assessment.

##### 4.3.1.1 Crowdfunding platform

As mentioned above, since the Crowdfunding platform is based in Denmark, the Danish FSA may come to the conclusion that Danish law is applicable. Provided that the Crowdfunding platform carries out its activities while based in Denmark, the Danish FSA will most likely come to the conclusion that the Danish licensing requirements are triggered in the overall assessment.

Further, Danish Crowdfunding platforms based on the Equity-model or Lending-model may be subject to the Danish Act on Prevention of Money Laundering and Terrorist Financing (“The Danish AML Act”) which is an implementation of EU legislation. The bill for a new act was introduced to the Danish Parliament on 13 October 2016. The act will implement the EU AMLD4 as close to the wording of the directive.

The Danish AML Act applies to entities with certain financial licenses, including banking, payment services and investment services. In general, any Crowdfunding platform holding such license is thus subject to the Danish AML Act.

#### **4.3.1.2 Company / project**

In general, Danish law is applicable.

However, in connection with the Danish prospectus regulation, the rules are triggered when financial instruments are offered to the public in Denmark. It is thus central to the overall assessment of the application of Danish or foreign law, where the financial instruments are offered.

#### **4.3.2 Danish Crowdfunding platform addresses foreign companies/projects**

Here the Danish Crowdfunding platform approaches Danish investors while representing foreign companies/projects.

As Danish investors are approached, Danish law is applicable.

##### **4.3.2.1 Crowdfunding platform**

As stated above, Danish law is applicable. Hence, the Danish licensing requirements under the Danish Financial Business Act and other financial regulation are triggered.

Danish Crowdfunding platforms based on the Equity-model or Lending-model may be subject to the Danish AML as stated above.

##### **4.3.2.2 Company / project**

Based on the assumption, that equity or securities of the foreign company may be offered to the public (Danish investors) through the Danish Crowdfunding platform, Danish prospectus rules apply.

### **4.4 Impact of EU regulation**

The impact of EU regulations as regards to Danish Crowdfunding platforms and in relation to the regulatory barriers for crossing borders are described above in paragraph 3 (Current Regulation of Crowdfunding).

### **4.5 Summary**

Before obtaining any relevant license in Denmark, the Crowdfunding platform must determine whether the Crowdfunding platform is subject to Danish law. This is first and

foremost triggered by the marketing of products or services to persons in Denmark or when a Crowdfunding platform carries out financial activities in Denmark. However, as the assessment may be somewhat difficult in some cases, this may present a barrier for Crowdfunding platforms when determining which local requirements to comply with.

Crowdfunding platforms from other EU countries are able to conduct financial activities and services in Denmark pursuant to the EU passporting rules. However, the Equity and Donations or Rewards Model may be subject to additional specific Danish regulations as regards to investor protection regulation and certain Danish regulation in respect of certain donation campaigns.

Danish Crowdfunding platforms that wish to conduct activities in another EU country must notify the Danish FSA in accordance with the EU passporting rules. Further, the Danish Crowdfunding platform may also be subject to Danish law.

## **5 Lessons learned from Danish regulation for a possible harmonised European Crowdfunding regulation**

The focus on Crowdfunding in Denmark is relatively new in a legal perspective. This explains the lack of specific regulation of Crowdfunding. Accordingly, lessons learned from Danish regulation in respect of possible harmonised European Crowdfunding regulation are fairly limited.

## **6 Conclusion**

Crowdfunding has experienced rapid growth in Denmark during the last few years with the lending-based and the reward-based models being the most common used models. However, the focus on Crowdfunding is relatively new in Denmark. There is no specific regulation aimed at Crowdfunding or Crowdfunding platforms in Denmark and Crowdfunding businesses have to operate within the existing regulatory framework. The report published in May 2015 by the Danish Ministry of Industry, Business and Financial Affairs provides an overview of the regulation that entities must consider subject to their choice of Crowdfunding model.

EU Crowdfunding platforms wishing to operate in Denmark must consider if their business model requires any licenses that also applies to platforms established in Denmark. Conduct of financial regulated activities in Denmark, triggers the license requirement.

If the platform is duly licensed in its home state the platform can passport its rights into Denmark. However, the platform must first properly notify the home state competent authority, which will then notify the Danish FSA.

A Danish platform wishing to passport its rights out of Denmark may use a similar procedure, but properly notifying the Danish FSA instead.

## 7 Summary – Crowdfunding regulation

| Country   | Denmark  |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Danish Growth Fund and the Danish Crowdfunding Association published a report regarding the Danish Crowdfunding market in 2016. According to the report, Crowdfunding has experienced a rapid growth over the last few years, with reward-based and lending based Crowdfunding being the most popular in Denmark. Further, the very first Danish equity-based Crowdfunding platform has recently been launched.</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• If a Crowdfunding platform facilitates offering of securities or investment products the operator of the platform renders financial services, which is subject to a licensing requirement</li> <li>• Donations or Rewards Model does not involve any form of financial investment or financial return and therefore is not within the scope of the Danish financial regulation but only subject to additional regulation.</li> <li>• The Danish Ministry for Industry, Business and Financial Affairs recently announced that the Danish government intends to make it easier for fintech companies to be established in Denmark. The aim is to create a fintech lab within the Danish FSA, which will make it easier for digital start-ups to navigate within the financial regulation.</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for offering of securities or investment products.</li> <li>• Threshold: EUR 1,000,000 per issuer within 12 months.</li> </ul>   |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Crowdfunding platform may qualify as an AIF and be subject to the Danish AIFM Act.</li> <li>• The persons administering the AIF – platform may qualify as Fund Managers of the AIF.</li> </ul>  |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Transfer of funds through an operator may constitute money remittance service.</li> <li>• Requires Danish FSA's authorisation.</li> <li>• A bill for a new act has been introduced to the Danish Parliament to implement PSD2-directive.</li> </ul>   |
| <b>Consumer credit regulation</b>                     | <p>If consumer borrowers are permitted on a platform and Crowd-funding offered is based on the Lending Model there are requirements to the loan agreement pursuant to the Danish Act on Credit Agreements.</p>   |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• The Danish Act on Measures to Prevent Money Laundering and Financing of Terrorism</li> <li>• Danish Marketing Practices Act</li> <li>• Danish Investment Associations, etc. Act.</li> <li>• Danish Act on Credit Agreements.</li> </ul>   |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>• Danish Tax Rules</li> <li>• Danish Fundraising Act.</li> </ul>  |
| <b>Regulatory barriers</b>     |  |
| <b>Inbound</b>                 | <ul style="list-style-type: none"> <li>• Crowdfunding platforms must determine whether Danish law is applicable. This is first and foremost triggered by the marketing of products or services to persons in Denmark or when a Crowdfunding platform carries out financial activities in Denmark.</li> <li>• A foreign Crowdfunding platform planning to offer its activities into Denmark on a cross border basis, have to overcome the same hurdles and barriers that applies to local Crowdfunding platforms</li> </ul> |
| <b>Outbound</b>                | Danish Crowdfunding platforms planning to commence cross-border activities in another EU country must hold an equivalent license and receive notification from the Danish FSA before starting its activities.  |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | See section 3 “ <i>Current regulation of Crowdfunding</i> ”  |
| <b>AIFM-Directive</b>          | See section 3 “ <i>Current regulation of Crowdfunding</i> ”  |
| <b>MiFID / MiFID II</b>        | See section 3 “ <i>Current regulation of Crowdfunding</i> ”  |
| <b>PSD / PSD II</b>            | See section 3 “ <i>Current regulation of Crowdfunding</i> ”  |

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# Estonia

## 1 Recent developments in the market of Crowdfunding in Estonia

During the last years there were the following significant developments in Estonia regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Based on our research and analysis there are two operating Crowdfunding platforms based on the Equity Model in Estonia.

One platform enables investors to back companies while receiving equity in return. There are few successful campaigns rising funds from about EUR 20,000 to EUR 100,000 have been completed during the last years.

The second platform enables investors to invest in start-up syndicate loans receiving tokens from the syndicate which are tradable on the same platform. It means that investors can trade with their tokens and decide whether to increase or decrease their investments on daily basis. Over EUR 2,300,000 have been raised from investors so far. This platform is a mixed platform operating both based on the Equity model and Lending Model.

As of today the Estonian Equity Model Crowdfunding market to date has a very limited size compared to the overall Crowdfunding market in Estonia.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There are several peer-to-peer lending platforms in Estonia where the individuals and businesses can invest and borrow money according to the terms (e.g. investment rate, interest, etc.) they agree on.

As far as we are aware there are at least two operating platforms that focus on investing in real estate. Such platforms provide the possibility to give variable interest (the interest of which depends on the return of the real estate investment project) loans for the financing in real estate projects.

The activity of the platforms is loan brokerage and loan handling. The platforms control and analyse to a certain extent borrowers' loan history, payment defaults, financial status and / or bank account statements. In case of platforms enabling the lending to finance real estate projects the platform may also do a pre-assessment of the real estate investment projects for which the loan is applied. The platforms enable the meeting of lending and borrowing interests and mediate payments between lenders and borrowers.

There are also two new platforms which provide companies to sell their receivable invoices at the auction to investors with the highest bid. By investing in these invoices investors will

obtain new short-term investment instruments. The platforms select the companies which can sell its invoices to investors. These platforms are mediating factoring services as bank with the difference that invoices are sold at the auction to individual investors.

Overall peer to peer lending is very popular in Estonia. The market volume in 2015 was approximately EUR 17,000,000 with almost 17 000 active investors involved in investing in Crowdfunding platforms. We do not have yet the numbers for 2016 but it is expected to increase substantially.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

The Donations or Rewards Model is currently used by three platforms to finance creative projects (including design, music, art, film & photo, theatre, sport). No financial investment or return is involved. Investors fund projects or companies and get no return at all or a non-monetary reward (e.g. tickets, books, thank you notes in publications etc.). In many cases these rewards are of a symbolic value only.

### **1.4 Real Estate Crowdfunding / Renewable Crowdfunding**

A Crowdfunding platform does not raise capital from investors for its own business. Moreover, the platform does not manage the underlying investment but merely arranges investments into projects or companies or intermediates loans between natural persons.

Currently there are two main Crowdfunding platforms who presenting real estate projects. According to information available to public these two platforms have raised over EUR 35,000,000 combined. In 2016 the highest Real Estate Crowdfunding project raised EUR 1,500,000 within only three days which clearly indicates that investors have great trust in Real Estate Crowdfunding projects in Estonia.

The Renewable Crowdfunding is not so popular in Estonia. As far we are aware there have been only one project raising funds for bio-methane plant constructions. The project raised EUR 200,000 from 265 investors as a loan for two year within 15% annual interest rate.

### **1.5 International approach**

There are few foreign Crowdfunding platforms from other European countries (mainly from Baltics) which are trying to enter or already operate in the Estonian market. As a result of a market size there is no indications at the moment that any US/Canadian or other European platform would be interested in enter and provide its services in the Estonian market.

## **2 Recent developments regarding Crowdfunding regulation in Estonia**

Creditors and Credit Intermediaries Act (*krediidiandjate ja vahendajate seadus*) came into force in March 2015 and it imposes a licence obligation on creditors and credit intermediaries. This act applies to those Crowdfunding platforms which are providing or intermediating

credits to consumers. They have an obligation to obtain a licence from the Estonian Financial Supervision Authority and comply with the requirements set out in the Creditors and Credit Intermediaries Act.

There have been no developments regarding Crowdfunding regulation directly by any other new legislation.

However, Finance Estonia, a public-private cluster organisation in Estonia gathering companies from financial sector, has created together with market participants a non-binding Best Practice for the Crowdfunding industry (hereinafter the “Best Practice”) in order to provide the code of conduct to all the internet-based Crowdfunding platforms in Estonia that have joined the Best Practice at hand. The compliance with the Best Practice does not exempt a Crowdfunding platform provider from following the requirements provided by law. The Best Practice operates based on the principle of „comply or explain“, which means that a Crowdfunding platform provider shall notify the public on its website of whether the Best Practice principles are being complied with or not. In case a Crowdfunding platform provider that has joined the Best Practice does not follow a principle provided for in the Best Practice, the platform provider shall explain on its website, which principles are not being followed and why. As the Best Practice is not a binding regulation, it will not be discussed below.

Moreover, the Estonian Financial Supervision Authority has also drafted a draft law to regulate Crowdfunding platforms. Their aim with this draft is to regulate all platforms providing for financial gain, i.e. to exclude non-profit platforms. As this initiative has not developed into an act yet, this will not be discussed below under Section 3.

### 3 Current Regulation of Crowdfunding in Estonia

#### 3.1 Licence under the Estonian Securities Market Act (*väärtpaberituruseadus*) and Credit Institutions Act (*krediitiasutuste seadus*)

##### 3.1.1 Equity Model

Investment services and activities include, inter alia, reception and transmission of orders related to securities, execution of orders related to securities in the name of or for the account of the client and organising an offer or issue of securities. Activity licences are required if such services are provided on professional basis as a permanent activity.

Securities are, inter alia, (a) shares in public limited companies (*aktsiaselts*) and other transferable securities equivalent to such shares; (b) bonds or other forms of securitised debt; (c) investment fund units; or (d) any other securities giving the right to acquire or sell any such transferable securities or the price of which is determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures.

It is worth noticing that shares in Estonian private limited companies (*osaiühing*) are often not transferable securities due to the pre-emptive right of other shareholders under the Commercial Code (*äriregistri seadustik*).

In summary, where an online Crowdfunding platform facilitates the offering of transferable securities, or its operator acts as a securities broker, most likely, the operator of the platform will be deemed to provide investment services within the meaning of the Securities Market Act and therefore will require an investment firm licence by the Estonian Financial Supervision Authority.

However, as mentioned above, the licencing requirements only apply if services are provided in relation to transferable securities. Therefore, if the equity model entails offering or brokerage of securities which are not transferable (e.g. shares in private limited companies where the pre-emptive right of other shareholders exists) or facilitating the formation of limited partnerships (*usaldusühing*) or the joining of additional partners into such limited partnerships, such activities do not constitute provision of investment services. Therefore, no licencing requirement under the Securities Market Act would apply.

None of the Crowdfunding platform based on Equity model existing currently in Estonia has a licence under the Securities Market Act.

### 3.1.2 Lending Model

Depending on the detailed structure of how the Lending Model is used, loans issued using the Lending Model are generally not considered as transferable securities and their offering or brokering would therefore not qualify as provision of investment services under the Securities Market Act.

Pursuant to the Credit Institutions Act, a company intending to receive cash deposits or other repayable funds from the public in any other manner and to grant loans for its own account and provide other financing, is a credit institution. The right to receive money from the public for the purposes of depositing is the exclusive right of the credit institution. In order to exercise this right the credit institution must hold a corresponding authorisation granted by the EFSA.

In Estonia, the Lending Model is based on loans between individuals and companies or individuals and is represented by private limited companies providing lending brokerage. Under Estonian models, the companies operating the platforms do not grant loans on their own account. Instead, they provide relevant information between potential borrowers and lenders. The whole process of investing and lending is under platform clients' own control.

Normally, the operators of platforms using the Lending Model receive money from lenders/borrowers, to pay the money on to, respectively, the borrowers as disbursement of the loan or the lenders as repayment of loan or interest.

However, in case a lending and borrowing interest do not meet, it may happen that the person who wanted to lend money may demand repayment of the funds from the platform operator, which may be deemed receipt of repayable funds from the public on part of the operator. On the other hand, the sums transferred to the operator are repaid only under exceptional circumstances and the repayment of sums is not the essence of the business.

Therefore, we would conclude that the risk that such platform operators are considered to receive money from the public for the purposes of depositing is not great.

Consequently, these broking companies are not credit institutions within the meaning of the Credit Institutions Act and do not require a licence for operation. However, if a company wishes to use the Lending Model in Estonia by gathering money from lenders and borrowing it on its own account, such activity would most probably require a credit institution licence.

### **3.1.3 Donations or Rewards Model**

Depending on the detailed structure it could be stated that these kinds of investments do not qualify as investment services as they do not relate to securities.

Also, as the money is donated rather than lent, such activity should not require a banking licence. In case the platform operator, under certain circumstances, repays the money donated to the donator, the analysis of whether such activity would constitute receipt of repayable funds from the public above would equally apply here. Similarly to the above analysis, in our opinion, it should not be deemed as receipt of repayable funds from the public.

## **3.2 Licence under Creditors and Credit Intermediaries Act**

### **3.2.1 Equity Model**

Crowdfunding platforms operating under the Equity model do not engage in crediting nor credit intermediating, thus, such platforms are not obliged to obtain a licence under the Creditors and Credit Intermediaries Act.

### **3.2.2 Lending Model**

Since March 2016, in order to operate as a creditor in Estonia, a licence must be held. In order to operate as a credit intermediary, a legal or natural person shall hold a licence. For the purposes of Creditors and Credit Intermediaries Act, granting of credit means also the postponement of a due date for a charge, leasing or any other similar financial accommodation, including the entry into credit agreements and performance of acts needed for this purpose in the person's own name and on the person's own account. Intermediation of credit means:

- intermediating the granting of credit or indicating the possibility to enter into a credit agreement to a consumer for a charge;
- assisting consumers in acts preliminary to entering into a credit agreement or in entering into the agreement and any other activities related thereto which have not been specified in clause 1) of this section;
- in the interests of and for the benefit of the creditor, negotiating or entering into agreements on behalf and on the account of the creditor independently and on a permanent basis.

Thus, when a Crowdfunding platform grants credit to consumers or intermediates granting of credit, it should obtain a licence under Creditors and Credit Intermediaries Act.

Currently 4 platforms have obtained a licence as credit intermediaries and at least 2 platforms have obtained a licence as creditor.

There is also one exception from licence obligations that can be exercised by a creditor or a credit intermediary whose parent company is a credit institution founded in a state which is a contracting party to the EEA Agreement and the creditor or the credit intermediary is a company controlled, within the meaning of article 10 of the Securities Market Act, by such credit institution and the creditor or the credit intermediary is subject to the consolidated supervision of the Financial Supervision Authority or the financial supervision authority of another EEA country. In such case the Crowdfunding platform does not need to obtain a licence, it is nevertheless obliged to follow certain rules and obligations from the Creditors and Credit Intermediaries Act.

### 3.2.3 Donations or Rewards Model

Such companies do not engage in granting of loans, thus, such Crowdfunding Platforms would not require a licence.

## 3.3 Prospectus requirements

If securities (including tradable shares and/or bonds) are publicly offered to investors, the company issuing the securities has to publish a prospectus. The prospectus can be published only after the EFSA approves it. Where securities are publicly offered through a Crowdfunding platform, the operator of the Crowdfunding platform should ensure that the securities are publicly offered through the Crowdfunding platform only after the prospectus is published.

Requirements for the preparation, submission and approval of the prospectus and exemptions from the requirement to publish the prospectus are established by the Securities Market Act. In contrast to several other countries, where the prospectus requirement does not apply to the offering of securities with a value of EUR 5 million or less within a one-year period, in Estonia specific requirements towards the prospectuses in such offerings are established by a regulation of the Minister of Finance (*Nõuded väärtpaberite avaliku pakkumise, kauplemis- ja noteerimisprospektile*) instead of the Prospectus Regulation (Commission Regulation (EC) No 809/2004). Therefore, publicly offering securities using a Crowdfunding platform in Estonia is likely to require publication of a prospectus, subject to certain exemptions.

The prospectus is not required if securities are not offered publicly. An offer of securities is not deemed to be public in the case of:

- an offer of securities addressed solely to qualified investors, or
- an offer of securities addressed to fewer than 150 persons per EEA Contracting State, other than qualified investors, or
- an offer of securities addressed to investors who acquire securities for a total consideration of at least EUR 100,000 per investor, for each separate offer, or

- an offer of securities with the nominal value or book value of at least EUR 100,000 per security, or
- an offer of securities with a total consideration of less than EUR 100,000 per all the EEA Contracting States in total calculated in a one-year period of the offer of the securities.

Also, the prospectus requirement does not apply if the offering does not concern securities (e.g. it involves shares in an Estonian private limited company). However, in case a foreign Crowdfunding instrument constitutes an investment fund, we note that public offering of non-tradable units of such non-Estonian investment fund may be subject to Estonian law regulation on the public offering of investment fund units.

The platforms operating Lending Model and Donations and Rewards Model are not subject to prospectus requirements.

### **3.4 Regulation of Crowdfunding under the AIFMD regime**

The Law enabling alternative investment fund managers (AIFM) from other EU countries marketing EU AIFs to passport to Estonia was passed on 20 June 2013, effective of 22 July 2013. Further amendments to the Investment Funds Act (*investeerimisfondide seadus*) were passed on 9 May 2014, effective of 19 May 2014. The aim of the amended Investment Funds Act was to transpose other provisions of the AIFMD into Estonian law. The new legislation does not introduce any new provisions that would explicitly deal with Crowdfunding, however, depending on the nature and the scope of services provided by a Crowdfunding platform it might qualify as an AIFM and therefore each situation should be evaluated on case by case basis. If the platform qualifies as an AIFM it will require a licence from EFSA.

### **3.5 Licence under the Payment Institutions and E-money Institutions Act (*makseasutuste ja e-raha asutuste seadus*)**

In addition to the requirements set out above, any transfer of funds through the operator of a Crowdfunding platform may generally constitute payment services (if a payment account is opened) or money remittance services (if no payment account is opened) within the meaning of the Payment Institutions and E-money Institutions Act. Transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform who then passes the funds to the person taking advantage of the Crowdfunding financing scheme, or back to the investor in case the funding transaction fails.

The platform operator might rely on the exemption for commercial agents under the Payment Institutions and E-money Institutions Act. However, there is no established practice in Estonia regarding when the commercial agents exemption applies.

As an alternative - in order to avoid such licencing or the need to apply for an exemption, as a case may be, requirements - the operator of a Crowdfunding platform might use an external provider or partner for processing payments rather than acting as an intermediary himself.

We are not aware of any cases in Estonia where a Crowdfunding platform holds a payment institution licence or where either of above exemptions has been applied to a Crowdfunding platform. Thus, in each situation where any of these exemptions is considered we strongly recommend that beforehand respective project the structure of each platform is coordinated with the EFSA and/or local counsel is involved.

### 3.6 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- The Law of Obligations Act (*võlaõigusseadus*);
- Money Laundering and Terrorist Financing Prevention Act (*rahapesu ja terrorismi rahastamise tõkestamise seadus*);
- Estonian Advertising Act (*reklaamiseadus*);
- Personal Data Protection Act (*isikuandmete kaitse seadus*);
- Consumer Protection Act (*tarbijakaitse seadus*)

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

As described above there is no single law governing the activities of the Crowdfunding platforms in Estonia. Therefore, the Crowdfunding platforms must closely monitor which laws are applicable to them as a result of their business structure. This could seem as a general regulatory barrier for Crowdfunding platforms wishing to provide their services in several states.

As a general rule, the laws of Estonia become applicable to foreign Crowdfunding platforms if they approach, offer or provide their services to persons whose place of residence or location is in Estonia. As a result, the Crowdfunding platforms may need to apply for a permit for operating in Estonia if referred so below.

Similarly, the Crowdfunding platforms operating in Estonia may need an approval from the Estonian FSA and the supervisory authority of a foreign state where the Crowdfunding platform wishes to pursue its activities in that foreign state.

The barriers to the Crowdfunding have been more closely reviewed below.

### 4.2 Inbound

In this situation European Crowdfunding platform enters Estonian market and therefore addresses Estonian investors.

## 4.2.1 Foreign Crowdfunding platform addresses investors in Estonia

As mentioned above according to the Estonian legislation the laws of Estonia become applicable to foreign Crowdfunding platforms if they approach, offer or provide their services to persons whose place of residence or location is in Estonia.

### 4.2.1.1 Crowdfunding platforms

#### (1) Licence obligations

The applicable regulatory law largely depends on whether Crowdfunding platform has a licence from another EEA Contracting State.

##### (a) MiFID licence

As stated under section 3.1 above if an online Crowdfunding platform facilitates the offering of transferable securities or its operator acts as securities broker, the operator of the platform is considered to provide investment services. If a foreign Crowdfunding platform and its operator provides such investment services in Estonia then their activities are subject to the regulation resulting from the Estonian Securities Market Act (implementing the MiFID). The investment services of a foreign Crowdfunding platform and its operator may be deemed to be provided in Estonia if the investment services are provided to persons whose place of residence or location is in Estonia or the services are advertised in Estonia or if the manner of the offer or the contents thereof enable to conclude that the offer is aimed at persons whose residence or location is in Estonia. Therefore, if the operator wishes to provide the investment services described above to the persons in Estonia it has to follow the requirements provided in the Estonian Securities Market Act.

Thus, if the operator of a Crowdfunding platform holding the licence of an investment firm from another EEA Contracting State wishes to found a branch or to start providing cross-border services in Estonia it can passport its licence of the home state to provide services in Estonia. Therefore, the Crowdfunding platform operator is required to inform the securities market supervisory agency of the EEA Contracting State and submit required information and documents.

If the operator of the foreign Crowdfunding platform does not hold an authorisation to provide investment services in its home state the foreign Crowdfunding platform is not able to apply the passporting or the authorisation requirements set above. This will most likely result in applying the full licencing process under the Estonian law in order to provide its services in Estonia.

##### (b) Granting or intermediate granting of credit licence

Where the foreign Crowdfunding platform approaches the investors in Estonia (consumers) to raise money through a Crowdfunding platform which constitutes for the platform as granting or intermediate granting of credit the Crowdfunding platform has to follow the requirements resulting from the Creditors and Credit Intermediaries Act.

If the foreign Crowdfunding platform is allowed to grant credit or intermediate granting the credit based on the legislation of its home state and holds a licence for providing such services from its home state competent authority then the Crowdfunding platform may provide the same services also in Estonia. For this purpose the foreign Crowdfunding platform may establish a branch in Estonia or provide its services cross-border. In order to establish a branch or provide its services cross-border in Estonia the foreign Crowdfunding platform is required to apply for a permit from the Estonian Financial Supervision Authority.

However, if the foreign Crowdfunding platform does not hold an authorisation to grant or intermediate granting the credit from its home state the foreign Crowdfunding platform is not able to apply to the permit based on the above. This will result in applying the full licencing process under the Estonian law in order to provide its services to Estonian consumers.

Also, the concept of credit intermediary under the Estonian law does not have clear borders. As a result, the range of services falling under this concept is wide. Therefore, the Crowdfunding platforms which are in any way involved in intermediating credit to consumers should consider whether their activities would fall under the credit intermediary.

#### **(c) AIFM licence**

If the Crowdfunding platform offers its services to Estonian investors and qualifies as an AIFM it will be subject to the requirements arising from the Estonian Investment Funds Act.

A Crowdfunding platform of an EEA Contracting State which qualifies as an AIFM and holds the licence to operate as an AIFM in another EEA Contracting State can passport its licence to provide services to investors in Estonia. The Crowdfunding platform should notify the Estonian Financial Supervision Authority through its home state supervisory authority.

#### **(d) Payment service licence**

The fund transfer is an ancillary service to Crowdfunding platforms when approaching Estonian investors. However, the activity is under the supervision of the Estonian Financial Supervision Authority.

The foreign Crowdfunding platform that allows the investors located in Estonia to transfer any of the funds through the operator of Crowdfunding platform and holds a licence for such services in a home state is required to establish a branch or provide services cross-border in Estonia in accordance to the Payment Institutions and E-money Institutions Act. Based on the origin of the state where the licence is granted the requirements for providing payment services in Estonia vary.

If the payment or e-money institution holds a licence of an EEA Contracting State then the institution is able to passport its licence in order to found a branch or provide cross-border services in Estonia. Therefore the payment or e-money institution of another EEA Contracting State has to inform and submit required information to the Estonian Financial Supervision Authority thereof through the financial supervision authority of the EEA Contracting State.

## **(2) Other financial regulation**

If the Crowdfunding platform is operating under any of the licenced activities referred to above through a branch they are subject to Estonian anti-money laundering regulation (Estonian Money Laundering and Terrorist Financing Prevention Act). Crowdfunding platforms offering cross-border services are not currently clearly stated to form a part of the obligated persons pursuant to Estonian anti-money laundering regulation. However, the Estonian Financial Supervision Authority has been of the opinion they are under the anti-money laundering regulation.

Note, that the Estonian anti-money laundering regulation is currently under revision and according to the new regulation the service providers above which offer cross-border services in Estonia are clearly within the scope of anti-money laundering obligations.

### **4.2.1.2 Company / project**

#### **(1) Estonian prospectus regulation**

If the securities are publicly offered to investors in Estonia by a foreign company/project it has to follow the requirements of public offering according to the Securities Market Act. Thus, the company has to publish a prospectus and the Estonian Financial Supervision Authority must approve it.

The issuer of securities of another EEA Contracting State can offer its securities in Estonia based on the prospectus registered by the securities market supervisory agent of another EEA Contracting State member state who has to confirm that the prospectus has been prepared pursuant to the requirements for prospectuses provided for in EEA legislation.

#### **(2) Other financial regulation**

Foreign companies issuing securities that are admitted to trading on a regulated market are subject to wider information disclosing requirements under the Estonian Securities Market Act.

If the issuing entity does not fall under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act then the issuer is not required to comply with the anti-money laundering regulation in Estonia.

## **4.2.2 Foreign Crowdfunding platforms addressing companies/projects in Estonia**

### **4.2.2.1 Crowdfunding platforms**

#### **(1) Licence**

Where the Estonian investors are not addressed or the service of the Crowdfunding platform is not offered in Estonia but the Estonian companies/projects are involved in the

Crowdfunding platform it will not trigger the licencing obligations as described under section 4.2.1. above.

Therefore, the MiFID licence in Estonia is not required if the investment services are not provided to persons whose place of residence or location is in Estonia or the services are not advertised in Estonia or if the manner of the offer or the contents thereof do not enable to conclude that the offer is aimed at persons whose residence or location is in Estonia.

The granting or intermediating of granting of credit do not require licencing in Estonia if the investors (consumers) from Estonia are not approached to raise money through a Crowdfunding platform.

The AIFM licence in Estonia is not required if the Crowdfunding platform does not offer it services to Estonian investors.

The licence of payment institution in Estonia is not required if the Estonian investors do not transfer funds through the Crowdfunding platform.

## **(2) Other financial regulation**

If the Crowdfunding platform does not require a licence pursuant to section 4.2.2.1 (1) above and therefore does not operate in Estonia through a branch or providing cross-border services then the anti-money laundering regulation in Estonia does not apply.

### **4.2.2.2 Companies / projects**

#### **(1) Estonian prospectus regulation**

If the securities are not publicly offered to investors in Estonia as described under section 4.2.1.2 (1) above the Estonian prospectus regulation does not apply. It should be clearly followed by the company that the securities are not offered to investors in Estonia.

#### **(2) Other financial regulation**

If the issuing entity does not fall under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act then the issuer is not required to comply with the anti-money laundering regulation in Estonia.

## **4.3 Outbound**

In this situation Estonian Crowdfunding platform enters European markets and therefore addresses foreign investors.

### **4.3.1 Estonian Crowdfunding platform addresses EEA investors**

As mentioned above according to the Estonian legislation the laws of Estonia become applicable to the Crowdfunding platforms approach, offer or provide their services to persons whose place of residence or location is in Estonia. However, if the Crowdfunding platform only provide their services to persons outside of Estonia and the provision of services does not let

to doubt that the services are only provided to investors outside of Estonia (e.g. usage of foreign language) then the Estonian legislation shall not apply.

#### **4.3.1.1 Crowdfunding platform**

##### **(1) Licence obligations**

###### **(a) MiFID licence**

If the operator of a Crowdfunding platform is holding the licence of investment firm in Estonia and wishes to provide the investment services provided for in its activity licence cross-border or to found its branch in another EEA Contracting State, the operator is able to passport its licence. However, the operator should notify the Estonian Supervision Authority of its intention and submit required information and documents to the Supervision Authority.

In addition, the Estonian operator of the Crowdfunding platform has to fulfil any of the legal requirements of the state where it wishes to start providing investment services and may therefore be subject to barriers.

###### **(b) Licence of granting or intermediate of granting credit**

If the Estonian Crowdfunding platform holding the licence to grant or inter-mediate granting of credit in Estonia wishes to start granting credit or inter-mediate credit granting outside of Estonia on their Crowdfunding platform, it may provide its services based on the authorisation from Estonia. However, for such activities the Estonian Crowdfunding platform has to apply for the respective permit from the Estonian Financial Supervision Authority.

In addition, the Estonian Crowdfunding platform has to fulfil any of the legal requirements of the state where it wishes to start granting or intermediate granting of credit and may therefore be subject to barriers.

###### **(c) AIFM licence**

An Estonian Crowdfunding platform which qualifies as an AIFM and holds the licence to operate as an AIFM in Estonia can passport its licence to provide its services to investors in another EEA Contracting State. The Crowdfunding platform is therefore required to notify the Estonian Financial Supervision Authority.

In addition, the Estonian Crowdfunding platform has to fulfil any of the legal requirements of the state where it wishes to start providing its services and may therefore be subject to barriers.

###### **(d) Payment institution licence**

If the Estonian Crowdfunding platform holds the licence of payment or e-money institution to allow also other EEA investors to transfer any of the funds through the operator of Crowdfunding platform it may provide such services to investors outside of Estonia after meeting certain criterions.

A payment or e-money institution holding a licence under Estonian law is able to passport its licence if it intends to found a branch in another EEA Contracting State. Therefore, the payment and e-money institution must inform the Estonian Financial Supervision Authority of its intention and submit required information and documents. Also if a payment or e-money institution holding a licence under Estonian law wishes to start providing payment or e-money services on a cross-border basis in a foreign state (EEA Contracting State) it has to inform the Estonian Financial Supervision Authority thereof and shall submit required information and documents.

In addition, the Estonian Crowdfunding platform has to fulfil any of the legal requirements of the state where it wishes to start offering any payment or e-money services and may therefore be subject to barriers.

## **(2) Other financial regulation**

The Estonian anti-money laundering regulation is applicable to the extent that the Crowdfunding platform established under any of the licences listed above offers its services in Estonia.

### **4.3.1.2 Company / project**

#### **(1) Prospectus regulation**

If an Estonian Crowdfunding platform presents an issuer registered in Estonia then pursuant to the Estonian Securities Market Act the Estonian issuer has the right to offer securities to the public in all other EEA Contracting State on the basis of a prospectus and supplements to the prospectus registered with the Estonian Financial Supervision Authority. In addition, the Estonian issuer has to fulfil any of the legal requirements of the state where it wishes to start offering securities and may therefore be subject to barriers.

#### **(2) Other financial regulation**

If the issuing entity does not fall under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act then the issuer is not required to comply with the anti-money laundering regulation in Estonia.

### **4.3.2 Estonian Crowdfunding platform addresses foreign companies/projects**

#### **4.3.2.1 Crowdfunding platform**

##### **(1) Licence Obligation**

In case the Estonian Crowdfunding platform approaches Estonian investors and presents foreign companies/projects the regulation the Estonian Crowdfunding platform is subject to general licencing process under the Estonian Securities Market Act. The Estonian Crowdfunding platform may be subject to additional requirements of the foreign state where the companies/projects are from, however this shall not be analysed under the Estonian law.

In case the Estonian Crowdfunding platform approaches EU investors and presents foreign companies /projects the regulation under section 4.3.1.1. (1) applies. Similarly to above, the Estonian Crowdfunding platform may be subject to additional requirements of the foreign state where the companies/projects are from, however this shall not be analysed under the Estonian law.

## **(2) Other financial regulation**

The Estonian anti-money laundering regulation applies if the services are provided to investors located in Estonia.

### **4.3.2.2 Company / project**

#### **(1) Prospectus regulation**

If the Estonian Crowdfunding platform presents foreign company/project to Estonian investors the Estonian Securities Market Act applies to the requirements on the prospectus in addition to the requirements of the home state of the foreign company/project pursuant to section 4.2.1.2. above. If the Estonian Crowdfunding platform however presents foreign company/project to foreign investors the Estonian prospectus requirements do not apply.

If the Estonian Crowdfunding platform presents Estonian company/project to Estonian investors the general prospectus requirements apply under the Estonian Securities Market Act.

#### **(2) Other financial regulation**

If the issuing entity does not fall under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act then the issuer is not required to comply with the anti-money laundering regulation in Estonia.

## **4.4 Impact of EU regulation**

### **4.4.1 Prospectus regulation**

The prospectus regulation has been implemented in Estonia in the Securities Market Act. The prospectus regulation has relatively high impact on the Crowdfunding market as it sets the requirements on the public offering of securities and to the prospectus to be published.

### **4.4.2 AIFMD**

The AIFMD has been implemented in the Estonian Investment Funds Act, which was revised in January 2017. Based on the AIFMD regulation the operators of Crowdfunding platforms which qualify as the AIFM-s are subject to unified regulation. It also allows the Crowdfunding platforms operating in other EEA Contracting State based on the AIFM licence to passport their licence and operate in Estonia without burdensome licencing process except if under the Estonian law it does not qualify as the AIFM. Therefore, the AIFMD simplifies

the process of operating Crowdfunding platforms cross-border and has thus high impact on the Estonian Crowdfunding market.

#### 4.4.3 MiFID and MiFID II

MiFID has been implemented in Estonia in the Estonian Securities Market Act. MiFID II comes into effect January 2018 and is changing the Estonian Securities Market Act. However, the impact of MiFID II on Estonian Crowdfunding platforms is rather limited as there are currently no Crowdfunding platforms in Estonian that operate based on a licence under the Estonian Securities Market Act.

#### 4.4.4 PSD and PSD II

The Payment Services Directive (PSD) was implemented in Estonia in January 2009 in the Payment Institutions and E-money Institutions Act and the Law of Obligations Act. The PSD II has to be implemented by January 2018. As described above then any transfer of funds through the operator of a Crowdfunding platform may generally constitute payment services or money remittance services and therefore the changes in the respective directives will also have impact on the Crowdfunding platforms. However, as stated above there are currently no Crowdfunding platforms that would operate in Estonia under the licence of payment or e-money institution. Therefore, the changes to the regulation could be deemed to have moderate impact in Estonia.

### 4.5 Summary

The main barriers to the inbound and outbound of operating Crowdfunding platforms result from the fragmented level of laws applicable to the Crowdfunding in different jurisdictions. As referred to above there is no single or general law in Estonia applying to Crowdfunding but several different laws which have to be followed depending on the model of the Crowdfunding platform. Thus, the Crowdfunding platforms wishing to operate cross-border have to follow carefully the requirements from the law possibly influencing the provision of their services.

The other main barriers to the inbound and outbound of Crowdfunding platforms result from the requirements of authorisation or notification of the competent authorities, as follows:

- Inbound
  - The Crowdfunding platforms holding the licence of an AIFM, payment or e-money institution from another EEA member state may passport their licence when offering their services in Estonia except if the platform having the AIFM or payment or e-money institution licence do not qualify as such under the Estonian law. Only these Crowdfunding platforms that hold the licence as creditors and credit intermediaries in their home state and wish to provide their services in Estonia have to apply for a permit. Therefore, the barriers to the Crowdfunding platforms qualifying as creditors or credit intermediaries are more extensive in comparison with other models of the Crowdfunding platforms.

- The Estonian prospectus regulation applies if the securities are offered to investors in Estonia.
- If Crowdfunding platform or the company/project falls under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act and is offering its services in Estonia through a branch or cross-border then the Crowdfunding platform or the company/project is required to comply with the anti-money laundering regulation in Estonia.
- Outbound
  - The Crowdfunding platforms holding the licence of an AIFM, payment or e-money institution from Estonia may passport their licence when offering their services another EEA member state. However, if the Crowdfunding platform operating in Estonia under the licence of creditor or credit intermediary then it has to apply for a permit from the Estonian Financial Supervision Authority to operate in another EEA member state and the authorisation from the competent authority of this state where the services are provided. Similarly to above, the Estonian Crowdfunding platforms which are operating in Estonia under the licence of a creditor or credit intermediary are not able to passport their licence and are therefore subject to more extensive barriers in comparison with other models of Crowdfunding platforms.
  - The Estonian prospectus regulation applies if the securities are offered to investors in Estonia.
  - The Estonian Crowdfunding platform has to take into account any of the legal requirements or barriers of the third country where it wishes to start providing its services.
  - If Crowdfunding platform or the company/project falls under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act and is offering its services in Estonia through a branch or cross-border then the Crowdfunding platform or the company/project is required to comply with the anti-money laundering regulation in Estonia.

## 5 Lessons learned from Estonia's regulation for a possible harmonized European Crowdfunding regulation

### 5.1 Role model ("dos")

There is no special regulation governing Crowdfunding in Estonia, therefore no legal provisions or practice can be presented as examples.

### 5.2 Aspects that should be avoided ("don'ts")

There is no special regulation governing Crowdfunding in Estonia, therefore no legal provisions or practice can be presented as examples.

## 6 Conclusion

There have been no substantial developments in relation to Crowdfunding in Estonia and currently there is still no regulatory regime that is specifically adapted to Crowd-funding in Estonia. There are two platforms operating Equity Model in Estonia, but this type of model might be subject to investment services or securities market regulation and thus be supervised by the FSA if the platform provides investment services such as securities brokering or organising an offer or issue of securities. In addition, those securities that are publicly offered are subject to the prospectus requirements.

As a change the lending based platforms in Estonia are governed by the Creditors and Credit Intermediaries Act as of March 2015.

The Donations and Rewards Model falls outside of the financial services scope and the corresponding regulation.

In case of Crowdfunding platforms using any of the above models, it should be analysed on a case by case basis whether a payment institution licence or applying for an exemption from the licencing obligation is needed. This will also apply to the crowd-funding platforms that wish to operate cross-border.

To conclude, the two models of Crowdfunding platforms operating in Estonia operate based on the licence of Creditors and Credit Intermediaries Act and are under the supervision of the Estonian Financial Supervision Authority.

## 7 Summary – Crowdfunding regulation

| Country   | <b>Estonia</b>   |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <p>Creditors and Credit Intermediaries Act (hereinafter “CCIA”) came into force in March 2016 and it imposes a licence obligation on creditors and credit intermediaries. This act applies to those Crowdfunding platforms which are providing or intermediating credit to consumers. Moreover, there is non-binding soft regulation regarding Crowdfunding platform which was drafted by a cluster organisation Finance Estonia together with important market players.</p>   |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• If Crowdfunding platform organises offering of securities or acts as a securities broker, it provides investment service<br/>→ FSA authorisation required</li> <li>• Crowdfunding platforms granting or intermediating credit to consumer need a licence from the FSA as a creditor or credit intermediary.</li> <li>• Crowdfunding platform operating the Donations/Rewards Model is not subject to financial services regulation.</li> </ul> <p>Currently 4 platforms have obtained a licence as credit intermediaries and 2 platforms have obtained a licence as creditor.</p> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for public offering of securities (securities do not include shares in Estonian private limited companies).</li> <li>• Exceptions apply, e.g. if the number of investors less than 150 per EEA country or total amount of investments less than EUR 100,000.</li> </ul>  |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• AIFMD regulation was implemented in the Investment Funds Act in 2013 and 2014.</li> <li>• Implementing act does not introduce any provisions that would explicitly deal with Crowdfunding.</li> </ul>   |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Transfer of funds through operator may constitute payment service or money remittance service<br/>→ FSA activity licence or application to use exemption required.</li> <li>• “Commercial Agents” exemption may be applicable to operators of Crowdfunding platforms.</li> <li>• Cooperation with payment institute / bank is necessary.</li> </ul>   |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• The Law of Obligations Act (võlaõigusseadus);</li> <li>• Money Laundering and Terrorist Financing Prevention Act (rahapesu ja terrorismi rahastamise tõkestamise seadus);</li> <li>• Estonian Advertising Act (reklaamiseadus);</li> <li>• Personal Data Protection Act (isikuandmete kaitse seadus);</li> <li>• Consumer Protection Act (tarbijakaitse seadus).</li> </ul>   |

| <b>Regulatory barriers</b>     |  |
|--------------------------------|--|
| <b>Inbound</b>                 | <ul style="list-style-type: none"> <li>• Fragmented laws</li> <li>• Requirements of permitting the activities for Crowdfunding platforms falling under the concept of creditor or credit intermediary inbound from other EEA Contracting States</li> <li>• Subject to prospectus regulation if the securities are offered to investors in Estonia</li> <li>• If Crowdfunding platform or the company/project falls under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act and is offering its services in Estonia through a branch or cross-border then the Crowdfunding platform or the company/project is required to comply with the anti-money laundering regulation in Estonia</li> </ul>   |
| <b>Outbound</b>                | <ul style="list-style-type: none"> <li>• Fragmented laws</li> <li>• Requirements of permitting the activities for Crowdfunding platforms falling under the concept of creditor or credit intermediary to outbound to other EEA Contracting States</li> <li>• Subject to prospectus regulation if the securities are offered to investors in Estonia</li> <li>• If Crowdfunding platform or the company/project falls under the definition of an obligated person pursuant to Estonian Money Laundering and Terrorist Financing Prevention Act and is offering its services in Estonia through a branch or cross-border then the Crowdfunding platform or the company/project is required to comply with the anti-money laundering regulation in Estonia</li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulation</b>   | Relatively high impact as the changes to the Prospectus regulation would influence the regulation regarding the public offering of securities in Estonia.  |
| <b>AIFM-Directive</b>          | The AIFMD has been implemented in the Estonian law and is therefore applicable to the Crowdfunding platforms that wish to operate in Estonia as AIFM-s. As the AIFMD simplifies the process of operating Crowdfunding platforms cross-border the change in the AIFMD would have high impact on the Estonian Crowdfunding market.   |
| <b>MiFID / MiFID II</b>        | As there are currently no Crowdfunding platforms in Estonia which operate based on a licence under MiFID then the impact to the Crowdfunding market in Estonia from the change in regulation would be limited.   |
| <b>PSD / PSD II</b>            | As there are currently no Crowdfunding platforms that would operate in Estonia under the licence of payment or e-money institution the changes to the regulation could be deemed to have moderate impact on the Crowdfunding market in Estonia.  |

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# Finland

## 1 Recent developments in the market of Crowdfunding in Finland

Finland's Crowdfunding market has grown rapidly and significantly during recent years. According to a survey conducted by the Ministry of Finance, the total amount of Crowdfunding collected in 2016 was estimated to be EUR 153 million, compared with EUR 70.5 million in 2015 and EUR 52 million in 2014. The increase in the size of the market has been particularly rapid in relation to equity-based and lending-based Crowdfunding.

The growth of the Crowdfunding sector can be seen as part of the emerging digitalisation of the financial sector, which lowers the threshold to enter the market and thus attracts new innovative market participants to the industry. Further, stringent regulatory environment has required start-up companies as well as small and mid-size companies to seek funding by means beyond traditional financing channels, which has supported the increasing popularity of Crowdfunding.

The Finnish Crowdfunding Act (734/2016, "CFA") took effect in 2016, establishing regulatory regime specifically for Crowdfunding in Finland. The CFA is part of Prime Minister Sipilä's key Government projects action plan where the Government aims to amend, deregulate and reform legal provisions and thus support Finland's growth, strengthen its competitiveness and promote digitalisation. The CFA aims to clarify the ground rules for Crowdfunding and facilitate entry into the Crowdfunding market, and is therefore expected to contribute to further growth of the market. In 2016, eight entities applied for registration from the Finnish Financial Supervisory Authority (the "FIN-FSA") as a Crowdfunding intermediary, most of which offer or mediate Lending Model Crowdfunding.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

The CFA particularly eased the regulation of the Equity Model as prior to the introduction of the CFA, general financial market legislation was applied to the provision of investment services through Crowdfunding. The clarified legislation is expected to attract new entities into the Crowdfunding market.

In 2016, the size of the Equity Model Crowdfunding market increased by 184 per cent from EUR 14.5 million in 2015 to approximately EUR 41.3 million. Further, two new entities providing Equity Model Crowdfunding applied for registration as a Crowdfunding intermediary from the FIN-FSA in 2016. In addition, some Finnish banks have recently entered the Crowdfunding market by either establishing their own equity-based Crowdfunding platforms or cooperating with existing Crowdfunding platforms.

## **1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

Lending-based Crowdfunding market has grown rapidly in Finland and it currently forms the most significant sector within the Finnish Crowdfunding market. Especially newly established start-up companies and small and mid-size companies have faced difficulties in obtaining necessary funding through traditional financing methods and consequently new innovative companies have engaged in Crowdfunding activities using the Lending Model to invest in their growth. Recently, Crowdfunding has become an increasingly popular way to seek financing for real estate and construction projects, especially in relation to renewable energy projects.

In 2016, business operators collected EUR 39.9 million through lending-based Crowdfunding, an increase of 92 per cent as compared to EUR 20.8 million in 2015. Furthermore EUR 71.3 million was collected through peer to peer lending in 2016, corresponding to an increase of 106 per cent compared to EUR 34.6 million in 2015. In 2016, six entities providing lending-based Crowdfunding services applied for registration from the FIN-FSA under the CFA.

## **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

In Finland, the Donations Model is used for the sole purpose of funding social or creative projects with no financial investment or return involved. Under Finnish legislation, the Donations Model is subject to a money collection permit and may only be used for charitable purposes for the public good. The largest donations-based Crowdfunding platform in Finland mediates Crowdfunding for both domestic and international charitable projects.

In Rewards Model, investors receive a non-monetary reward, such as a product or service that has been developed and produced with the collected funds. Hence, the Rewards Model involves the characteristics of an advance sale or advance booking. The reward may also be of a symbolic value only. The Rewards Model is generally utilized by companies or private individuals that only seek minor amount of financing. Currently, there are at least two Rewards Model Crowdfunding operators in Finland focusing on Crowdfunding supporting business, culture and sports. In 2016, the funds collected through Donations Model Crowdfunding amounted to EUR 846 thousand, an increase of 32 per cent as compared to EUR 640 thousand in 2015.

## **1.4 Real Estate Crowdfunding and Renewable Crowdfunding**

Crowdfunding has recently emerged in the real estate sector, particularly in relation to financing renewable energy projects. Crowdfunding is especially utilized in early-stage projects that often fail to receive sufficient financing through traditional means due to the high risks relating to the projects. In Real Estate and Renewable Crowdfunding projects, Crowdfunding is generally used as an additional financing instrument on top of bank loans.

The first Finnish platform focusing specifically on Real Estate Crowdfunding was established in 2016, followed by a few more Real Estate operators entering the Crowdfunding

market. The Real Estate Crowdfunding platforms mainly offer and mediate lending-based Crowdfunding offering small-scale investors the opportunity to engage in real estate investments with a moderate amount of capital and a high expected interest return.

In 2016, a Finnish Crowdfunding operator successfully completed the largest real estate Crowdfunding project to date in Finland, which realizes one of the largest solar power plans in Finland and a geothermal heating system. The funds collected through the project amounted to EUR 605 thousand. The success of the project demonstrates the great potential of the Finnish Real Estate and Renewable Crowdfunding market and the willingness of private individuals to invest in unconventional projects with a higher risk and higher return expectations than traditional investments.

### 1.5 International approach

Although the Finnish Crowdfunding market mainly consists of domestic platforms and domestic companies and projects, at least one Finnish Crowdfunding platforms has recently engaged in presenting foreign companies and projects on their platform. In addition, certain foreign Crowdfunding platforms have become active in Finland.

## 2 Recent developments regarding Crowdfunding regulation in Finland

Prior to the introduction of the CFA, Finland did not have coherent regulatory regime specifically adapted for Crowdfunding and thus the regulatory treatment of a Crowdfunding platform depended on how the service of the platform and the product it offered were constructed. Particularly the Equity Model was subject to heavy regulation, as the general financial market legislation was applicable to the provision of investment services through Crowdfunding. The Lending Model, on the other hand, was missing clear legislative-level ground rules and was in some cases considered to be an unregulated activity. The objective of the CFA is to clarify the responsibilities of various authorities in the supervision of Crowdfunding, to improve investor protection and to diversify the financial markets.

The CFA lays down provisions on acquiring, offering and professionally mediating lending-based and equity-based Crowdfunding, which both seek a financial return, for the purpose of financing business activity. The CFA also applies, with certain exceptions, to credit institutions, payment institutions, fund management companies, investment firms and alternative investment fund managers (“AIFM”) that engage in mediating Crowdfunding. However, the CFA is not applicable to lending-based Crowdfunding in cases where the borrower is a consumer. Furthermore, the CFA is not applicable to cases where the recipient of Crowdfunding is a public listed company.

Through the introduction of the CFA, the earlier administratively burdensome and time-consuming operating licence process was replaced by a less expensive, simpler and faster registration process. Entering the Crowdfunding market was further facilitated by abolishing the requirement for Crowdfunding intermediaries to join the Investors’ Compensation Fund. However, the requirement to join the Investors’ Compensation Fund may be triggered in cases

where an Crowdfunding intermediary engages in certain regulated activities pursuant to the Finnish Investment Services Act (747/2012, “ISA”), such as the arranging of an emission.

Through the CFA, the minimal capital requirement for a Crowdfunding intermediary was reduced from EUR 125,000 to EUR 50,000. A Crowdfunding intermediary may also benefit from an exemption to the capital requirement where it has a guarantee, such as a professional liability insurance or a bank guarantee, which the FIN-FSA deems to be sufficient.

Investor protection was improved by, for example, extending the obligation to disclose information to situations where securities other than those referred to in the Finnish Securities Market Act (746/2012, “SMA”) are offered. The SMA and the ISA are not applicable to securities other than those referred to in the SMA, namely non-transferrable securities, and therefore such securities previously fell outside the scope of investor protection.

The CFA does not apply to cases where a business entity seeks funding from the public by independently offering its own securities by means of, for example, arranging a share issue through the business entity’s own website with no Crowdfunding intermediary involved. In such cases, the business entity shall comply with the SMA and other legislation concerning the offering of securities.

Authorised credit institutions, payment institutions, fund companies, investment service companies and alternative fund managers may engage in Crowdfunding mediation by virtue of their own operating licence provided that they comply with certain separately specified provisions of the CFA.

In addition, a Decree of the Ministry of Finance on the disclosure obligation of a Crowdfunding recipient (1045/2016) took effect in 2016, laying down provisions on the content and structure of the basic information to be provided to potential investors in connection with the offering.

Furthermore, new national regulation was provided for peer to peer Crowdfunding using the Lending Model. While the CFA does not apply to peer to peer lending among consumers, such activities now fall under the scope of consumer protection provisions and registration requirements under the Finnish Consumer Protection Act (38/1978, “CPA”).

### **3 Current Regulation of Crowdfunding in Finland**

#### **3.1 Banking or Financial Service licence requirements**

##### **3.1.1 Equity Model / Lending Model**

Pursuant to the CFA, mediating investment-based or lending-based Crowdfunding requires registration in the register of Crowdfunding intermediaries maintained by the FIN-FSA.

Under the CFA, lending-based Crowdfunding means the acquisition, offering or brokering of a loan for a financial return, where a debt relationship is created between the Crowdfunding

recipient and the customer of the Crowdfunding intermediary. Investment-based Crowdfunding means an equity or debt investment for the purpose of acquiring, offering or mediating, in respect of the Crowdfunding recipient, a share of ownership or of debt, or other stake based on a financial return, specified in a subscription agreement or investment agreement concerning a financial instrument or concerning securities other than those referred to in the SMA, or in a comparable agreement.

Under the CFA, a Crowdfunding intermediary refers to an economic operator that is not a credit institution, payment institution, fund management company, investment firm or an AIFM, and that professionally mediates lending-based or equity-based Crowdfunding. Pursuant to the CFA, the recipient of Crowdfunding shall be a legal entity other than a public listed company.

The FIN-FSA shall register the notice provider as a Crowdfunding intermediary provided that

- the notice provider has the right to engage in business in Finland;
- the notice provider is not bankrupt and, in case of a natural person, is an adult and his or her competency has not been restricted;
- the notice provider is not undergoing corporate restructuring procedures or undergoing debt adjustment for private individuals;
- the notice provider is reliable, and
- the notice provider is familiar with the operation of financial markets to the extent that is necessary in view of the nature and scope of the Crowdfunding mediation.

In order to be registered as a Crowdfunding intermediary, the economic operator must have at least EUR 50,000 in equity. Alternatively, the economic operator must have a professional liability insurance policy, bank guarantee or other corresponding collateral that fulfils the requirements set forth in the CFA and that the FIN-FSA deems to be sufficient considering the nature and scope of the economic operator's activities. If the Crowdfunding intermediary intends to receive customer assets, the intermediary is also required to be able to store and process customer assets in accordance with the CFA.

Crowdfunding intermediaries that are entered in the register maintained by the FIN-FSA may also transmit and receive securities or other orders concerning fund units of undertakings for collective investment in transferable securities as referred to in the ISA, as well as offer investment advice concerning lending-based and investment-based Crowdfunding. Such activities are subject to the provisions of the ISA.

Furthermore, pursuant to the Finnish Act on Credit Institutions (610/2014, "ACI"), an authorisation to act as a credit institution is required if repayable funds are received from the public. However, platforms using Lending Model in Finland are generally constructed in such manner that the platforms do not receive repayable funds from the public.

However, pursuant to the CPA, offering or mediating Lending Model Crowdfunding to consumers requires registration in the register of credit providers and peer loan intermediaries maintained by the Regional State Administrative Agency of South Finland. The registration requirement also applies to the provision of peer to peer Crowdfunding where the borrower is a consumer.

### **Additional regulatory requirements pursuant to the CFA**

Through the implementation of Article 3 of the Market in Financial Instruments Directive (2004/39/EC, “MiFID I”), if a registered Crowdfunding intermediary uses transferrable financial instruments, it must use an authorized investment firm or credit institution as an intermediary or an agent. However, such intermediary or agent is not required in cases where transferrable securities are offered only to certain professional investors as referred to in MiFID I.

Notwithstanding, a registered Crowdfunding intermediary may mediate assignments relating to non-transferrable securities directly to non-professional investors without using an authorized intermediary or agent.

A Crowdfunding intermediary registered under the CFA must comply with the provisions of the ISA concerning management of conflicts of interest, the acquisition of information about the customer (appropriateness test) if the investment exceeds EUR 2,000, the duty of disclosure, information to be stored on transactions and services, recording telephone calls and handling customer complaints.

In addition, the Crowdfunding intermediary must comply with the provisions on knowing the customer laid down in the Act on Detecting and Preventing Money Laundering and Terrorist Financing (503/2008).

Where the Crowdfunding intermediary offers or mediates securities referred to in the SMA, provisions of the SMA on the disclosure duty of the Crowdfunding recipient shall be applied.

#### **3.1.2 Donations or Rewards Model**

Crowdfunding platforms using the Donations or Rewards Model are not subject to financial services regulation in Finland, unless they receive repayable funds from the public. Pursuant to the ACI, an authorisation to act as a credit institution is required if repayable funds are received from the public. In practice, Donations and Rewards Model Crowdfunding platforms in Finland are constructed in such manner that the platforms do not receive repayable funds from the public.

Rewards Model Crowdfunding is subject to the CPA in cases that involve a relationship between a business operator and a consumer. On the other hand, the Finnish Sale of Goods Act (355/1987) may become applicable to Rewards Model Crowdfunding between two consumers or two businesses.

In Finland, collecting funds without compensation by appealing to the public is subject to the provisions of the Finnish Money Collection Act (255/2006 “MCA”). Therefore, Donations Model Crowdfunding falls under the scope of the MCA and requires a money collection permit granted by the police department of the State Local District, which is the domicile of the Crowdfunding recipient.

Pursuant to the MCA, a money collection permit may only be granted for the purpose of non-profit activities, i.e. for a general social, cultural or ideological purpose or other general non-governmental activities. Further, in order to receive a money collection permit, a corporation or foundation seeking Crowdfunding shall have a purely non-profit purpose and be registered in Finland. The unregistered status is due to provisions laid down on the corporation’s status in Finnish law or to the temporary nature of the corporation’s activity. The Ministry of Interior is currently investigating the need for a reform of the MCA.

## 3.2 Prospectus requirements

### 3.2.1 Equity Model / Lending Model

The SMA lays down provisions concerning the obligation to publish a prospectus in connection with offering securities to the public.

Under the SMA, a security means:

- a share in a limited-liability company or a corresponding share of another entity as well as a depositary receipt in respect of such right;
- a bond or other securitised debt as well as a depositary receipt in respect of such right;
- any other security giving the right to acquire or sell a security referred to in paragraph 1 or 2 or a security giving rise to a cash settlement determined by reference to a security, currency, interest rate or yield, commodity or other index or measure;
- a unit in a fund referred to in the Act on Common Funds (48/1999), or a unit issued by a collective investment undertaking comparable thereto.

A security shall not, however, mean a right which alone or together with other securities produces the right to possess a specific apartment, other premises or real estate or a part of real estate.

However, pursuant to the CFA, Crowdfunding recipients do not need to publish a prospectus if the securities are offered in Finland and their combined consideration over 12 months is less than EUR 5 million.

Furthermore, pursuant to the SMA, Crowdfunding recipients do not need to publish a prospectus if – inter alia – the securities are offered:

- solely to qualified investors;

- calculated per each EEA Member State, to fewer than 150 investors, other than qualified investors;
- to be acquired for a total consideration of at least EUR 100 000 per investor and per offer or in units with a denomination or consideration of at least EUR 100 000; or
- in an amount with a total consideration of less than EUR 2 500 000 calculated in the EEA over a period of 12 months.

### **Content of the prospectus**

In case the obligation to publish a prospectus arises, the prospectus shall provide an investor with sufficient information to make an informed assessment on the securities and their issuer as well as the possible guarantor. The prospectus shall contain essential and sufficient information on the assets, liabilities, financial position, profit and losses and prospects of the issuer and the possible guarantor as well as on the rights attached to the securities and other factors with a material effect on the value of the securities. The information shall be presented in a logical and easily comprehensible form.

Detailed requirements of the content of the prospectus are included in the SMA, the Decree of the Ministry of Finance (1019/2012), the Prospectus Directive (2003/71/EY) and the Prospectus Regulation (EY N:o 809/2004).

The prospectus shall be published either as a single document or as a document consisting of three parts named the registration document, the securities note and the summary.

The prospectus shall be published in Finnish or Swedish if the securities are offered to the public solely in Finland. However, the FIN-FSA may, upon application, consent to the drawing up of the prospectus in another language.

If securities are offered to the public only in an EEA Member State other than Finland, the prospectus shall be drawn up in the language accepted by the competent authority of the host EEA Member State or in English.

Any mistake or omission in the prospectus or material new information which arises or is noted after the approval of the prospectus but before the closing of the offer and which may be of material importance to the investor shall, without undue delay, be communicated to the public by publishing a correction or supplement to the prospectus.

The prospectus shall be valid until the validity of the offer relating to the securities referred to in the prospectus has closed or the securities referred to in the prospectus have been admitted to trading on a regulated market, however, at most for 12 months after its publication.

### **Document containing basic information**

Where the offer is not subject to an obligation to publish a prospectus, the Crowdfunding recipient shall publish a document containing true and sufficient information about the factors

that are likely to materially influence the company's value or its solvency prior to starting to acquire funds. Crowdfunding intermediaries shall take care to ensure that Crowdfunding recipients meet the disclosure obligations laid down in the CFA.

The Decree of the Ministry of Finance (1045/2016) lays down the requirements on the content and structure of the basic information to be provided to investors in connection with the offering.

The document containing the basic information shall be published in Finnish or Swedish and it shall be kept available to investors during the validity of the offering. The content and the presentation of the document shall be clear, easily readable and easily comprehensible. The information shall be kept up to date and any amendments or new information shall be included in the document without undue delay.

The document shall include information on – inter alia – the recipient of Crowdfunding, the offering and the financial instrument concerned, the intended use of the collected proceeds, the key risks relating to the business operations of the Crowdfunding recipient and the financial instrument concerned as well as the possible guarantor or collateral.

Both Crowdfunding recipients and Crowdfunding intermediaries shall disclose without delay information about material changes that occur in their economic conditions and about other factors that affect the fulfilment of their obligations.

### **3.2.2 Donations or Rewards Model**

No prospectus requirement is likely to apply to Donations or Rewards Model.

## **3.3 Regulation of Crowdfunding under the AIFMD regime**

Under the Finnish Act on Alternative Investment Fund Managers (162/2014 “AIFMA”), Alternative Investment Fund (“AIF”) refers to a fund or other collective investment undertaking which:

- raises capital from a number of investors;
- invests it in accordance with a defined investment policy for the benefit of those investors; and
- the undertaking does not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS).

### **3.3.1 Operating company seeking funding**

Pursuant to the AIFMA, a company operating within a certain field and seeking funding with the purpose of generating profit for its shareholders would be excluded from the definition of an AIF, as generally such company does not have a defined investment policy for the benefit of the investors. Furthermore, in such company, the investors do not typically have the possibility for daily evaluation or supervision of investment targets.

However, an operating company may also have the intention to invest into certain investment targets, which might constitute an AIF (with the exemption of holding companies, which are excluded from the scope of the AIFMA). It should also be noted that an operating company would not normally constitute an AIF in the event of the Lending, Equity or Donations or Rewards Models, in which the investor itself chooses the investment target, since activities in which investment decisions are made by the investor itself are not regarded as AIF activities.

### **3.3.2 Project company seeking funding**

The AIFMA does not apply to business in which collective investments are not conducted in the form of an AIF. In the event that collective investments are connected to the regular business of an entity and where the investors maintain significant control over the project, such joint ventures (established to finance a single project) would not be regarded as AIFs.

However, it cannot be ruled out that a project company would constitute an AIF in the event that the project company would have several investors (at least two) and there would be a collective investment policy.

#### **3.3.2.1 Equity Model**

Primarily, it would seem that in the type of Equity Model Crowdfunding where the investment decisions are made by the investors and there is no collective investment policy, the criteria for an AIF are not met.

However, equity model Crowdfunding may constitute an AIF in the event that there is an element of collective investment policy and the other qualifications of an AIF are met.

#### **3.3.2.2 Lending model**

Similarly as in respect of the equity model, it would seem that Lending Model does not constitute an AIF, where the investor retains the power to make the investment decisions. However, it is possible that such types of the lending model, in which the investment decisions are made according to a defined investment policy, the qualifications of an AIF could be met.

#### **3.3.2.3 Donation or rewards model**

The Crowdfunding platforms offering the Donations or Rewards Model are not likely to be governed by the AFMA, since the investor in this model retains the power to consider, supervise and make investment decisions and there is no element of a collective investment policy.

### **3.3.3 Crowdfunding platform**

It is possible that the Crowdfunding platform could constitute an alternative investment fund manager (“AIFM”) within the meaning of the AIFMA. Additionally, in respect of the Equity Model or Lending Model (as presented above), the question is whether the investment decisions are made on behalf the investor or by the investor. In the event that the platform

makes the investment decisions, an AIF would be formed, and the Crowdfunding platform could be seen as an AIFM.

It would also seem that since the Donations or Rewards Model do not entail an element of collective invest policy, there is no AIF would be formed and the Crowdfunding platform would not be seen as an AIFM.

### **3.3.4 Pooling vehicle**

In case the company seeking funding prefers funding by just one major investor instead of a large number of small retail investors, it is possible that the platform involves a pooling vehicle. A pooling vehicle is a company founded to concentrate a large number of investors. Such pooling vehicle is likely to be an AIF and therefore be subject to the AIFMA.

## **3.4 Regulation under the Payment Services Directive**

Crowdfunding platform operators receive funds from investors after the financing round is completed and it has been deemed successful. This may be considered money remittance in accordance with the Finnish Payment Institutions Act (297/2010, “PIA”) implementing the Payment Services Directive in Finland.

In order to provide payment services, service providers must either acquire authorisation for their business in accordance with the PIA or, in case of smaller scale activities, submit a notification of intention to provide payment services without authorisation. This requires that the service provider fulfils the requirements stipulated in the PIA applicable to the provision of payment services without authorisation.

There are good reasons to argue that transfer of funds through the platform operator’s customer deposit account does not constitute a money remittance service and that the operators would be able to rely on the exemption of commercial agents on the basis that they have authorisation to negotiate or conclude contracts on behalf of the funder and the funding seeker. However, this interpretation has not been tested and the platform providers may be required to acquire authorisation or make a notification. The legal treatment of the Lending Model from this perspective is currently not resolved satisfactorily.

To avoid the licence requirements, the Crowdfunding platform provider may also use an external authorised payment service provider to process the payments.

## **3.5 Possible additional regulations**

Other common regulations which may be applicable to a Crowdfunding platform or a Crowd-funding recipient include:

### **3.5.1 Money Collection Act**

In other parts of the world, Crowdfunding has been widely used to raise finance for charity targets and to support arts projects. In Finland, the decision of the National Police Board

restricts the use of the Donations Model: collecting money from the public with no compensation and for charity requires a money collection permit granted by the authorities.

According to the MCA, a money collection permit may be issued for a corporation or or foundation which is registered in Finland and has a purely non-profit purpose. Furthermore, according to the MCA, money can only be collected for charitable purposes. The money collection permit may not be issued for a private individual (see also section 3.1.2).

Despite the strict interpretation of the MCA, there is at least one platform in Finland offering Donations Model Crowdfunding for projects with a charitable purpose. The platform requires that a money collection permit is acquired before the project can be entered in the platform.

### 3.5.2 Consumer Protection Act and Act on Registration of Certain Creditors

The CPA regulates domestic and distance selling to consumers as well as the distance selling of financial services and instruments. No conduct that is inappropriate or otherwise unfair from the point of view of consumers shall be allowed in marketing. In addition, false or mis-leading information shall not be conveyed in marketing. It is also forbidden to not provide such information in marketing or consumer relations that is relevant taking into account the context and which the consumer needs for a proper purchase decision.

The CPA also regulates the offering of consumer credit and sets out several obligations with respect to the offering of credit to consumers. These obligations include, for example, the duty of disclosure of a company offering consumer credit with regard to interest rate and other costs related to the credit, amount of credit and credit limit, duration of the credit agreement, cash price of the commodity, the aggregate amount of the credit, credit costs and the number of instalments. Additionally, obligations include, e.g. the duty to provide the consumers with sufficient information on the credit before entering into the credit agreement, the obligation of the company offering the credit to act in accordance with principle of responsibility, the duty to assess the creditworthiness of the consumer before entering into the credit agreement, the obligation to verify the identity of the consumer applying for the credit and the duty to inform the consumer if the creditor's rights under the credit agreement or the agreement itself will be assigned to a third party.

In addition, a Crowdfunding platform provider offering consumer credit has an obligation to register in the register for creditors pursuant to Act on Registration of Certain Creditors (853/2016). However, consumer credits fall outside of the scope of the CFA.

### 3.5.3 Other legislation

Furthermore, Crowdfunding activities may fall under the scope of – inter alia – the following Finnish legislation:

- the ACI
- the ISA

- the SMA
- the Finnish Act on Detecting and Preventing Money Laundering and Terrorist Financing
- the Finnish Personal Data Act (523/1999)

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

Finnish financial regulation may become applicable where a Crowdfunding platform operates in Finland and/or the company or project seeks funding from Finnish investors. The applicable law depends on how the service of the platform and the product it offers are constructed and whether the platform wishes to operate on a cross border basis or by establishing a branch in Finland.

### 4.2 Inbound

Finnish legislation may apply to the

- Crowdfunding platform (essentially licence, information and compliance obligations); and / or the
- company / project seeking financing through Crowdfunding (essentially prospectus and information obligations).

#### 4.2.1 Foreign Crowdfunding platform addresses investors in Finland

##### 4.2.1.1 Crowdfunding platform

###### (1) Licence obligations

The applicable legislation and procedure depends on whether the Crowdfunding platform has a passportable MiFID licence in another EU member state.

###### (a) Passporting procedure

If an Equity Model platform qualifies as an investment services provider as defined in the ISA, the platform may enter the Finnish Crowdfunding market through passporting procedure. A platform holding a MiFID licence can passport its licence into Finland by requesting the competent authority of the home Member State to inform the FSA of the platform's intention to operate in Finland as well as a programme of the investment services it intends to perform and whether it intends to use tied agents in Finland. The competent authority of the home Member State shall forward the information to the FIN-FSA and the platform may then start to provide the investment services concerned.

In case of passporting on a cross border basis, the laws of the home Member State will be applied on the basis of home country control principle by the Member State where the platform has obtained its MiFID licence.

If a platform receiving repayable funds from the public qualifies as a credit institution under the laws of the home Member State, it may access the Finnish Crowdfunding market by either passporting its licence and operating on a cross border basis or establishing a branch in Finland by notifying the supervisory authority of its home Member State. Even when the platform operates on a cross border basis, the platform must comply with all the requirements of ACI and other relevant Finnish laws.

Alternatively, in case of establishing a branch in Finland, the competent authority of the home Member State must notify the FIN-FSA of the establishment of the branch. In that case the branch must comply with relevant Finnish rules and regulations such as Chapter 10 of the ISA as well as the local rules and regulations of the home Member State. The FIN-FSA will supervise the branch on the basis of Finnish rules and regulations while the competent authority of the home Member State will have supervision over the platform. The FIN-FSA shall determine the time when the branch may commence its business.

Where a foreign Crowdfunding platform mediates Lending Model or Equity Model Crowdfunding in Finland through a passporting procedure, certain provisions of the CFA become applicable.

#### **(b) Registration as a Crowdfunding intermediary**

An Equity Model or Lending Model Crowdfunding platform from another Member State may be registered in the register of Crowdfunding intermediaries maintained by the FIN-FSA provided that the conditions set forth in the CFA are met (see section 3.1.1). However, the obligation to register in accordance with the CFA does not apply to economic operators located in another state of the European Economic Area that temporarily mediate Crowdfunding in Finland. Therefore, Crowdfunding platforms from another Member State may mediate Crowdfunding in Finland with no licence requirement on a temporary basis.

Under the CFA, the obligation to register as a Crowdfunding intermediary does not apply to economic operators located in another state of the European Economic Area that temporarily mediate Crowdfunding in Finland.

#### **(c) Application for authorisation**

If a foreign Crowdfunding platform does not have a MiFID licence and its intended activities do not fall under the scope of the CFA, the foreign Crowdfunding platform may be required to apply for an authorisation in order to offer financial services in Finland.

For example, if the platform qualifies as a grantor of consumer credits that falls within the scope of the CPA, the platform must be registered in a list maintained by the Regional State Administrative Agency of Southern Finland. The registration requirement also applies to the provision of peer to peer Crowdfunding where the borrower is a consumer.

### **(2) Other financial regulation**

A Crowdfunding intermediary registered under the CFA must comply with the provisions of the ISA concerning management of conflicts of interest, the acquisition of information about the customer (appropriateness test) if the investment exceeds EUR 2,000, the duty of disclosure, information to be stored on transactions and services, recording telephone calls and handling customer complaints. In addition, the Crowdfunding intermediary must comply with the provisions on knowing the customer laid down in the Act on Detecting and Preventing Money Laundering and Terrorist Financing.

According to the MCA, a money collection permit may be issued for an association or foundation which is registered in Finland and if the sole purpose of the association is to work for public good. Furthermore, according to the MCA, money can be collected only for charitable purposes. Thus, a foreign platform interested in collecting funds solely for charitable purposes with no compensation in Finland must first establish a branch in Finland and apply for a money collection permit.

#### **4.2.1.2 Company / project**

Companies / projects seeking Crowdfunding in Finland fall under the scope of Finnish prospectus requirements. However, as described under section 3.2.1, Crowdfunding recipients may benefit from an exemption from the obligation to publish a prospectus in connection with the public offering of securities in cases where securities are offered in Finland and their combined consideration over 12 months is less than EUR 5 million.

Nevertheless, the Crowdfunding recipient is required to publish a document containing true and sufficient information about the factors that are likely to materially influence the Crowd-funding recipient's value or its solvency. The document shall be made available to investors prior to starting to acquire funds (for a more detailed description, see section 3.2.1).

#### **4.2.2 Foreign Crowdfunding platform addresses Finnish companies / projects**

Finnish legislation is not likely to apply for a foreign Crowdfunding platform presenting Finnish companies to foreign investors. However, Finnish legislation may apply to a Finnish company / project intending to be funded through a foreign Crowdfunding platform in Finland, essentially the provisions on prospectus and disclosure obligations.

##### **4.2.2.1 Crowdfunding platform**

In case the foreign Crowdfunding platform does not become active in Finland or approach Finnish investors, Finnish legislation is not likely to apply to its operations and the Crowd-funding platform will not be required to apply for an authorisation or registration in Finland.

The regulatory requirements concerning foreign Crowdfunding platforms becoming active in Finland are described above (see 4.2.1.1).

##### **4.2.2.2 Company / project**

###### **(1) Finnish prospectus requirement**

A Crowdfunding recipient offering securities as referred to in the SMA to the public in Finland may fall under the scope of the obligation to publish a prospectus (see section 3.2).

As described under section 3.2.1, Crowdfunding recipients may benefit from an exemption from the obligation to publish a prospectus in connection with the public offering of securities in cases where securities are offered in Finland through a Crowdfunding intermediary registered under the CFA and their combined consideration over 12 months is less than EUR 5 million.

Nevertheless, the Crowdfunding recipient is required to publish a document containing true and sufficient information about the factors that are likely to materially influence the Crowd-funding recipient's value or its solvency. The document shall be made available to investors prior to starting to acquire funds (for a more detailed description, see section 3.2.1).

### 4.3 Outbound

In this situation a Finnish Crowdfunding platform enters the Crowdfunding market of another Member State and presents foreign or domestic companies / projects on its platform.

Under this section, the following different alternatives are considered:

- Finnish Crowdfunding platform addresses foreign (EU) investors or
- Finnish Crowdfunding platform addresses companies / projects in another EU country

#### 4.3.1 Finnish Crowdfunding platform addresses foreign (EU) investors

##### 4.3.1.1 Crowdfunding platforms

A Finnish authorised credit institution, payment institution, fund company or investment service company that operates as a Crowdfunding platform may become active based on its licence obtained from the FIN-FSA without having to apply for another licence in the host Member State by following a passporting procedure in accordance with MiFID. Alternatively, the platform may establish a branch in another Member State.

In case of passporting, the Crowdfunding platform shall notify the FIN-FSA of the Member State in which it intends to operate, a programme of operations it intends to perform and whether it intends to use tied agents in the Member State concerned. The FIN-FSA shall forward the information to the competent authorities of the Member State in which the platform wishes to operate and the platform may then start to provide the investment services concerned. However, additional local rules may apply and it is recommended that the platform obtains local law advice before becoming active in another Member State.

However, Crowdfunding platforms using the Rewards Model and Donations Model fall out-side the scope of the MiFID passporting procedure and therefore such platforms may require relevant local licences before they can expand their business to another Member State.

A Finnish Crowdfunding platform registered as a Crowdfunding intermediary under the CFA may mediate Crowdfunding using the Equity Model and Lending Model to another state of the European Economic Area provided that such activities are not prohibited or limited in the state concerned. However, the scope of activities the Crowdfunding platform may engage in depend on the legislation of the state concerned. Thus, when a Finnish Crowdfunding platform intends to operate in other EU Member States, it is recommendable to apply for an investment service company operating licence, as this will facilitate the access to European markets.

#### **4.3.1.2 Company / project**

Under the SMA, the obligation to publish a Finnish prospectus only applies in cases where securities are offered in Finland. Therefore, the Finnish regulations concerning the obligation to publish a prospectus do not apply in cases where a Finnish company / project offers securities by means of Crowdfunding to another Member State. Whether the Finnish company / project is required to publish a prospectus in connection with offering securities in another Member State depends on the legislation of the Member State concerned.

### **4.3.2 Finnish Crowdfunding platform addresses companies / projects in another EU country**

#### **4.3.2.1 Crowdfunding platform**

In case a Finnish Crowdfunding platform approaches Finnish investors and presents foreign companies or projects on its platform, the Crowdfunding platform must either register as a Crowdfunding intermediary pursuant to the CFA or apply for an investment service company operating licence or another applicable authorisation or registration as further described under section 3.1. The Crowdfunding platform will be subject to Finnish Crowdfunding regulations as described under section 3.

#### **4.3.2.2 Company / project**

In case a foreign company / project offers securities as referred to in the SMA through a Finnish Crowdfunding platform in Finland, the foreign company / project may be subject to the obligation to publish a prospectus, unless the conditions of the exemptions under the SMA or the CFA are met (see section 3.2).

Notwithstanding, the foreign company / project may be subject to prospectus requirements pursuant to its home Member State.

## **4.4 Impact of EU regulation**

### **4.4.1 Prospectus rule / regimes**

The European Prospectus Directive has been implemented in Finland through the SMA. The SMA covers the offering of securities as defined above under section 3.2.1.

Through the introduction of the CFA, Crowdfunding recipients benefit from an exemption from the obligation to publish a prospectus in cases where securities are offered in Finland and their combined consideration over 12 months is less than EUR 5 million, while the general national threshold for the obligation to publish a prospectus is 2.5 million.

#### 4.4.2 AIFM-Directive

The AIFM-Directive and the implementing AIFMA mainly affect equity-based Crowdfunding in the event that a project company would have several investors (at least two) and the company would have a collective investment policy. However, in the event that collective investments are connected to the regular business of the entity and the investors maintain significant control over the project, such joint ventures would not be regarded as AIFs.

#### 4.4.3 MiFID / MiFID II

The CFA implements Article 3 of MiFID I by facilitating the mediation of Crowdfunding with lighter administrative requirements in respect of investment-based Crowdfunding instead of requiring an operating licence procedure. Through the implementation of Article 3 of MiFID I, a registered Crowdfunding intermediary that uses transferrable financial instruments is required to use an authorized financial market operator as an intermediary or an agent, unless transferrable securities are offered only to certain professional investors as referred to in MiFID I.

Moreover, MiFID I and MiFID II may be applied in relation to Crowdfunding where a Finnish Crowdfunding platform intends operate in another EU Member State by applying for a MiFID licence (see section 4.3.1.1).

#### 4.4.4 PSD / PSD II

The Payment Services Directive was implemented through the PIA and Payment Services Act (290/2010). The Payment Services Directive II entered into force in 2016 and shall be implemented by January 2018.

In general, any transfer of funds through the operator of a Crowdfunding platform is regarded as money remittance services within the meaning of the PIA and subject to authorisation requirement in accordance with the PIA. Small-scale activities may benefit from an exemption from the authorisation requirement and instead submit a notification of the intention to provide payment services without authorisation. To avoid the licence requirements, the Crowdfunding platform provider may also use an external authorised payment service provider to process the payments.

### 4.5 Summary

The CFA is a modern law that takes into account the characteristics and international development of Crowdfunding activities within the regulatory framework laid down by the EU. The CFA is regarded as an example of Crowdfunding regulation that aims to support

Crowdfunding activities instead of restricting them. Regulatory obstacles in relation to cross-border Crowdfunding activities primarily arise from EU legislation.

The following regulatory barriers may be identified in relation to cross-border Crowdfunding in Finland.

- Finnish Crowdfunding platforms registered as Crowdfunding intermediaries under the CFA cannot become active in another EU Member State through a passporting procedure. Whether a Finnish Crowdfunding intermediary may operate in another EU Member State based on its registration depends on the regulation of the EU Member State concerned.
- Foreign companies may be subject to different or even duplicate prospectus requirements in case they seek Crowdfunding from both Finland and their home EU Member State.
- Collecting funds from the public with no compensation falls under the scope of the MCA. Therefore, a foreign platform interested in collecting funds solely for charitable purposes with no compensation in Finland must first establish a branch in Finland and apply for a money collection permit. The Ministry of Interior is currently investigating the need for a reform of the MCA.

## **5 Lessons learned from the Finnish regulation for a possibly harmonised European Crowdfunding regulation**

### **5.1 Role models (“dos”)**

The CFA significantly lightens the regulation and administrative procedures concerning mediation and acquisition of Crowdfunding in Finland and therefore facilitates growth companies’ access and supports the growth of the Finnish Crowdfunding market. Further, the CFA finally sets ground rules for the previously unregulated forms of lending-based Crowdfunding and therefore enhances investor protection.

For a possible harmonised European Market, the following aspects can serve as a role model:

- establishing a coherent regulatory regime specifically for Crowdfunding;
- replacing burdensome and time-consuming operating licence processes with a lighter registration process;
- extending the scope of exemptions from the obligation to publish a prospectus.

### **5.2 Aspects that should be avoided (“don’ts”)**

However, the following aspect should not be inherited:

requiring money collection permit for the collection of funds for charitable purposes with no compensation and restricting the scope of application to operators registered in Finland.

## 6 Conclusion

Although the Finnish Crowdfunding market is currently small in relation to those of other Member States, the Finnish Crowdfunding market has grown significantly during recent years and the introduction of the CFA is expected to contribute to further growth of the market.

While the CFA clarifies and lightens the Crowdfunding regulation in Finland, the CFA does not apply to all models of Crowdfunding. Therefore, a foreign Crowdfunding platform considering becoming active in Finland should make itself aware of its legal definition under Finnish law as the construction of the platform and the services it offers have an effect on the prerequisites for becoming active in Finland as well as the regulatory treatment of the operation of the platform.

## 7 Summary – Crowdfunding Regulation

| Country   | Finland   |
|---|---|
| Summary   |   |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• The Finnish Crowdfunding Act (“CFA”) took effect in 2016, laying down provisions on acquiring, offering and professionally mediating Crowdfunding using the Lending Model and Equity Model</li> <li>• A Decree of the Ministry of Finance on the disclosure obligation of a Crowdfunding recipient took effect in 2016, laying down provisions on the content and structure of the basic information to be provided to potential investors in connection with the offering</li> <li>• New national regulation was provided for peer to peer Crowdfunding using the Lending Model and such activities now fall under the scope of consumer protection provisions and registration requirements under the Finnish Consumer Protection Act (“CPA”)</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |   |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Pursuant to the CFA, mediating investment-based or lending-based Crowdfunding requires registration in the register of Crowdfunding intermediaries maintained by the FIN-FSA</li> <li>• Investment-based Crowdfunding means an equity or debt investment for the purpose of acquiring, offering or mediating, in respect of the Crowdfunding recipient, a share of ownership or of debt, or other stake based on a financial return, specified in a subscription agreement or investment agreement concerning a financial instrument or concerning securities other than those referred to in the SMA, or in a comparable agreement</li> <li>• Pursuant to the Finnish Act on Credit Institutions (“ACT”), an authorisation to act as a credit institution is required if repayable funds are received from the public</li> <li>• Pursuant to the CPA, offering or mediating Lending Model Crowdfunding to consumers requires registration in the register of credit providers and peer loan intermediaries maintained by the Regional State Administrative Agency of South Finland</li> <li>• Collecting funds without compensation by appealing to the public is subject to the provisions of the Finnish Money Collection Act (“MCA”) and a money collection permit granted by authorities</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• A Crowdfunding recipient offering securities as referred to in the SMA to the public in may fall under the scope of the obligation to publish a prospectus</li> <li>• Pursuant to the CFA, Crowdfunding recipients do not need to publish a prospectus if the securities are offered in Finland and their combined consideration over 12 months is less than EUR 5 million</li> </ul>  |
| <b>AIFMD-regulation</b>                               | The AIFM-Directive and the implementing Finnish Act on Alternative Investment Fund Managers (“AIFMA”) mainly affect equity-based Crowdfunding in the event that a project company would have several  |

|                                      |   |
|--------------------------------------|---|
|                                      | investors (at least two) and the company would have a collective investment policy  |
| <b>Payment service regulation</b>    | Receiving funds from investors may be considered money remittance in accordance with the Finnish Payment Institutions Act (“PIA”) implementing the Payment Services Directive in Finland  |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• The Act on Registration of Certain Creditors</li> <li>• The Securities Market Act</li> <li>• The Investment Services Act</li> <li>• The Act on Detecting and Preventing Money Laundering and Terrorist Financing</li> </ul>  |
| <b>Regulatory barriers</b>           |   |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addresses Finnish investors</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• If an Equity Model platform qualifies as an investment services provider as de-fined in the ISA, the platform may enter the Finnish Crowdfunding market through passporting procedure</li> <li>• If a platform receiving repayable funds from the public qualifies as a credit institution under the laws of the home Member State, it may access the Finnish Crowdfunding market by either passporting its licence and operating on a cross border basis or establishing a branch in Finland by notifying the supervisory authority of its home Member State</li> <li>• Where a foreign Crowdfunding platform mediates Lending Model or Equity Model Crowdfunding in Finland through a passporting procedure, certain provisions of the CFA become applicable</li> <li>• An Equity Model or Lending Model Crowdfunding platform from another Member State may be registered in the register of Crowdfunding intermediaries maintained by the FIN-FSA</li> <li>• Under the CFA, the obligation to register as a Crowdfunding intermediary does not apply to economic operators located in another state of the European Economic Area that temporarily mediate Crowdfunding in Finland</li> <li>• If a foreign Crowdfunding platform does not have a MiFID licence and its intended activities do not fall under the scope of the CFA, the foreign Crowdfunding platform may be required to apply for an authorisation in order to offer financial services in Finland</li> <li>• A foreign platform using the Donations Model must first establish a branch in Finland and apply for a money collection permit</li> </ul> <p><i>Company or project</i></p> <ul style="list-style-type: none"> <li>• Companies / projects seeking Crowdfunding in Finland fall under the scope of Finnish prospectus requirements</li> <li>• Crowdfunding recipients may benefit from an exemption from the obligation to publish a prospectus in connection with the public offering of securities in cases where securities are offered in Finland through a registered Crowdfunding intermediary</li> </ul> |

|                        |   |
|------------------------|---|
|                        | <p><b>Foreign Crowdfunding platform addresses Finnish companies / projects</b></p> <p><i>Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• In case the foreign Crowdfunding platform does not become active in Finland or approach Finnish investors, Finnish legislation is not likely to apply to its operations and the Crowdfunding platform will not be required to apply for an authorisation or registration in Finland</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>• A Crowdfunding recipient offering securities as referred to in the SMA to the public in Finland may fall under the scope of the obligation to publish a prospectus</li> <li>• Crowdfunding recipients may benefit from an exemption from the obligation to publish a prospectus in connection with the public offering of securities in cases where securities are offered in Finland</li> <li>• Nevertheless, the Crowdfunding recipient is required to publish a document containing true and sufficient information about the factors that are likely to materially influence the Crowdfunding recipient's value or its solvency</li> </ul>  |
| <p><b>Outbound</b></p> | <p><b>Finnish Crowdfunding platform addresses foreign (EU) investors</b></p> <p><i>Crowdfunding platforms</i></p> <ul style="list-style-type: none"> <li>• A Finnish authorised credit institution, payment institution, fund company or investment service company that operates as a Crowdfunding platform may become active based on its licence obtained from the FIN-FSA without having to apply for another licence in the host Member State by following a passporting procedure in accordance with MiFID</li> <li>• Alternatively, the platform may establish a branch in another Member State</li> <li>• However, Crowdfunding platforms using the Rewards Model and Donations Model fall outside the scope of the MiFID passporting procedure and therefore such platforms may require relevant local licences before they can expand their business to another Member State</li> <li>• A Finnish Crowdfunding platform registered as a Crowdfunding intermediary under the CFA may mediate Crowdfunding using the Equity Model and Lending Model to another state of the European Economic Area provided that such activities are not prohibited or limited in the state concerned</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>• Finnish regulations concerning the obligation to publish a national prospectus do not apply in cases where a Finnish company / project offers securities by means of Crowdfunding to another Member State</li> </ul> <p><b>Finnish Crowdfunding platform addresses companies / projects in another EU country</b></p> <p><i>Crowdfunding platform</i></p> |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>• In case a Finnish Crowdfunding platform approaches Finnish investors and presents foreign companies or projects on its platform, the Crowdfunding platform must either register as a Crowdfunding intermediary pursuant to the CFA or apply for an investment service company operating licence or another applicable authorisation or registration</li> <li>• The Crowdfunding platform will be subject to Finnish Crowdfunding regulations</li> </ul> <p><i>Company / project</i></p> <ul style="list-style-type: none"> <li>• In case a foreign company / project offers securities as referred to in the SMA through a Finnish Crowdfunding platform in Finland, the foreign company / project may be subject to the obligation to publish a prospectus</li> <li>• The SMA and the CFA contain exemptions from the obligation to publish a prospectus</li> <li>• Notwithstanding, the foreign company / project may be subject to prospectus requirements pursuant to its home Member State.</li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | The European Prospectus Directive has been implemented in Finland through the SMA  |
| <b>AIFM-Directive</b>          | The AIFM Directive and the implementing AIFMA mainly affect equity-based Crowdfunding in the event that a project company would have several investors (at least two) and the company would have a collective investment policy  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• The CFA implements Article 3 of MiFID I by facilitating the mediation of Crowd-funding with lighter administrative requirements in respect of investment-based Crowdfunding instead of requiring an operating licence procedure</li> <li>• MiFID I and MiFID II may be applied in relation to Crowdfunding where a Finnish Crowdfunding platform intends operate in another EU Member State by applying for a MiFID licence</li> </ul>  |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• The Payment Services Directive was implemented through the PIA and Payment Services Act</li> <li>• In general, any transfer of funds through the operator of a Crowdfunding platform is regarded as money remittance services within the meaning of the PIA and subject to authorisation requirement in accordance with the PIA</li> <li>• Small-scale activities may benefit from an exemption from the authorisation requirement</li> </ul>   |

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# France

## 1 Recent developments in the market of Crowdfunding in France

Since 2014, France has a dedicated Crowdfunding regulation which had a positive impact on the market, although it has set some significant limitations, aiming firstly to protect investors.

Two specific statuses have been created for the Crowdfunding platforms, i.e. **CIP** – *conseil en investissement participatif* (Crowdfunding investment advisor) and **IFP** – *intermédiaire en financement participatif* (Crowdfunding investment intermediary), which are optional but clarify the prior regulatory uncertainties on platform activities. Derogations to public offering rules and banking monopoly have also put an end to the exposure borne by the issuers, and by the lenders (both statuses are further described below).

As a result, IFPs will offer straight loans matching the traditional “Lending Model” as well as donations with or without rewards, while the CIP platforms may offer equity (shares) or other (new) debt instruments similar to securities under French law (bonds) or treated as such by French Crowdfunding regulations (Minibons), thus carrying offerings matching a combination of the traditional “Lending” and “Equity Models”.

In addition to IFPs and CIPs, traditional market actors, i.e. **PSI** – *prestataires de services d’investissement* (investment service providers, under MiFID) can offer the same instruments as CIPs to the crowd on dedicated platforms.

In 2016, the French Crowdfunding market has continued its steady growth, with positive additional regulatory changes, notably with the increase of the amount of funds collected on the platforms and the authorisation for project holders to offer new instruments to the crowd.

### 1.1 Recent market evolutions for lending, equity and donations

At the end of 2015, the overall French Crowdfunding market was composed of approx. 80 active platforms. Meanwhile, in 2016 the number of French registered Crowdfunding platforms stabilized, after two years of continuous increase, going down from 61 CIP platforms mid-2016 to 58, and stabilizing to 31 IFP platforms. The French market is more and more structured and institutional banks are now interested in entering into partnerships with Crowdfunding platforms or even in registering their own platforms.

Based on a report of the French Crowdfunding Association “*Financement Participatif France*” (a non-profit association regrouping a large number of French prominent platforms) dated February 2017, there were more than 2.6 million crowdfunders in France in 2016 (against 2.3 million in 2015).

The French Crowdfunding activities doubled between 2015 and 2016. Collected funds have increased by 40% during this same period. The overall investments for 2015 represented about EUR 297 million and reached EUR 629m in 2016. By way of comparison, funds raised through

Crowdfunding platforms reached approx. EUR 78m in 2013, approx. EUR 152m in 2014, and approx. EUR 133m during the first semester of 2015. Loans then represented the largest part in such market (about EUR 80m raised in 2014).

Until 2016, most projects crowdfunded in France achieved financing through the Lending Model, mostly with interest bearing loans, as follows:

- EUR 96.6m were collected for projects financed by way of loans i.e. straight loans with or without interests, straight bonds, and *bons de caisse* / Minibons increasing by 46% in comparison to 2015 (with c. EUR 76m for the first semester of 2015, with fewer debt instruments);
- EUR 68.2m were collected through equity investment increasing by 36% in comparison to 2015 (with approx. EUR 35m for the first semester of 2015); and
- EUR 68.6m were collected for projects financed by way of donations or against a reward, increasing by more than 37% against 2015. As is the case in other jurisdictions, most of the projects that offer retribution for a donation (reward) will present the value of the reward, which can be non-monetary, according to a table identifying the details of the rewards to be attributed for a set amount of donation, generally operating under the principle “the bigger the donation, the bigger the reward”.

## 1.2 Focus on Real Estate Crowdfunding / Renewables Crowdfunding

### 1.2.1 Real Estate Crowdfunding

French real estate Crowdfunding still represents less than 0.1% of real estate lending, but it is already a significant 25% of the French Crowdfunding market at large and its fastest growing segment.

On this sector, two thirds of the EUR 40m collected in 2016 for real estate projects, were raised by three market leaders, *Anaxago Immobilier* and *WiSeed Immobilier*, the real estate branches of equity Crowdfunding platforms *Anaxago* and *WiSeed*, and specialized real estate pioneer *Lymo*.

The main characteristics of the French real estate Crowdfunding are as follows:

- Property development (80% of platforms) leads ahead of fix-and-flip (60%) and buy-to-let (30%). Development funds are typically used to purchase the land which the developer will then use as collateral to borrow the funds necessary for building construction from traditional banks.
- Residential properties (96%) dominates, ahead of commercial real estate (35%) and social housing (23%)
- Special Purpose Vehicles (92%) in form of simplified joint-stock holding companies (SAS) sit between investors and the dedicated building company (SSCV), set to

hold the real estate project, in order to limit the liability of investors to their contributions.

- Bonds (69%) are the preferred financial instruments ahead of shares (42%) or commercial papers (6%). The maturity of real estate development bonds typically ranges from 12 to 36 months.
- Gross returns range from 3% to 20% for these projects, which is substantially higher for property development than for buy-to-let.
- Net returns are much lower as, in addition to the unknown default rate, fees and commission can reach between 4% and 8%.

Schemes for Crowdfunding investment in real estate have a complex structuring, notably since they use unlimited liability companies (such as French “*société civile immobilière*” or SCI) which may be directly held by investors or held through a limited liability holding company (such as an SAS).

Thus, the *Autorité des Marchés Financiers* (“AMF”), the French financial markets regulator, has issued some warnings in 2015 in this respect and pushed for full transparency towards the investors on the investment scheme and associated risks. In addition, discussions have arisen as to whether or not such structuring would qualify as alternative investment funds under the Alternative Investment Funds Management Directive (“AIFMD” - see below).

### 1.2.2 Renewables Crowdfunding

There is an emerging legal trend in France to facilitate Crowdfunding for renewable energy projects, pushed by the French government since 2014.

French Crowdfunding platforms related to projects dealing with renewable energies and/or sustainable development (“RES projects”) are mostly debt-based projects, which loan offering is made either in the form of bonds (obligations) or straight loans. Such loans are governed by two separate set of rules under the new French regulation, as bonds (securities) are offered by CIPs when straight loans are offered by IFPs, due to regulatory constraints (below).

French RES projects funded by Crowdfunding are mostly projects related to wind or solar farm, although the French government has adopted measures to incentive funding of other green energy sources. The usual mechanism, under a debt-based funding pattern, is that once a platform has selected a project holder and completed its subsequent due diligence, the project holder already collected the funds through a bank loan. Then, the amount raised through the Crowdfunding platform will pay off a proportional part of the bank loan. Such mechanism is notably used by *Lendosphere* for funding its selected projects.

The average interest rate for investors in RES Projects in France usually ranges from 5% to 8%.

Since 2012, approx. EUR 1.4 million have been raised for financing RES projects, which represents less than 4% of the aggregate amount raised by Crowdfunding, all sectors included.

It is thus an emerging market for Crowdfunding in France, which is expected to considerably grow in the upcoming years.

On 22 July 2015, the French Parliament adopted the Energy Transition for Green Growth Act (the “Act”), which provides for several goals for the promotion of RES projects in France, notably:

- RES projects shall constitute 23% of the final consumption of energy in 2020 and 32% in 2030;
- RES projects shall constitute 40% of electricity production in 2030;
- electricity produced by nuclear facilities shall be reduced to 50% in 2025; and
- an energy shall be adopted programme for 2016-2023, which will define the development and investment guidelines for French RES projects (the details of which have been laid-out by Decree on 27 October 2016).

This new regulation aims to implement and favour the global integration of RES projects into the domestic electricity market in a progressive way.

The Act also provides for specific provisions on Crowdfunding for renewable energy production companies, and modifies the French Energy Code as well as the Code regulating the Public local authorities (*Code des collectivités territoriales*) in quite a substantial way.

Thus, it authorizes the creation of commercial companies limited by shares (*sociétés par actions* governed by general company rules) or, cooperating companies governed by the Code regulating the Public local authorities, where local authorities and individuals will co-invest in / co-finance renewable energy production installations. The Act expressly provides that such co-investment / co-funding can be proposed to the individuals, either directly or, through CIP, PSI or IFP platforms.<sup>1</sup>

### 1.3 International approach

Foreign platforms which offer Crowdfunding under the donation / reward model have been established for a few years in French (notably US and UK ones). However, when it comes to the offering of loans and securities or similar instruments, foreign platforms need to register as CIP, PSI (meaning they need to be registered in France) or IFPs, thus making the French market less attractive to foreign platforms.

## 2 Recent developments regarding Crowdfunding regulation in France

As indicated above, since October 2014, two different specific statuses have been implemented for Crowdfunding platforms (IFPs and CIPs), while PSIs (qualifying under MiFID) may also offer instruments to the crowd on dedicated platforms.

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<sup>1</sup> Article L. 314-28, III of the French energy Code.

Since 1 October 2016, new instruments may be offered to trade by PSI and CIP platforms, i.e. preferred shares with voting rights attached (versus ordinary shares only previously), convertible bonds (versus straight bonds only previously), and the Minibon, a debt instrument inspired from the French *bon de caisse*, previously used by certain Crowdfunding platforms outside the scope of the former Crowdfunding regulations and that of *bons de caisse*; a specific new banking monopoly having been set for lenders in the framework of Minibons issuance.

In addition, the maximum amounts to be offered / lent per project on Crowdfunding platforms have been increased per the terms of Decree no. 2016-1453 dated 28 October 2016.

### 3 Current Regulation of Crowdfunding in France

The French legal framework for Crowdfunding activities applicable as from 1 October 2014 was adopted on 30 May 2014 and detailed in Ordinance no. 2014-559 as later detailed on specific provisions by Decree no. 2014-1053 dated 16 September 2014.

As indicated above, the French regulation has been revised on 1 October 2016 with the entry into force of the Law no. 2015-990 dated 6 August 2015, known as “Loi Macron” and detailed in Ordinance no. 2016-520 dated 28 April 2016 and Decree no. 2016-1453 dated 28 October 2016.

Further to the adoption of this new set of rules, the AMF’s *Règlement Général* (“**AMF Regulation**”) has been modified by Ministerial Order dated 12 October 2016.

The French regulation provides exception to securities public offering rules and banking monopoly, and creates two specific regulatory statuses, i.e., IFPs and CIPs, both subject to anti-money laundering and anti-terrorists regulations.

#### 3.1 CIP and IFP registration requirements under the Ordinance on Crowdfunding activities dated 30 May 2014, Decree dated 16 September 2014, Ordinance dated 28 April 2016 and Decree dated 28 October 2016

The CIP and IFP statuses are optional since the Crowdfunding platform operators can also register or be licensed, if they meet the relevant statutory criteria, as PSI or credit institutions (implying far more costs and constraints). The election of a status by the relevant operators will depend on the range of financial and advisory services they are willing to offer to their clients/the investors.

##### 3.1.1 CIP status (offering of bonds, shares and Minibons)

###### 3.1.1.1 Regulatory status

As indicated above, CIPs are those platform operators which provide investment services in securities (ordinary and preferred shares), and other debt instruments (straight bonds,

convertible bonds and Minibons) on an internet website complying with specifications set forth by the AMF Regulation.<sup>2</sup>

Minibons are interest bearing notes, or *bons de caisse*, registered, non-negotiable securities, that provide a trader's undertaking to effect payment on a specific maturity date in return for a loan; being specified that only companies having approved at least three annual financial statement and having a fully paid-up share capital may issue Minibons.<sup>3</sup> Their repayment date must be set within five years maximum as from their issuance and repayment instalments must occur at least once per quarter.

A specific exception to the French banking monopoly regulation has been implemented for Minibons subscribers under French law.<sup>4</sup> Such exception applies to individuals acting for non-professional and non-commercial purposes and to companies subscribing such Minibons as an ancillary activity to their main activity.

In respect of Minibons, the French Government has authorized the use of distributed ledger technology for the issuance of Minibons and recording of trades. The statute defines blockchain technology as a “*shared electronic recording system allowing authentication*”. It states that the issuance of Minibons can be recorded on a blockchain “*under conditions fixed by a decree in Council of State*”.<sup>5</sup> However, such decree has not been published to date so that the blockchain technology cannot yet be used to record Minibons' trade.

In addition to the above, CIPs may provide a limited number of ancillary services (e.g., handling subscription applications). However, they cannot receive funds from investors (except for their remuneration) and are not authorized to receive securities from issuing companies. CIPs cannot have other activities except those of IFP (see below), in which case, although they will be IFPs, they shall not provide payment services.

CIPs shall be legal entities established in France. Although no license is required to operate their activities, CIPs are placed under the supervision of the AMF and are subject to registration obligations. Thus, CIPs shall (i) be registered with the ORIAS (register for intermediaries in banking operations and payment services), (ii) present certain moral guarantees, (iii) be members of an AMF accredited association<sup>6</sup> which controls their activities (if the association is not accredited specific control procedures are implemented) in compliance with the AMF Regulation and (iv) subscribe specific insurance policies (minimum guaranteed amount shall be EUR 400,000 per covered damage instance and EUR 800,000 each year covered by the insurance, this being mandatory as from 1 July 2016).

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<sup>2</sup> See articles 325-35 and seq. AMF Regulation.

<sup>3</sup> See articles L. 223-6 and seq. of the French monetary and financial Code (“CMF”).

<sup>4</sup> See article L. 511-6, 7bis CMF.

<sup>5</sup> French Conseil d'Etat, the administrative supreme court.

<sup>6</sup> See articles 325-34, 325-45 and 325-51 and seq. AMF Regulation.

They shall also (v) comply with the legal good conduct rules set forth in the CMF<sup>7</sup> (as amended) and the AMF Regulation<sup>8</sup> and (vi) ensure that their clients' interests are protected and that they receive the adequate level of information to appreciate the risks connected to their investment.

To be registered as CIPs with the ORIAS, platforms must join AMF accredited associations.<sup>9</sup> Such accredited associations shall control the professional capacity of their members and must have the AMF approve the good behaviour code and the capacity rules that they apply to their members. They also have reporting obligations towards the AMF<sup>10</sup>, which has the power to revoke the accreditation of an association.

CIPs will endure a screening process managed by the relevant accredited association before their ORIAS registration is accepted. The applicants shall provide the relevant accredited association with specific information and meet certain professional (honour, repute) and competence criteria. The detailed conditions of access to the status have been specified by in the AMF Regulation<sup>11</sup>, as modified per Ministerial Order dated 22 September 2014.

To date, no such association has been accredited by the AMF yet, as indicated in a report issued by the AMF and the French banks and insurance companies regulator – “ACPR” (*Autorité de contrôle prudentiel*) on Crowdfunding regulation on 26 August 2016. In the absence of accredited associations or when the platform has not joined such an accredited association, the registration is managed by the AMF which screens the applicants before they can register with the ORIAS. To that aim, the applicants to the CIPs status must demonstrate to the AMF that they comply with their obligations both (i) to inform their clients on risks associated with their investments and the costs associated thereto; and (ii) to ensure that the investments elected by their clients is proportionate to their experience, knowledge about investments, financial capacities and investment targets.

Contrarily to what applies for PSIs, CIPs are not subject to any statutory provision as to a minimum share capital and they do not benefit from a European passport in relation to their activities.

### 3.1.1.2 Caps on offerings

Offerings of shares and bonds on CIP and PSI platforms are capped at **EUR 2.5 million / issuer / year**.

However, **offers exceeding EUR 1 million and reaching up to EUR 2.5 million may not be made for shares or convertible bonds representing more than 50% of the issuer's capital**. This limitation **does not apply to holding companies**, which purpose is to hold and

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<sup>7</sup> See articles L. 547-1 and seq. CMF.

<sup>8</sup> See articles 325-35 and seq. AMF Regulation.

<sup>9</sup> See AMF Regulation and of article L. 547-4 CMF.

<sup>10</sup> See articles 325-60 and seq. AMF Regulation.

<sup>11</sup> See articles 325-32 and seq. AMF Regulation.

manage a shareholding in project companies, **provided the holding companies' shareholding does not exceed 50% of the project companies' share capital.**

For the avoidance of doubt, the **EUR 1 million / issuer / year cap rule does not apply to straight bond** issuances which can reach EUR 2.5 million in any event.

As for Minibons, subscription offers **cannot exceed EUR 2.5 million** over a 12-month period computed as from the first issuance of Minibons by a project holder. As indicated above, such offerings shall be repaid over a maximum 5-year period.

### 3.1.1.3 Prospectus exemptions

Since 1 October 2014, as amended in 28 October 2016, a new derogatory regime has been implemented with respect to the obligation, for issuing companies, to establish a prospectus for the public offering of shares or bonds.

#### (1) Prospectus exemption applying to Crowdfunding activities of CIPs and certain PSIs

Nowadays, the offering of equity and debt instruments by a CIP or a PSI, **on their Crowdfunding websites** is not considered as a public offering (subject to a prospectus), if the offering amount is lower than **EUR 2.5 million per issuer over a 12-month period**.<sup>12</sup>

An adequate level of information (simple, clear, balanced) must however be made available to the prospective investors. Pursuant to the provisions of articles 217-1 and 314-106 AMF Regulation, CIPs or authorised PSIs offering such securities on their websites are bound to provide the investors (CIPs) / their clients (PSIs) with detailed information meant to assess the risks associated with the investment, to permit a better understanding of the organisation and management of the beneficiary of the investment.

PSIs can manage subscription forms when their clients subscribe to a project for which prospectus obligations are waived but should nonetheless comply with the provisions of article 315-66-1 AMF Regulation, which sets obligations and procedures PSIs undertaking such role must abide by.

Similar rules apply to CIPs for the provision of services of subscription forms management.<sup>13</sup>

#### (2) Specific information obligations binding on CIPs and PSIs when prospectus exemptions apply

Where the project holders do not have to issue a prospectus in relation to the offering of shares or fixed interests bonds in their companies on CIP or PSI platforms, the relevant

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<sup>12</sup> See articles L. 411-2 and D. 411-2 CMF.

<sup>13</sup> See article 325-50 AMF Regulation.

CIP/PSI has to provide the investors with an adequate level of information on its website, in a language accessible to a lay person.

Such information mainly consists of:

- presenting the activity and the project of the issuer together with specific risks associated therewith;
- providing the last statutory accounts of the issuer together with financial projections;
- providing the level of participation of the management of the issuer in the project;
- detailing the financial rights, voting rights and information rights attached to the securities offered and those attached to the categories of securities not offered as part of the offer, and the categories of beneficiaries of such not offered securities;
- details on conditions (inter alia financial) and limits to the liquidity of the securities according to the provisions of a shareholders' agreement or of the by-laws;
- conditions subject to which an investor can be provided with copies of recordings in the issuer's books relating to its investment (e.g., copy of his/its individual shareholder's account certified true and exact by the legal representative of the company);
- details of costs to be borne by the investor at the time of subscription and thereafter; and
- the opportunity to receive on demand the details of the services provided to the issuer and of the associated fees.

### **(3) Public offering of shares of SAS**

*Société par actions simplifiée* or "SAS" (the more flexible type of limited liability company by shares that may be set up in France - often used for venture capital) are no longer prohibited from making public offering where proposed by a CIP or a PSI on their websites and only with respect to Crowdfunding operations.

A number of conditions are set out in newly applicable article L. 227-2-1 of the French commercial Code on the content of such SAS articles of association (in particular for voting rights, calls to and powers of the shareholders' meetings and the decisions that can be taken at such meetings).

#### **3.1.1.4 Other relevant corporate matters**

Based on the new regulations, PSI/CIP can no longer take a share in the companies/projects they organise sponsoring for. As a result, they can no longer have seats at the board of directors of the relevant companies as was the practice implemented by the major PSI/CIP platforms previously. Via this system, the Crowdfunding platforms also used to collect proxies for general shareholders' meetings from the investors which they can no longer

do as they are not shareholders in the financed companies (in France mandates of representation at general shareholders meetings cannot be given to third parties to the companies).

As a result, some advocate that to organize proxy advisor solutions (which is allow for publicly traded companies on regulated markets<sup>14</sup>) to make sure that no disturbance emerges in the management of the sponsored companies meanwhile ensuring that such investors/contributors still be able to participate in the decision making process and therefore protect their investment.

### 3.1.2 IFP status (straight loans, donations and rewards)

As mentioned above, online fundraising platforms which propose project financing under loans (straight loans bearing interest or not), donations or donations against rewards, may register as *Intermédiaires en Financement Participatif* (“**IFP**”).

#### 3.1.2.1 Regulatory status

IFPs are legal entities (not necessarily established in France – can be branches of foreign companies) putting in contact, through a website, people carrying projects and people financing such projects by way of straight loans (bearing interests or not) or donations (see below), within conditions and limits set forth in article D. 548-1 of the French monetary and financial Code (“**CMF**”), as regards straight loans (see below).

IFPs may also be banking and credit institutions, payment institutions, electronic currency establishments, PSIs and CIPs (if not licensed payment services intermediaries – prohibited under the CIP regime).

As to lenders, an exception to the banking monopoly has been set for project sponsors lending funds on IFP platforms and IFPs as intermediaries. Under this statutory exception, individuals and legal entities can lend money to project holders on IFP platforms, in a non-professional capacity, within the limit of one loan per project.

While acting in a professional capacity, both **individuals** and **legal entities** may raise funds on IFP platforms under straight loans or donations.<sup>15</sup> Conversely, where acting in a non-professional capacity, only **individuals** may borrow funds under interest free straight loans and receive donations from **legal entities** and **individuals** provided these lenders / donors do not act in a professional or commercial capacity.<sup>16</sup>

Registration as an IFP is possible but not mandatory for platforms operating under the donation and/or the reward schemes. If a donation or reward platform elects to register as

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<sup>14</sup> See article L. 225-106, I §2 of the French commercial Code.

<sup>15</sup> See article L. 511-6, 1° CMF.

<sup>16</sup> See article L. 511-6, 3° CMF.

IFP, it shall have the same license and registration obligations as those operating a straight loan platform.

To qualify as an IFP, a platform shall (i) be registered with the ORIAS, (ii) present certain moral guarantees, (iii) subscribe specific insurance policies (minimum guaranteed amount is EUR 250,000 per covered damage instance or EUR 500,000 by year, covering at least two damage instances per year); and (iv) abide by a good conduct code provided in the CMF.<sup>17</sup>

Additionally, Decree no. 2017-245 dated 27 February 2017 provides that IFPs who solely operate under a Donation Model shall subscribe to insurance policies with minimum guaranteed amounts of EUR 100,000 per covered damage instance and EUR 200,000 per years covered by the insurance.

Decree no.2014-1053 specified (a) the conditions of applicability of the good conduct code together with (b) the registration modalities for the internet site of the intermediaries and (c) the conditions of use of the intermediaries' services (see below).

If IFPs wishes to implement transfer of funds between lenders and borrowers, and therefore act as payment establishments, they would then need to be authorized by the ACPR and to hold a licence as a payment institution (*Prestataire de Services de Paiement*) under a simplified regime. In such instance, their share capital shall at least amount to EUR 40,000.

IFPs and credit institutions which are subject to a derogatory prudential regime (*régime prudentiel allégé*) can receive a maximum payment amount set to EUR 3 million per month.<sup>18</sup>

IFP platforms shall publish on their website, prior to 30 June of every year, an annual report regarding the previous calendar year of operations to make available to the public (i) a presentation of its management bodies, (ii) the number and overall amount of received and retained projects over the given year, (iii) that of actually financed projects, (iv) the overall amount of loans, interest-free loans and donations, together with (v) the number of lenders, average number of lenders per project, (vi) average loan amount, (vi) interest-free loan amount and (vii) donations per loan/donation and per lender / donor and (viii) the number of defaults on loans.<sup>19</sup>

IFPs shall provide on their websites, inter alia template loan and interest-free straight loan agreements, as well as donation agreements (with a minimum of clauses to be provided according to the provisions of articles R. 548-6 and R. 548-10 CMF), selection criteria for the projects on the part of the platform, possible renunciation option for the lenders, etc.

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<sup>17</sup> See articles L. 548-1 and *seq.* CMF.

<sup>18</sup> See articles D. 522-1-1 and *seq.* CMF.

<sup>19</sup> See article R. 548-4, II CMF.

### 3.1.2.2 Caps on offerings

A project holder cannot borrow more than **EUR 1 million per project** on an IFP platform (loan bearing interests or not).

Since 28 October 2016, a single **lender may not lend more than EUR 5,000 per year and per project for interest-free loans**, with no limitation currently set on such interest-free loans' duration.

Conversely, a single **lender may not lend more than EUR 2,000 per year and per project for interest bearing loans**; which shall be of a maximum duration of seven (7) years and may not be granted at usury rates (determined according to a legally binding formula).

### 3.1.3 National approval label granted to IFP, CIP and PSI

The platforms being registered as IFPs, CIPs, or PSI, can refer on their communications to the national approval label's logo showing that they have been approved by the French control authorities:

Such label aims to grant the platform users comfort as to the reliability of such labelled platforms.

Specific criminal sanctions apply to IFP and CIP statuses.

Both IFPs and CIPs are subject to good behaviour rules set forth by law (see above). In addition, they must comply with organisation and operation requirements. The management is also subject to specific prohibitions with respect to their capacity for being granted access to the IFP and CIP statuses. Shall they breach the regulations applying to the good behaviour codes and the organisational rules, IFPs and CIPs will be subject to criminal fines.



## 3.2 Regulation of Crowdfunding under the AIFMD regime

The Alternative Investment Funds Management Directive has been transposed into French law by Ordinance no. 2013-676 modifying the framework of assets management dated 25 July 2013 and Decree no. 2013-687 taken on 25 July 2013 for the application of such ordinance, under articles L. 214-24 and seq. CMF.

It results from the provisions relating to the scope of application of the AIMFD in France and the definition of Alternative Interest Funds (“AIFs”), that this regulation does general not apply to Crowdfunding platforms in France.

Indeed, AIFs are identified in French law:

- as collective investment undertakings, other than UCITs,
- which “*raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors*”. Under guidelines published by ESMA (European Securities and Market Authority), characteristics of such collective investment undertakings are that they

- do not have a general commercial or industrial purpose;
- pool capital raised from its investors for the purpose of investment with a view to generating a pooled return for those investors; and
- allow unit holders or shareholders of the undertaking no day-to-day discretion or control.

Under the current regulation, and as anticipated in last year's comments, the Crowdfunding platforms that would be likely to present projects falling under the definition of the AIF's scope of activities would be the CIPs.

CIP platforms do not generally "collect" the funds raised by the project holders, since they are prohibited from doing so under their specific regulatory regime. Most of the projects funded on CIP platforms are to be operated by operating companies or project companies which have a general commercial or industrial purpose.

Therefore, since the criteria described above will generally not be met by CIP selected projects, the AIFMD regime shall not apply to most Crowdfunding platforms in France.

However, the AMF pointed out recently that the AIFM regime could apply to Crowdfunding operations<sup>20</sup>, if platforms create holding companies to regroup shareholders of a single target company to simplify the relationships with the project holder, and in an exit perspective with a potential purchaser. In such a situation, a case by case analysis will have to be conducted to determine whether the company meets the definition of AIF, notably as regards its investment policy and its corporate purpose.

### 3.3 Licence under the Payment Services regulations

The Payment services directive was transposed into French law by Ordinance no.2009-866 dated 15 July 2009 which modified the provisions of the CMF.

Pursuant to the provisions of article L. 521-1, I CMF, "*payment services providers are payment establishments and credit institutions*".

As a result, any IFP Crowdfunding platform proposing payment services whereby it gets paid funds on behalf of third parties in the framework of Crowdfunding operations, will be acting as payment services provider.

Pursuant to the provisions of article L. 548-2, III CMF, the relevant IFP shall be at least licensed as payment establishment (*Etablissement de Paiement*) by the ACPR<sup>21</sup> or be registered as agent for payment services provider (*Agent pour Prestataire de Services de Paiement*<sup>22</sup>). These IFPs shall have a minimum capital equal to EUR 40,000.<sup>23</sup>

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<sup>20</sup> See *S'informer sur le nouveau cadre applicable au financement participatif (Crowdfunding)* – Note on Crowdfunding regulations jointly issued by the AMF and the ACPR on August 26, 2016, p.12.

<sup>21</sup> See articles L. 522-1 and *seq.* CMF.

<sup>22</sup> See articles L. 523-1 and *seq.* CMF.

<sup>23</sup> See article D. 522-1-1 CMF.

IFPs shall mention on their websites at an easily accessible location the mention of their accreditation as payment services provider.<sup>24</sup> Breach of these provisions exposes the contravening IFP platform to criminal fines and management to both criminal fines and jail sentences.<sup>25</sup>

### 3.4 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Anti-terrorism control regulations,
- Anti-money laundering regulations,
- Consumer credit acts and regulations,
- Financial canvassing (*démarchage financier*) regulation (prohibited for IFPs and very strictly limited for CIPs<sup>26</sup>),
- Information privacy regulations.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

Where IFP, CIP, PSI Crowdfunding platforms address French investors or investors domiciled in France (notably by using the French language on the platform), French regulations will apply to the platform (status/registration, information to be provided to the project holders and to the crowd, and compliance obligations) and the project holder seeking funding (mainly in terms of information obligations towards the crowd, and on the cap on the amount of funds to be raised on a platform for a specific project, on top of the fact that working capital cannot be funded per se on a Crowdfunding platforms but only a specific project i.e. purchasing a specific item of inventory, financing a designated investment, etc.).

As a reminder, IFP platforms cannot solicit funding of projects on their platforms from a database of known investors.<sup>27</sup> Funds raised on an IFP platform are capped at EUR 1m per project and lenders can only lend EUR 4,000 per year on Crowdfunding platforms if the loan is interest bearing or EUR 5,000 otherwise.

As regards PSIs and CIPs, they can solicit investors (*démarchage*) to have them sponsor a specific project.<sup>28</sup> Offerings of securities or instruments such as bonds and convertible bonds can be offered without issuance of a prospectus by the project holders, up to a campaign aiming to raise EUR 2.5m maximum (see details above). Obligations of due diligences from the platforms on the projects they offer/the project holders offering them, and on information of

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<sup>24</sup> See article L. 548-1, I CMF.

<sup>25</sup> See articles L. 572-5 and *seq.* CMF.

<sup>26</sup> CIPs may promote their services under "institutional advertising" if not limited to a specific operation, unless it communicates on an operation for which a prospectus has been issued.

<sup>27</sup> See article L. 341-3 CMF.

<sup>28</sup> See article L. 341-3 CMF.

potential crowdfunders are quite stringent. Indeed, when offerings are made exempt of a prospectus, the CIP / PSI platforms must provide the crowd with the following information:

- the activity and the project of the issuer together with specific risks associated therewith;
- the last statutory accounts of the issuer together with financial projections;
- the level of participation of the management of the issuer in the project;
- details of the financial rights, voting rights and information rights attached to the securities offered and those attached to the categories of securities not offered as part of the offer, and the categories of beneficiaries of such not offered securities;
- details on conditions (inter alia financial) and limits to the liquidity of the securities according to the provisions of a shareholders' agreement or of the by-laws;
- conditions subject to which an investor can be provided with copies of recordings in the issuer's books relating to its investment (e.g., copy of his/its individual shareholder's account certified true and exact by the legal representative of the company);
- details of costs to be borne by the investor at the time of subscription and thereafter; and
- the opportunity to receive, on demand, the details of the services provided to the issuer and of the associated fees.

With the exception of broader regulations applying to PSIs (under MiFID), which may offer Crowdfunding projects to investment/financing, with a EU passport status (and a French subsidiary), the French regulation applying to Crowdfunding activities is so specifically tailored to the domestic market that foreign operators cannot enter the French market, except the donations/rewards one.

Conversely, the CIP and IFP statuses being specificities of French law (for lending and securities offerings but not for offering of rewards and donations campaigns), and since equivalent statuses do not exist in other European countries or outside of Europe, they cannot be passported under MiFID; so that CIPs and IFPs cannot operate their activities under their French status outside of France.

Development of cross-border Crowdfunding would thus require a harmonisation of applicable rules and statuses first at the EU level, before discussions may be initiated with non-EU/non-EEA countries.

## 4.2 Inbound and foreign Crowdfunding platform address investors / lenders in France

### 4.2.1 Crowdfunding platform

Applicable regulations depend on whether the Crowdfunding platform has a (passportable) MiFID licence in another EU member state and a French subsidiary benefiting from that EU Passport or not.

In any event, foreign platforms will have to abide by French public offering regulations (prospectus regulations and banking monopoly) when targeting investors / lenders.

Also three different cases apply:

- donation / reward platforms can freely access the French market (not regulated other than through general principles of French law – Foreign platforms not having their principal place of business in France and targeting French donors will be subject to French regulations notably on donation amounts, taxes, customer protection and data privacy) ;
- platforms that offer straight loans bearing interests or not will have to comply with the French offering regulations and banking monopoly rules; and
- platforms that offer loans other than straight loans (e.g. bonds, convertible bonds), and equity might be able to access the French market provided they hold a MiFID licence and have a French subsidiary and that they comply with general French offering/prospectus regulations.

#### 4.2.1.1 Scope of MiFID

The Markets in Financial Instruments Directive (“MiFID”) entered into force in 2004. MiFID for the first time created a basis regulation for European trade markets for financial instruments (i.e. securities and related transferable finance products) and therefore defined the pan-European term “financial instrument”. Financial instruments pursuant to MiFID comprise transferable securities and financial instruments similar to transferable securities. Securities are, inter alia, stocks as well as debt-based products such as securitised bonds. Other financial instruments that are similar to securities must fulfil the following criteria:

- transferability;
- standardisation (no individual tailoring of the shares, e.g. regarding duration, volume and basic price);
- Tradability and going along with that, the possibility to acquire shares in good faith.

#### 4.2.1.2 EU Passport

As a general rule, a foreign Crowdfunding platform with a foreign MiFID licence can conduct business in France subject to complying with public offering rules in France (“EU

Passport"). The instruments which will be offered will thus be limited to those the PSIs can offer on their platforms and most likely be subject to French prospectus regulations.

## 4.2.2 Project holders

### 4.2.2.1 Loans and equity Crowdfunding

As mentioned above, specific exceptions to French prospectus requirements and French banking monopoly have been implemented for French projects financed through Crowdfunding in France.

Any offering outside this scheme would be subject to the general French financial regulations/may not be offered on Crowdfunding platforms (notably prospectus for offerings of securities/equity instruments above EUR 2.5m), thus, foreign project holders will have to abide by French public offering regulations.

Please note that criminal penalties and sanctions would apply to a breach of such mandatory offering/prospectus rules and banking monopoly regulations.

### 4.2.2.2 Donations

Foreign project holders may launch a Crowdfunding campaign on French / foreign Crowdfunding platform targeting donors located in France (notably by using the French language when presenting their projects for donations).

In such a case, French law will apply, inter alia, to donation amounts, taxes, customer protection and data privacy.

## 4.3 Outbound

In this situation, a French platform operator enters foreign (European) markets and therefore addresses foreign investors.

### 4.3.1 French platforms address foreign (EU) investors/lenders

Here, only foreign investors (e.g. French platform addresses German investors) are addressed.

German laws may apply in addition to the above mentioned French regulation as to how the offering shall be organized / non-compliance would be sanctioned.

Additionally, per French law, a French-based CIP / PSI platform must operate its activities through an internet website, which content is strictly regulated by the French AMF (and might not match the requirements of the foreign market regulation). The website must indeed present the information on the projects / project holders by using notably a “*clear and comprehensive language*” to the investors / lenders. It is therefore very unlikely that a French platform would have the right to exclusively use the English language on its website, since the website shall mainly be accessible to French speaking investors / lenders.

A French IFP Crowdfunding platform intending to address a foreign (EU) market shall comply with the laws and regulations of the foreign market regarding Crowdfunding rules.

### **4.3.2 Project holders**

#### **4.3.2.1 Prospectus regulation**

In case that a project holder only addresses foreign investors (e.g. a German platform addresses French investors) again prohibited by French law in theory, the company / project does not target the French market/French investors. The French prospectus regulation is – as a general rule – not applicable.

#### **4.3.2.2 Other financial regulation**

Local financial regulations in the country where the platform is based may apply with their specific offerings.

### **4.3.3 French platform operators addresses foreign project holders**

With the exception of the dedicated Crowdfunding exceptions, French Prospectus regulations establish a prospectus requirement only in case the financial products are offered in France.

A CIP / PSI may offer on its website securities issued by a foreign project holder as long as the platform is able to comply with its duty to act in the best interest of the investors, notably regarding (i) the selection of projects based on criteria clearly defined and published in its website, (ii) the quality and the completeness of the information provided on the issuer, (iii) the ability of the CIP / PSI to confirm the adequacy/relevancy of the contemplated investment with the financial capacities of the investor.

It is however reminded that since the French CIP status is a domestic status, CIPs are not authorized to offer their services in countries other than France.

## **4.4 Impact of EU Regulations**

Besides what has been mentioned above on access of PSIs to the French Crowdfunding market and the fact that data privacy regulations are naturally getting more and more harmonized due to the adoption of the, and soon to be transposed, General Data Protection Regulation in domestic laws across the EU, EU laws have no impact on the access of the French platforms to the foreign EU markets and conversely on the access of non-French EU platforms to the French market.

However, the AIFM-Directive may affect equity-based Crowdfunding since, as mentioned above, the AIFM regime could apply to Crowdfunding operations, if the platforms create holding companies to regroup shareholders of a single target company to simplify the relationships with the project holder, and in an exit perspective with a potential purchaser. In such a situation, a case by case analysis will have to be conducted to determine whether

the company meets the definition of AIF, notably as regards its investment policy and its corporate purpose.

#### 4.5 Summary

With the growing number of countries implementing specific Crowdfunding regulation, it is becoming more burdensome for European market participants to develop a pan-European Crowdfunding offering and for foreign and EU based Crowdfunding platforms to enter into other domestic markets.

### 5 Lessons learned from the French regulation for a possible harmonised European Crowdfunding regulation

- In particular, regulatory and subsequent practical or factual barriers hinder cross-border activities of Crowdfunding platforms from a French perspective:
- French Crowdfunding platforms cannot passport local licences within the EU; and
- foreign project holders might face different (or even multiple) local prospectus regime in case they approach French investors and even investors from their (EU) home country.

### 6 Conclusion

The new regulation should prove more tailored to the Crowdfunding market's needs and further evolution. Based on communication from the major actors of the sector in France, true enthusiasm emerges from the operators which are now ensured to operate their activities in a legal framework were they are not exposed to criminal sanctions for dealing in an unregulated sector.

The Crowdfunding operators in France have already witnessed a fast and steady development of additional platforms to keep up with the demand of the French public at large, following the enactment of the new regulations (notably with new clean energy investment schemes).

Although operators have gladly welcomed the implementation of the CIP and IFP statuses, commentators already anticipate that when growing platforms will want to develop their activities in other fields and will most surely apply to pre-existing regulatory statuses (PSI, credit institutions, etc.) which offers more business opportunities. Indeed, a number of platforms have already elected the PSI status.

## 7 Summary – Crowdfunding Regulation

| Country  | France   |
|--|--|
| <p><b>Summary</b></p> <p><b>Recent developments in Crowdfunding regulation</b></p> | <ul style="list-style-type: none"> <li>• New regulation applicable since 1 October 2014 and significantly amended since 28 October 2016.</li> <li>• Creation of 2 optional statuses (alternative to more costly and stringent statuses), subject to the control and disciplinary powers of the <i>Autorité des Marchés Financiers</i> (“AMF”) and the <i>Autorité de contrôle Prudentiel et de Résolution</i> (“ACPR”): <ul style="list-style-type: none"> <li>– “CIP” – <i>conseil en investissement participatif</i> (Crowdfunding investment advisor), including offering of new instruments (convertible bonds, preferred shares with voting rights attached and Minibons);</li> <li>– “IFP” – <i>intermédiaire en financement participatif</i> (Crowdfunding investment intermediary) for straight loans and donations.</li> </ul> </li> <li>• Crowdfunding activities opened to “PSIs” – <i>prestataire de services d’investissement</i> (investment services advisors).</li> <li>• New exceptions to banking monopoly and prospectus requirements.</li> </ul> |
| <p><b>Current / planned Crowdfunding regulation</b></p>                            |  |
| <p><b>General regulation</b></p>   | <p>Monetary and financial Code as modified by Ordinance no. 2014-559 dated 30 May 2014, Ordinance no. 20165-520 dated 28 April 2016, Decree no. 2014-1053 dated 16 September 2014 and Decree no. 2016-1453 dated 28 October 2016.</p>  |
| <p><b>Prospectus requirement</b></p>   | <ul style="list-style-type: none"> <li>• Specific Crowdfunding exceptions: Ordinary shares and/or preferred shares of sociétés par actions simplifiées with specific provisions in their by-laws can be offered on Crowdfunding platforms to the public.</li> <li>• General cap applying to CIPs and PSIs for public offering on Crowdfunding websites of ordinary shares, preferred shares, bonds (either convertible or non-convertible bonds) for a maximum raised amount of EUR 2.5 million per year.</li> </ul>   |
| <p><b>AIFMD-regulation</b></p>   | <ul style="list-style-type: none"> <li>• Generally not applicable.</li> <li>• Can apply where platforms may create holding companies to regroup shareholders of a single target company to simplify the relationships with the project holder and a potential purchaser in an exit scenario. A case by case analysis will determine if they fall in the category of AIF subject to the AIFM regulations.</li> </ul>  |
| <p><b>Payment service regulation</b></p>   | <ul style="list-style-type: none"> <li>• CIPs cannot collect payments for the project holders from the investors.</li> <li>• IFPs can apply to be licensed as payment services operator (unless they also are CIPs and are prohibited from doing so).</li> </ul>   |

|                                      |  |
|--------------------------------------|--|
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Anti-terrorism control regulations,</li> <li>• Anti-money laundering regulations,</li> <li>• Consumer credit acts and regulations,</li> <li>• Financial canvassing (<i>démarchage financier</i>) regulation (prohibited for IFPs and very strictly limited for CIPs ),</li> <li>• Information privacy regulations.</li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addresses French investors</b></p> <ul style="list-style-type: none"> <li>• CIPs must be French-based legal entities</li> <li>• A foreign platform may potentially operate in France under two hypothesis where in any event it will have to comply with French offering (prospectus) and banking monopoly regulations: <ul style="list-style-type: none"> <li>– the foreign platform benefits from a EU Passport, if certified as PSI by the French ACPR in its EU domestic state; or</li> <li>– the foreign platforms registers a French subsidiary as CIP or PSI.</li> </ul> </li> </ul> <p><b>Foreign Crowdfunding platform addresses French project holders</b></p> <ul style="list-style-type: none"> <li>• See above.</li> <li>• Where a foreign platform is targeting French project holders but is offering the securities/instruments to foreign investors and not French investors, the foreign platform will most likely be subject to the laws and regulations of the territories in which the securities/instruments are offered.</li> </ul>   |
| <b>Outbound</b>                      | <p><b>French Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>• CIPs/PSI must operate a website under strict regulation of the AMF, i.e., present the information by using a “clear and comprehensive” language to the investors.</li> <li>• The English language is unlikely to be considered as “clear and comprehensive” for investors/lenders based in France.</li> </ul> <p><b>French Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>• A CIP/PSI may offer on its website securities issued by a foreign project holder as long as the platform is able to comply with its duty to act in the best interest of the investors, notably regarding (i) the selection of projects, (ii) the quality and the completeness of the information provided on the issuer, (iii) the ability of the CIP/PSI to confirm the adequacy/relevancy of the contemplated investment with the financial capacities of the investor.</li> <li>• If CIPs/PSI intend to operate on foreign markets, they will have to comply with local laws and regulations.</li> <li>• IFPs may offer their services outside French territory as long as they comply with local laws and regulations on Crowdfunding activities.</li> </ul> |
| <b>Impact of EU regulation</b>       |  |
| <b>Prospectus regulations</b>        | See above  |

|                         |           |
|-------------------------|-----------|
| <b>AIFM-Directive</b>   | See above |
| <b>MiFID / MiFID II</b> | See above |
| <b>PSD / PSD II</b>     | See above |

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# Germany

## 1 Recent developments in the market of Crowdfunding in Germany

During the last years there were the following significant developments in Germany regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

In the early stages of Crowdfunding in Germany equity based Crowdfunding was commonly organised by means of silent partnerships (*stille Gesellschaftsbeteiligungen*). However, due to the very low prospectus threshold amounting to EUR 100.000 equity based Crowdfunding did not evolve to a considerable size in Germany.

Further, there did exist one platform that offered securities after transforming the project company (a GmbH) into a stock corporation (*Aktiengesellschaft*). However, this platform changed its business model and now presents real estate projects funded by subordinated profit-participating loans (*partiarische Nachrangdarlehen*).

Currently, there exist very few equity Crowdfunding platforms that offer equity silent partnerships (*stille Beteiligungen*) or shares in a cooperative (*Genossenschaft*). However, most platforms currently have no Crowdfunding campaigns going on.

In a nutshell, the German equity Crowdfunding market to date has a very limited size compared to the overall Crowdfunding market in Germany.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

Due to the former lack of a regulation for subordinated profit-participating loans (*partiarische Nachrangdarlehen*) in Germany, there was a shift towards this kind of investments in the past years. This was encouraged by the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz* – “**KASG**”) coming into force mid-2015. The Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) on the one hand regulated subordinated profit-participating loans (*partiarische Nachrangdarlehen*) for the first time in Germany, but – on the other hand – implemented a Crowdfunding exception (“**Crowdfunding Exception**”). The Crowdfunding Exception allows Crowdfunding projects (fulfilling certain requirements) to collect up to EUR 2.5 mio. without the requirement of a prospectus. However, the Crowdfunding Exception only applies in case the company/project collects the monies by means of abovementioned subordinated profit-participating loans (*partiarische Nachrangdarlehen*).

This trend – now tied down by the German legislator – led to an increase in platforms and companies/projects that organise Crowdfunding campaigns by means of subordinated profit-participating loans (*partiarische Nachrangdarlehen*). In these investments the investors participate in the success of the funded project or company as the interests are linked to the profit of the project or company. Still, the investor does not share liability for any losses. Nowadays, German Crowdfunding projects almost exclusively use subordinated profit-participating loans (*partiarische Nachrangdarlehen*).

There is also a clear trend towards a diversification of the activities of German Crowdfunding platforms. E. g. Crowdfunding platforms set up different platforms for different sectors (start-ups, renewables, real estate, etc.) or focus more and more on one sector only. However, there are also big Crowdfunding platforms (also the biggest Crowdfunding platform in Germany) presenting any kind of companies / projects from any sector.

Furthermore, peer to peer lending (“**P2P lending**”) became popular in Germany. To date, P2P lending is one of the most considerable sectors within the Crowdfunding market with a market volume of EUR 76.7 mio. in 2016. The biggest German P2P lending platform has – according to the company’s own information – brokered about 83,000 loans since its launch. In 2015 the loans amounted to EUR 63.8 mio.

Also after the implementation of the Retail Investors’ Protection Act (*Kleinanlegerschutzgesetz*) a bank needs to be involved in this process in Germany. There are two (indirect) P2P lending models – both with a bank as intermediate – common in Germany. In the most common business model the Crowd (lenders) grants loans via a P2P lending platform to an intermediate (fronting) bank. The bank bundles the single loans and grants one loan to the borrower. The claim for repayment is then splitted by the bank and assigned to the Crowd (lenders). In second P2P Lending model is quite similar besides the fact that an additional intermediary is involved. The P2P platform first brokers the repayment claims from the bank to the intermediary entity that is commonly owned by the P2P platform: The bank grants the loan to a borrower, transfers the (partial) repayment claims (*(Teil-) Rückzahlungsansprüche*) arising from the loan agreement in full to the intermediary entity and the intermediary entity then offers partial repayment claims to the Crowd (lenders).

Due to the fact that the genuine direct P2P lending business model not involving a bank or an intermediary entity may result in license requirements of the investors (lenders) as financiers and the borrowers, such a model does not really exist in Germany and is therefore not subject to further review.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

In Germany the Donations or Rewards Models are used predominantly to finance social or creative projects or companies (e.g. NGOs). Here, no financial investment or return is involved. Investors fund projects or companies and get no return at all or a non-monetary reward (e.g. tickets, CDs etc.). In some cases the rewards are of a symbolic value only. Actually, the Crowdfunding platform with the largest community (Crowd) in Germany is a platform offering reward based Crowdfunding for creative projects.

Noteworthy is the current and continuing trend that well established market players – like cooperative banks (*Volksbanken*) – started offering their own platforms for donations and/or rewards based Crowdfunding. On these platforms regional projects (sports clubs, schools etc.) look for financial support from the Crowd. Thereby, the regionally organised cooperative banks (*Volksbanken*) want to bring Crowdfunding also to rural areas and intensify the relationship to their customers.

### 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

Irrespective of the aforementioned categories, there is an emerging trend in Germany to facilitate Crowdfunding to finance real estate and renewable projects.

New Crowdfunding platforms specialised in this kind of projects emerge and existing platforms are extending their business.

Real estate Crowdfunding (equity and lending based Crowdfunding) in 2016 has the biggest growth rate of all Crowdfunding sectors (92.5 %) and a market share of 63.1 % and EUR 40.3 mio. There are two main grounds for this development: In Germany there is a long tradition of investments in real estate (“concrete gold”) and therefore high confidence in such investments. Secondly, the risk of non-payment is lower since the underlying asset (real estate) often has a (objectively assessed) value whereas start-ups oftentimes value themselves which might result in overvaluations.

Currently, there are five main Crowdfunding platforms either solely presenting real estate projects or at least also real estate projects.

Also the Renewable Crowdfunding is popular in Germany. Most of the projects are invested in renewable projects that finance or operate commercial power plants that produce electric power using photovoltaic cells – often with the support of local citizens, so called participation models or projects (“Citizen Participation Model” – *Bürgerbeteiligungsmo*del). Besides, there are several other renewable projects seeking funding by means of Crowdfunding platforms, i. a. wind farms, bio gas plants, replacements of old energy intensive illuminants with modern LED technology, combined heat and power plants, etc.

Most of the renewable projects use more than one source of funding. Therefore, almost every renewable project is partly financed via traditional bank loans. However, recently an increasing number of renewable projects use Crowdfunding as part of its finance structure – benefiting from the lower costs connected with funding over the Crowd compared to the conditions of bank loans. Most renewable projects also use subordinated profit-participating loans (*partiarische Nachrangdarlehen*) whereas very few renewable projects were funded by means of equity shares in a cooperative (*Genossenschaft*).

Although the legislator and the German Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* – "BaFin") try to encourage alternative financing for renewable energy projects the share in the market – against the overall trend (39 % increase of Crowdinvesting market (equity and debt-based Crowdfunding)) – decreased by 17.4 % in 2016 to only 7.6 % market share (in total EUR 4.8 mio.).

Currently, there are four main Crowdfunding platforms presenting renewable energy projects whereby the two biggest Crowdfunding platforms generate almost three-quarter of the market volume.

### 1.5 International approach

Finally, more and more US / Canadian Crowdfunding platforms and platforms from other European countries (try to) enter the German market and plan to establish international Crowdfunding platforms in order to reach (at least) the complete European market with just one platform. However, due to the increasing differences in the national Crowdfunding regulations such projects require a lot of efforts and legal advice from 28 countries.

## 2 Recent developments regarding Crowdfunding regulation in Germany

### 2.1 Retail Investors' Protection Act

On 10 July 2015 the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) which contains a first German regulation tailored to Crowdfunding entered into force.

Main topic of the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) is the extension of the scope of the German Investment Products Act (*Vermögensanlagengesetz*). This in particular affects Crowdfunding and its regulation. Until then, subordinated profit-participating loans (*partiarische Nachrangdarlehen*) were not classified as investment products. According to the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) they are now – as well as all comparable investment products – covered by the German Investment Products Act (*Vermögensanlagengesetz*). According to the legislative materials the new regulation intends to avoid

circumventions of investors' protection intended with the German Investment Products Act (*Vermögensanlagengesetz*).

This extension of the scope of the German Investment Products Act (*Vermögensanlagengesetz*) was only a matter of time. Even for legal experts it was hard to distinguish silent partnerships (*stille Beteiligungen*) and debt participation rights (*Genussrechte*) from profit-participating loans (*partiarische Darlehen*). It was hard to understand why silent partnerships and participation rights on the one side trigger the requirement to publish extensive prospectuses (that must be approved by BaFin while on the other side profit-participating loans (*partiarische Darlehen*) were completely unregulated.

In a nutshell, the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) provides for the following changes:

- subordinated profit-participating loans (*partiarische Nachrangdarlehen*) as well as (partial) repayment claims (*(Teil-)Rückzahlungsansprüche*) qualify as investment products (*Vermögensanlagen*) and – as a rule – trigger a prospectus requirement under the German Investment Products Act (*Vermögensanlagengesetz*). Since the wording of the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) was not fully clear concerning the categorization for offering (partial) repayment claims in case of P2P lending, BaFin confirmed credit claims involved in P2P lending to be classified as commercially comparable investments (*wirtschaftlich vergleichbare Anlagen*).
- increased regulation for all investment products (*Vermögensanlagen*) – such as silent partnerships (*stille Beteiligungen*), participation rights (*Genussrechte*) and (now also) subordinated profit-participating loans (*partiarische Nachrangdarlehen*) as well as (partial) repayment claims (*(Teil-)Rückzahlungsansprüche*):
  - extended requirements for prospectus
  - extended obligation to publish addenda to a prospectus
  - “ad-hoc” notifications
  - strict rules for marketing of investment products (*Vermögensanlagen*) - especially rules regarding duties to publish specific warning notices with any advertising
  - three-page fact sheet (*Vermögensanlagen-Informationsblatt* – “VIB”) – which must contain a highlighted warning notice
  - exception from Investment Products Act (*Vermögensanlagengesetz*) for cooperatives (*Genossenschaften*) is narrowed
  - extended powers for BaFin

- exception from most requirements under the German Investment Products Act (*Vermögensanlagengesetz*) explicitly tailored to fit financing by means of Crowdfunding (Crowdfunding Exception)
  - only applicable when offering profit participating loans (partiarische Darlehen), subordinated loans (Nachrangdarlehen) or commercially comparable investments (wirtschaftlich vergleichbare Anlagen)
  - no prospectus requirement up to a threshold of EUR 2.5 million per project
  - total investment amount for each investor is limited to a maximum of EUR 10,000; if exceeding a threshold of EUR 1,000 investors must comply with further requirements, i.e. self-exploration on wealth or income
  - corporations (Kapitalgesellschaften) are not limited to the absolute maximum investment of EUR 10,000 per investor
  - online platforms need a licence under the German Trade, Commerce and Industry Regulation Act (Gewerbeordnung), under the German Banking Act (Kreditwesengesetz) or the German Securities Trading Act (Wertpapierhandelsgesetz)
  - mandatory right of withdrawal (Widerrufsrecht) from investment for investors
  - (electronic) confirmation of warning notice included in fact sheet (VIB)
  - no combination of Crowdfunding Exception with other exceptions under Investment Products Act (*Vermögensanlagengesetz*)

## 2.2 Development of Crowdfunding in Germany and evaluation of KASG by German legislator

The overall market volume (equity- and debt-based Crowdfunding and P2P lending) increased by 39 % to approximately EUR 140 mio. in 2016 – however, the growth decelerated (in 2015 the growth rate was about 100 %).

Main drivers of the overall Crowdfunding growth is the real estate sector which almost doubled in 2016. Also the P2P lending market increased by around 15 %. The financing of start-ups and small and medium-sized enterprises (“SME”) made no headway in 2016 and stagnated at EUR 18.8 mio. (plus 0.4 %).

One further key finding regarding the development of Crowdfunding in Germany in 2016 is the increased press coverage regarding bad Crowdfunding news – especially regarding insolvencies of companies / projects (although there were only two insolvencies in 2016 with a low amount of losses for investors (EUR 135.000)). However, in 2017 a start-up funded by Crowdfunding went bankrupt and caused the so far biggest “Crowdfunding insolvency” in Germany (EUR 2.4 mio. losses for investors).

It can be stated from the above that since the introduction of the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) the Crowdfunding market in Germany enhanced, diversified and also consolidated to certain extent.

Anticipating these developments the German legislator added a provision to the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) stating that the Crowdfunding Exception should be reviewed by the German government until the end of 2016. In particular, the impact and usage of the thresholds of the Crowdfunding Exception as well as other (reduced) information obligations should be evaluated – supported by a study concerning the actual usage of the Crowdfunding Exception by Crowdfunding platforms. The Government report ended in legislative amendments made by the German legislator in mid-2017.

By means of the legislative amendments of the Investment Products Act (*Vermögensanlagengesetz*), entered into force in August 2017, the German legislator implemented the following most significant changes:

- prevention of any conflict of interests: exclusion of those offerings, where the issuer of the investment product can exercise direct or indirect significant influence (*maßgeblicher Einfluss*) on the operator of the Crowdfunding platform (e.g. a management or board member of the issuer is a management or board member of the Crowdfunding platform operator at the same time or both companies are affiliated companies pursuant to Stock Corporation Act (*Aktiengesetz*) and
- stronger regulation of the three-page fact sheet (VIB) and approval of BaFin before publication.

### 3 Current Regulation of Crowdfunding in Germany

#### 3.1 Licence under the German Banking Act (*Kreditwesengesetz*)

##### 3.1.1 Equity Model / Lending Model

###### (1) General Rule

Pursuant to the German Banking Act (*Kreditwesengesetz*), anyone intending to provide financial services in Germany commercially or on a scale which requires a commercially organised business undertaking requires a written licence from BaFin.

The provision of "financial services" i. a. includes the brokering of business involving the purchase and sale of financial instruments or their documentation (investment broking), the purchase and sale of financial instruments in the name of and for the account of others (contract broking) and the placement of financial instruments without commitment to take up those instruments (placement of financial instruments).

"Financial instruments" within the meaning of the German Banking Act (*Kreditwesengesetz*) include

- (equity and debt) securities
- investment products (*Vermögensanlagen*) and
- shares in collective investment undertakings (*Investmentvermögen*).

Securities include shares in stock corporations, shares in collective investment undertakings (*Investmentvermögen*) as well as debt securities including (debt) participation certificates (*Genussscheine*), bearer bonds (*Inhaberschuldverschreibungen*) and order bonds (*Orderschuldverschreibungen*). Investment products (*Vermögensanlagen*) under the German Investment Products Act (*Vermögensanlagengesetz*) comprise, inter alia, shares in other legal entities (such as limited liability companies, limited partnerships, civil law partnerships or silent partnerships (*stille Beteiligungen*), participation rights (*Genussrechte*) with regard to profits in those legal entities, shares in trust assets (*Treuhandvermögen*) and registered bonds. Until recently, subordinated profit-participating loans (*partiarische Nachrangdarlehen*) were not classified as investment products under the German Investment Products Act (*Vermögensanlagengesetz*) and therefore were not considered as "financial instruments" within the meaning of the German Banking Act (*Kreditwesengesetz*).

Since July 2015 subordinated profit-participating loans (*partiarische Nachrangdarlehen*) qualify as investment products (*Vermögensanlagen*) and therefore subordinated profit-participating loans (*partiarische Nachrangdarlehen*) are now covered by the German Investment Products Act (*Vermögensanlagengesetz*).

Further, also "other investments that grant or promise a repayment claim and a claim for interest or a cash settlement for the temporary payment of money" – as a rule – qualify as investment products (*Vermögensanlagen*) – the so called "commercially comparable investments" (*wirtschaftlich vergleichbare Anlagen*). Primarily, this captures all direct investments in container, ships, aircrafts, forests, precious metals, art, wine etc. that grant or promise cash settlement. Further, – as already mentioned – also the (partial) splitted repayment claims used in P2P lending now fall under the above definition of economically comparable investments. Therefore, both common P2P lending models are also covered by the German Investment Products (*Vermögensanlagengesetz*). In summary, where an online Crowdfunding platform facilitates the offering of securities, investment products (*Vermögensanlagen*) or shares in collective investment undertakings (*Investmentvermögen*), the operator of the platform provides financial services within the meaning of the German Banking Act (*Kreditwesengesetz*) and therefore, as a general rule, requires a license by BaFin.

## (2) Exemptions from licencing requirement

If securities (such as shares in stock corporations) are offered, no exemptions from the licensing requirement are available.

However, most German Crowdfunding platforms offer subordinated profit-participating loans (*partiarische Nachrangdarlehen*) or (partial) repayment claims (*(Teil)Rückzahlungsansprüche*) in case of P2P lending and can therefore benefit from a statutory exception to the licensing requirement (also under the new Crowdfunding Exception).

The following requirements must be met:

- only investment broking and contract broking are conducted,
- only investment products (*Vermögensanlagen*) within the meaning of the Investment Products Act (*Vermögensanlagengesetz*) or shares in collective investment undertakings (*Investmentvermögen*) are publicly offered for the first time;
- no acquiring of ownership or possession with regard to funds or shares of customers (unless a specific licence to do so has been obtained).

Where these requirements are met, the operator only needs a licence under section 34f of the German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*). Compared to a licence under the German Banking Act (*Kreditwesengesetz*) this is a relatively straightforward matter.

## (3) Additional regulatory requirements pursuant to German Financial Investment Brokerage Regulation (*Finanzanlagenvermittlungsverordnung*)

Crowdfunding and P2P lending platforms must comply with the following on-going obligations pursuant to the German Financial Investment Brokerage Regulation (*Finanzanlagenvermittlungsverordnung*)

- status information sheet (*Statusinformationsblatt*) which the investor must receive before the first investment and which must contain details about
  - status and details of the platform;
  - financing costs, risks, conflicts of interests;
  - conditions and reimbursements of project initiators or investors;
  - financial compensations and contributions of third parties.
- appropriateness test (*Angemessenheitsprüfung*) of investors regarding
  - previous investments of investors
  - knowledge of and experience with financial investments (e. g. professional background and relevant occupations of investors)

- investment objectives, duration and risk profile

However, even if the Crowdfunding platform comes to the conclusion that the investment is not appropriate for the investor, the investor is allowed to invest. The Crowdfunding platform is only required to inform the investor that the Crowdfunding platform believes that the investment is not appropriate for the investor.

### 3.1.2 Donations or Rewards Model

The donations model is not regulated at all.

Nevertheless, as stated before the Investment Products Act (*Vermögensanlagengesetz*) – as amended by the Retail Investors’ Protection Act (*Kleinanlegerschutzgesetz*) – provides for a rule stating “comparable investments that grant a claim for repayment and interest or a cash settlement for the temporary payment of money” (commercially comparable investments - *wirtschaftlich vergleichbare Anlagen*) are considered as investment products (*Vermögensanlagen*).

It cannot be completely excluded that the formerly unregulated reward-based investments could be subject to the new regulation of the Investment Products Act (*Vermögensanlagengesetz*). It could be argued that certain kinds of rewards based Crowdfunding projects could qualify as investment products (*Vermögensanlagen*) as they are considered as a comparable investment within the meaning of the Investment Products Act (*Vermögensanlagengesetz*). However, BaFin has not yet commented on a possible application of the Investment Products Act (*Vermögensanlagengesetz*) to reward-based Crowdfunding.

## 3.2 Prospectus requirements

### 3.2.1 Equity Model / Lending Model

Entrepreneurs issuing securities or investment products (*Vermögensanlagen*) to investors can be subject to a prospectus requirement. Either there is a requirement to publish a prospectus approved by BaFin under the German Securities Prospectus Act (*Wertpapierprospektgesetz*) where securities are offered (e.g. shares in stock corporations) or under the German Investment Products Act (*Vermögensanlagengesetz*) where investment products (*Vermögensanlagen*) are offered (e.g. silent partnerships, subordinated profit-participating loans (*partiarische Nachrangdarlehen*) or commercially comparable investments (*wirtschaftlich vergleichbare Anlagen*) such as (partial) loan repayment claims (*(Teil)Rückzahlungsansprüche*) in case of P2P-Lending.

The general prospectus requirement regarding securities does – inter alia – not apply where the offering of securities meets the following requirements:

- sales price does not exceed EUR 100,000 within a time period of 12 months;

- offer addresses not more than 150 investors per country in the European Economic Area or
- price per share amounts to minimum EUR 100,000 per investor

The general prospectus requirement regarding investment products (*Vermögensanlagen*) does not apply where the offering of investment products (*Vermögensanlagen*) is subject to the following:

- sales price does not exceed EUR 100,000 within a time period of 12 months;
- offering of up to 20 shares of the same investment product (*Vermögensanlage*) or
- price per share amounts to minimum EUR 200,000 per investor

According to the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) subordinated profit-participating loans (*partiarische Nachrangdarlehen*) and (partial) loan repayment claims (*((Teil)Rückzahlungsansprüche*) are now also covered by the Investment Products Act (*Vermögensanlagengesetz*). Consequently, entrepreneurs offering these investment products (*Vermögensanlagen*) are – as a rule – also subject to the prospectus requirement under the Investment Products Act (*Vermögensanlagengesetz*). In case of P2P lending the offeror of the investment products (*Vermögensanlagen*) and therefore the party obligated to prepare a prospectus would generally be the borrower or the intermediary entity. The bank itself is not offeror of the (partial) loan repayment claims since it does not “issue” these investment products to the investors.

In any case, the Crowdfunding / P2P lending platform generally is not considered as the offeror and therefore is not subject to any possible prospectus requirement.

Due to the fact that subordinated profit-participating loans (*partiarische Nachrangdarlehen*) and in case of P2P lending – (partial) repayment claims (*((Teil)Rückzahlungsansprüche*) are – by far – the most common investment products (*Vermögensanlagen*) used by Crowdfunding platforms in Germany the inclusion of these as investment products (*Vermögensanlagen*) was the most relevant change of the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*).

#### **(4) Content of the prospectus**

The Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) provides for extended requirements regarding the prospectus. The prospectus is only valid for 12 months after its publication, more information concerning the addressed investors is demanded, and BaFin is verifying the operability of the business model and is authorized to demand more information within the approval process to guarantee the investors' protection.

Moreover, the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) introduces extra requirements for additions to the prospectus during an offering and contains on-going obligations to notify the investors about substantial changes which also comprises the time period after the termination of the offer ("ad-hoc disclosure obligation"). This on-going obligation only ceases when the issued investment products are completely redeemed to the investors.

#### **(5) Crowdfunding Exception from prospectus requirement**

However, the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) provides for a new ex-emption from the prospectus requirement for the offering of subordinated profit-participating loans (*partiarische Nachrangdarlehen*) resp. – in case of P2P lending – for the offering of (partial) repayment claims (*(Teil-)Rückzahlungsansprüche*) that is specifically tailored to Crowdfunding.

According to this Crowdfunding Exception, a lighter regulation shall apply if the following (cumulative) conditions are met:

- total offering maximum: EUR 2.5 million;
- offering only of profit-participating loans (*partiarische Darlehen*), subordinated loans (*Nachrangdarlehen*) or commercially comparable investments (*wirtschaftlich vergleichbare Anlagen*);
- total amount for each investor per investment product (*Vermögensanlage*) of one issuer (company / project) is restricted as follows:
  - up to EUR 1,000: no restrictions
  - more than EUR 1,000: cash deposits or financial instruments of the investor must exceed EUR 100,000 or maximum investment up to two monthly net incomes
  - EUR 10,000: absolute maximum investment per investor that is not a corporation
  - corporations, i.e. stock corporation (*Aktiengesellschaft*), limited partnership by shares (*Kommanditgesellschaft auf Aktien*) and limited liability company (*Gesellschaft mit beschränkter Haftung*): no restrictions
- marketing via online platforms that must have a licence under the German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*), under the German Banking Act (*Kreditwesengesetz*) or the German Securities Trading Act (*Wertpapierhandelsgesetz*).
- according to the new amendments of the Investment Products Act (*Vermögensanlagengesetz*) the issuer of the investment product may not have direct or indirect significant influence (*maßgeblichen Einfluss*) on the operator of the Crowdfunding platform (e.g. a management or board member of the issuer is a management or board member of the Crowdfunding platform)

operator at the same time or both companies are affiliated companies pursuant to Stock Corporation Act (*Aktiengesetz*))

If these requirements are met no prospectus is required.

#### **(6) Fact sheet (*Vermögensanlagen-Informationsblatt – VIB*)**

Instead only a three-page fact sheet (*VIB*) must be provided to the investors to inform them about the company / project. The fact sheet (*VIB*) must contain the most relevant information about the company / project and the issued investment product (*Vermögensanlage*). It also must inform the investors about the risks, inter alia, in the form of typographically emphasized warning notices on the first page. As a rule, the investor must confirm in writing that he took notice of it by means of a signature under the fact sheet (*VIB*). However, in the case that the investment is concluded by means of distance communication (*Fernkommunikationsmittel*), e.g. the internet, the investor can confirm the warning notice electronically. This requires that the investor's identity must be verified by means of specific data, such as name, address, date and place of birth, e-mail-address or phone number and the number of his identity card / passport and the issuing authority.

#### **(7) Ban of combination (*Kombinationsverbot*)**

Once the requirements for the Crowdfunding Exception are met, it cannot be combined with other exceptions (such as issuing of only 20 shares of the same investment product (*Vermögensanlage*)) of the Investment Products Act (*Vermögensanlagengesetz*) until the investment products (*Vermögensanlagen*) are either no longer offered or are not completely redeemed to the investors.

This so called ban of combination (*Kombinationsverbot*) could result in a restriction for large-scale investors (e. g. municipal energy suppliers or communities) which intend to invest higher amounts in companies / projects along with the investors. In particular for larger start-ups the ban of combination (*Kombinationsverbot*) might have a large impact and fails to put the funding structure on a broader base.

As a rule, the co-investment of Crowdfunding and large-scale investors puts the funding structure of companies / projects on a broader base and therefore enhances their financial and economic possibilities. In turn the chance of the companies / projects to “survive” the start-up period as well as the prospects of the investors to get a return on their investments increases.

Further, the co-investment of large-scale investors could constitute an additional “protection” for the investments of the crowd investors since large-scale investors will often be in the position to conduct due diligence examinations before investing in the company / project. As a rule, these examinations result in a professionalization of the

organisation and structure of the examined company / project. Investors can directly benefit from these measures taken by the large-scale investor.

Moreover, the wording of the ban of combination (*Kombinationsverbot*) seems to be unclear. According to a narrow wording-based interpretation, the wording could lead to the assumption that only debt based investment products (*Vermögensanlagen*) should fall under the ban of combination (*Kombinationsverbot*). It appears that equity-based investments – which are predominantly preferred by large-scale investors – often by means of a private placement could be excluded. Section 2a para. 4 Investment Products Act (*Vermögensanlagengesetz*) refers to the other investment products (*Vermögensanlagen*) that should be completely redeemed. Since only debt-based investment products (*Vermögensanlagen*) can be *redeemed* by the investors, it can be argued that the Crowdfunding exception cannot be combined with other exceptions where debt-based investment products (*Vermögensanlagen*) are offered.

BaFin – hopefully – will soon clarify that this clause does not cover such kind of parallel investments of “professional” investors. However, so far it cannot be excluded that a parallel investment of a large-scale investor with crowd investors requires a more complex structure in order to comply with regulatory requirements.

#### **(8) Exception for cooperatives (*Genossenschaften*)**

Shares of cooperatives (*Genossenschaften*) or subordinated profit-participating loans (*partiarische Nachrangdarlehen*) issued by the cooperative to members of the cooperative were not considered as investment products (*Vermögensanlagen*) within the meaning of the Investment Products Act (*Vermögensanlagengesetz*) until the Retail Investors’ Protection Act (*Kleinanlegerschutzgesetz*) entered into force.

In the past cooperatives (*Genossenschaften*) were often used as an investment vehicle especially in the Renewables sector. Therefore, cooperatives (*Genossenschaften*) could have established as a real alternative to the debt-based subordinated profit-participating loans (*partiarische Nachrangdarlehen*), in case that a real equity-based investment is preferred.

However, the Retail Investors’ Protection Act (*Kleinanlegerschutzgesetz*) provides for additional restrictions to this exception – taking into account the risk that the regulation might be circumvented by means of cooperatives (*Genossenschaften*). As a result, the “cooperative exception” now only applies if no performance-based remuneration is paid for the marketing of the investments. As a conclusion, this option does not really appear to be attractive for many Renewable Energy Sources (*RES*) Projects since – if the investors are not limited to local citizens – usually the sales and marketing firms demand a performance-based remuneration. Maybe also due to the increased regulation the renewable energy sector of Crowdfunding decreased by almost 20 % in 2016 compared to 2015 (only EUR 4.8 mio.).

## (9) Advertisement

The Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) does not limit the possibilities to advertise investment products (*Vermögensanlagen*) (other than the previous drafts of the Act). Instead, advertisements must contain some specific warning notices which shall illustrate the risks that may arise from the investments.

The following warning notice must – as a rule – be contained in every advertisement.

*“The acquisition of this investment product is associated with considerable risks and can result in the loss of the deployed funds.”*

A special provision (which considers the particular characteristics of Crowdfunding like advertisements by means of twitter) to this general requirement only applies if the following requirements are met:

- advertisement in electronic media
- solely text-based advertisements
- less than 210 characters
- link – which is called “warning notice” – to separate document that includes the warning notice

Further, advertisements which promote investment products (*Vermögensanlagen*) that do not provide for a fixed interest rate must contain a respective warning notice in addition.

Finally, any references to the competences of BaFin as well as the use of the word “funds” are prohibited in connection to the investment product (*Vermögensanlage*).

### 3.2.2 Donations or Rewards Model

As already stated above, it cannot be excluded with absolute certainty that specific kinds of rewards based Crowdfunding projects are covered by the category of “comparable investments that grant or promise a claim for repayment and interest”. As a result those kind of companies / projects could – as a rule – also require a prospectus (unless one of the exceptions e.g. the Crowdfunding Exception is applicable).

## 3.3 Regulation of Crowdfunding under the AIFMD regime

According to the Capital Investment Act (*Kapitalanlagegesetzbuch*) the Alternative Investment Fund Manager Directive (“AIFMD”) regulation of funds and fund managers applies when there is an alternative investment fund (“AIF”) managed by an alternative investment fund manager (“AIFM”). The Retail Investor's Protection Act (*Kleinanlegerschutzgesetz*) does not affect this regulation.

The Capital Investment Act (*Kapitalanlagegesetzbuch*) provides that AIFs include a collective investment undertaking which:

- raises capital from a number of investors,
- with a view to investing it in accordance with a defined investment policy for the benefit of those investors;
- is not an operating company conducting business outside the financial sector and
- does not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS).

### 3.3.1 Operating company seeking funding

German AIFMD regulation does not apply to operating companies outside the financial sector which do not invest in accordance with a defined investment policy.

BaFin clarifies in its interpretation guideline on the "Scope of application of KAGB / Interpretation of the term collective investment undertaking" that companies are operating companies if they operate the facility or production themselves within their day-to-day business. However, BaFin states that an operating company can make use of the service of an intra-group company or an external service provider, as long as the day-to-day discretion remains at the company.

Taking this into account, companies / projects seeking funding by means of a Crowdfunding platform are operating companies outside the financial sector if:

- their business strategy is simply the commercial success of their business;
- they do not intend to follow any defined investment policy but want to finance their on-going day-to-day business; and
- they operate the facility, production or project themselves within their day-to-day business or make use of the service of an intra-group company or an external service provider (as long as the day-to-day discretion remains at the company)

In general, these requirements are met by the "typical" start-up or developing company seeking funding for its general commercial business by means of a Crowdfunding platform. Such companies should therefore fall outside the scope of the German AIFMD regulation.

### 3.3.2 Project Company seeking funding

#### (1) Equity Model

However, basically typical project companies (especially in the sectors real estate or renewables) could fall under the AIFMD regulation.

BaFin illustrates in its Interpretation Guideline that companies (besides companies structured as cooperatives (*Genossenschaften*)) that are established to finance a single project ("**Project Company**") such as – regarding the renewable energy sector – a wind farm or a solar park and do not operate the facility or production themselves or by means of an outsourcing company leaving the day-to-day discretion to the Project Companies cannot qualify as operating companies.

Further, regarding the real estate sector BaFin explicitly expresses in its Interpretation Guideline that both the operation of real estate property, e. g. a hotel or a health care facility (*Pflegeeinrichtung*) and project development (design, acquisition, development of real estate property and subsequent sale of self-developed real estate property) should be regarded as operative activities. On the other side, the acquisition, rental, lease, management and sale of real estate properties should not be regarded as operative activities.

Accordingly, these kinds of Project Companies might constitute an AIF within the meaning of the German AIFMD regulation if they seek funding in return for a share in the profits or revenue generated by the project as in the Equity Model and do not conduct operative activities.

## **(2) Lending Model**

Investments by means of subordinated loans (*Nachrangdarlehen*) (or other debt-based investments) can generally be structured as non-AIF investments because the investors do not share liability for any losses.

## **(3) Donations or Rewards Model**

Some of the Project Companies do not offer any kind of revenue but instead (often small) non-financial rewards in return (Donations or Rewards Model). In the latter case (e.g. if the promised reward is a ticket or a copy of the movie or game) it can be argued that the funds are not invested for the benefit of those investors and the funding therefore contains no collective investment undertaking and no AIF. BaFin has not yet commented on a possible application of the AIFMD regime to rewards based Crowdfunding.

### **3.3.3 Crowdfunding Platform**

Due to the fact that an operator of a Crowdfunding platform does not raise capital from investors for its own business, it should not qualify as an AIF. Further, there are sound arguments to state that the Crowdfunding platform does not "manage" the underlying investment, but merely arranges investments into projects or companies.

Hence, the operator of a Crowdfunding platform does not qualify as an AIF or an AIFM.

### 3.3.4 Pooling vehicle

In case the company / project prefers funding by just one major investor instead of a large number of small retail investors, it is possible that the platform involves a pooling vehicle. A pooling vehicle is a company founded to concentrate a large number of investors. Such pooling vehicle is likely to be an AIF and therefore to be subject to the German AIFMD-regulation – provided that the pooling vehicle issues equity and no debt based investments. However, since the Crowdfunding Exception requires debt based investments, campaigns that want to benefit from the Crowdfunding Exception must offer debt instruments anyway. In this case also pooling entities can be implemented.

Further, a contractual pooling of the investors can be recommendable. In this structure no pooling *entity* is involved but rather the investors enter into a pooling agreement with the company / project itself or a third party.

### 3.4 Regulation under the Payment Services Directive

Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services (*Finanztransfersgeschäft*) within the meaning of the German Payment Services Supervisory Act (*Zahlungsdienstaufsichtsgesetz*) – that implements the Payment Services Directive in Germany. Such transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform who then passes the funds to the company / project.

In this context BaFin has decided that operators of internet platforms (such as Crowdfunding platforms) in general cannot benefit from the exemption for commercial agents. In order to avoid such licencing requirements the operator of a Crowdfunding platform could cooperate with a bank or a licenced payment institution for the handling of payments rather than acting as an intermediary itself. However, the structure of this cooperation must meet detailed requirements by BaFin.

Another alternative solution is that the company / project simply collects the funds from the investors on their own bank account. The power of disposal (*Verfügungsbefugnis*) over the funds by the company / project should be limited until the respective Crowdfunding platform agrees.

### 3.5 Possible additional Regulations

- Other common regulations to which the operator of a Crowdfunding platform may be subject include:
- German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*)
- German Act on Money Laundering (*Geldwäschegesetz*)
- German Securities Trading Act (*Wertpapierhandelsgesetz*)

- Consumer Credit Regulation (Vorschriften für Verbraucherdarlehensverträge)

## 4 Regulatory barriers for Crowdfunding crossing borders

As already stated almost every funding is made by means of subordinated profit-participating loans (*partiarische Nachrangdarlehen*) on the German Crowdfunding market. From a practical point of view the security regulation (Prospectus Directive and implementing Securities Prospectus Act (*Wertpapierprospektgesetz – WpPG*) as well as the upcoming Prospectus Regulation) are irrelevant for the German Crowdfunding sector. This is due to the fact that there are currently no platforms presenting companies / projects offering securities (*Wertpapiere*).

### 4.1 Applicable law

According to BaFin German financial regulation applies in case German investors are approached by (foreign) financial actors (such as issuers of financial instruments or brokers, etc.). In this regard BaFin follows a marketing focussed approach (*vertriebsbezogener Ansatz*). In a corresponding circular (Notes regarding the licensing requirements for conducting cross-border banking business and / or providing cross-border financial services dated April 2005) BaFin states that not only providers of financial services that have their registered office or ordinary residence in Germany fall under German regulatory law but also in case the financial actor targets the German market in order to offer financial services to companies / persons in Germany. Indicators for BaFin to assume that a financial actor targets the German market are

- addressing of potential German investors by direct mail, fax or e-mail
- regarding internet offers: whether it is clear from the content of the website (and not its technical accessibility on the internet) that these products are targeted to the German market, i. a. the following criteria are considered by BaFin
  - domain name
  - (in particular) German language
  - product description
  - financial or other country-specific client information and legal framework
  - prices and methods of payment
  - provision of German contact details
  - fact that financial services are actually being sold to German clients
  - content of possible advertising
  - disclaimer is only one of many indications

As a conclusion, also foreign financial actors not having their place of business or residence in Germany are captured by German regulation in case they approach German investors – which mainly depends on the language used at the platform.

## 4.2 Inbound

The question is if the Crowdfunding platform addresses German investors or wants to present German companies / projects on its platform.

### 4.2.1 Foreign Crowdfunding platform addresses German investors

German regulatory law can apply to the

- Crowdfunding platform (mainly licence, information and compliance obligations)
- and / or the
- company / project seeking funding (mainly prospectus and information obligations)

As mentioned above according to BaFin – as a general rule – German financial regulation applies in case the German market (German investors) is approached by (foreign) financial actors. BaFin considers several criteria in order to assume that the German market is approached and (therefore) German regulatory law is applicable. The main criterion of BaFin is whether the German language is used to present the investment opportunities. Therefore, in case the investment opportunities are presented in German language (as we assume in this case) BaFin will (most likely) come to the conclusion that German regulatory law applies.

#### 4.2.1.1 Crowdfunding platform

##### (1) Licence obligations

The applicable regulatory law (and its extent) depend on whether the Crowdfunding platform has a (passportable) MiFID licence in another EU member state.

##### (a) The platform holds a MiFID licence in another EU member state

##### *Scope of MiFID*

The Markets in Financial Instruments Directive (“**MiFID**”) entered into force in 2004. MiFID for the first time created a basis regulation for European trade markets for financial instruments (i. e. securities (*Wertpapiere*) and related transferable finance products) and therefore defined the pan-European term “financial instrument”. Financial instruments pursuant to MiFID i. a. comprise transferable securities (*übertragbare Wertpapiere*) and financial instruments equal to transferable securities (*übertragbare Wertpapiere*). Transferable securities (*übertragbare Wertpapiere*) are, inter alia, stocks (*Aktien*) as well as debt-based products such as securitised bonds (*verbriefte Anleihen*). Other financial instruments that are equal to transferable securities (*übertragbare Wertpapiere*) must fulfil the following criteria:

- transferability (Übertragbarkeit)
- standardisation (Standardisierung) (no individual tailoring of the shares, e.g. regarding duration, volume and basic price)
- tradability (Handelbarkeit) and going along with that, the possibility to acquire shares in good faith (gutgläubiger Erwerb).

Also the second Markets in Financial Instruments Directive (“**MiFID II**”) which came into force on 3 July 2014 did not change its scope of applicability. Hence, also the definition of transferable securities and other financial instruments that are equal to transferable securities (*übertragbare Wertpapiere*) remains unaffected. EU member states have to implement MiFID II into national law until 3 July 2017. All market participants have to apply the new rules from January 2018 – in Germany MiFID II will i. a. be implemented by means of the German Banking Act (*Kreditwesengesetz*).

In Germany, all start-up companies are organised in the legal form of a limited liability company (*GmbH*) or an entrepreneurial company (*UG haftungsbeschränkt*). Project companies are usually structured also as limited liability companies (*GmbH*) or limited partnerships (*GmbH & Co. KG*). This is due to the fact that these company forms can be easily established and handled without causing high costs (other than e. g. stock corporations (*Aktiengesellschaften*)).

Nearly all Crowdfunding platforms in Germany facilitate the investment in companies / projects by means of subordinated profit-participating loan (*partiarisches Nachrangdarlehen*).

Shares in a limited liability company (*GmbH*) (or *UG (haftungsbeschränkt)*), in limited partnerships (*GmbH & Co. KG*) as well as subordinated profit-participating loan (*partiarisches Nachrangdarlehen*) are not tradable. In particular the transfer of shares of a German limited liability company (*GmbH*) requires a notarial certification.

Due to this fact, shares of a limited liability company (*GmbH*), of an entrepreneurial company (*UG haftungsbeschränkt*) or limited partnerships (*GmbH & Co. KG*) are not fungible and hence no financial instruments within the meaning of MiFID. As a consequence they are not covered by the scope of MiFID.

Also subordinated profit-participating loans (*partiarische Nachrangdarlehen*) are not tradable and therefore not covered by MiFID.

#### *Scope of German Banking Act (Kreditwesengesetz)*

In Germany, MiFID was mainly implemented in the Securities Trading Act (*Wertpapierhandelsgesetz – WpHG*) (mainly regarding the trading of securities (*Wertpapiere*) and related obligations) and the German Banking Act (*Kreditwesengesetz – KWG*) (mainly regarding possible licence requirements).

Other than the scope of MiFID the scope of the German Banking Act (*Kreditwesengesetz*) covers – inter alia – investment products (*Vermögensanlagen*) within the meaning of the German Investment Products Act (*Vermögensanlagengesetz*). In detail, the scope of the German Investment Products Act (*Vermögensanlagengesetz*) covers

- all kinds of shares of companies (also shares in limited liability companies (*GmbH*), entrepreneurial companies (*UG (haftungsbeschränkt)*) and limited partnerships (*GmbH & Co. KG*) and
- (since the Retail Investors’ Protection Act (*Kleinanlegerschutzgesetz*)) subordinated profit-participating loans (*partiarische Nachrangdarlehen*)

Therefore, the scope of the German Banking Act (*Kreditwesengesetz*) is wider than the scope of MiFID since it covers also the non-tradable investment products (*Vermögensanlagen*).

#### *EU Passport*

As a general rule, a foreign Crowdfunding platform with a foreign MiFID licence can conduct business in Germany without applying for a licence and without having a presence in Germany – so-called notification procedure pursuant to section 53b German Banking Act (*Kreditwesengesetz*) (“**EU Passport**”).

However, in case the Crowdfunding platform holds a MiFID licence and intends to address German investors it is unclear whether the MiFID licence is sufficient also for providing financial services with regard to financial instruments *not* covered by this MiFID licence – e. g. broking of shares in a limited liability company (*GmbH*) or subordinated profit-participating loans (*partiarische Nachrangdarlehen*).

Until now, BaFin did not develop any administrative practice with regard to this issue. Judged by the purpose of the introduction of an EU Passport as well as the intention of the European legislator (intending to create a level playing field across the EU) these MiFID licences should also cover financial instruments covered by the MiFID licence of the target country. Especially taking into account the purpose to ensure a protection of the consumers / investors, a MiFID licence should be sufficient since the regulatory requirements for a MiFID licence are much higher than the German licence according to section 34f German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*).

On the other side, generally European law only covers such areas where it explicitly is applicable by means of European law (Regulations or Directives) (primacy of application (*Anwendungsvorrang*)). Other areas where only national law exists may therefore not be covered by European regulation (e. g. MiFID).

As a conclusion of these different scopes, it cannot be excluded that a Crowdfunding platform with a foreign MiFID licence might need – in addition – a licence under section 34f German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*) or section 32 German Banking Act (*Kreditwesengesetz*) – in order to be allowed to offer all kinds of company shares as well as subordinated profit-participating loans in Germany.

Nevertheless, in case the Crowdfunding platform facilitates the offering of securities or equal financial instruments it is generally allowed to use the EU passport.

#### **(b) The platform has no MiFID licence**

As already mentioned, if the Crowdfunding platform intends to address German investors, German regulation is applicable. Therefore, the Crowdfunding platform must – as a principle – apply for a licence according to section 32 of the German Banking Act (*Kreditwesengesetz*) if the platform targets the German market in order to offer financial services.

In the case that the Crowdfunding platform intends to broker only profit-participating loans (*partiarische Darlehen*), subordinated loans (*Nachrangdarlehen*) or commercially comparable investments (*wirtschaftlich vergleichbare Anlagen*) the local licence according to section 34f German Trade, Commerce and Industry Regulation Act (*Gewerbeordnung*) might be sufficient.

#### **(2) Other financial regulation**

The foreign Crowdfunding platform might be subject to other German regulation in exceptional cases (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*) in case the Crowdfunding platform provides services related to (equity / debt) securities.

In addition, the German Act on Money Laundering (*Geldwäschegesetz*) is the only German regulatory law which – in principle – is not connected to the marketing focussed approach (*vertriebsbezogener Ansatz*) set out above. Rather, it establishes identification and further obligations in case the obliged person has its place of residence / business in Germany. Since the foreign Crowdfunding platform does not have its place of business in Germany it cannot be subject to German anti-money laundering regulation (but may be subject to the local anti-money laundering regulation of its home (EU) country).

##### **4.2.1.2 Company / project**

#### **(1) German prospectus regulation**

As mentioned above according to BaFin – as a general rule – German financial regulation applies in case the German market (German investors) is approached by (foreign) financial actors. The main criterion of BaFin to assess whether German

regulatory law is applicable comprises whether the German language is used to present the investment opportunities.

As already mentioned, in Germany there exist two prospectus regimes:

- German Securities Prospectus Act (*Wertpapierprospektgesetz*) provides for a prospectus requirement for the public offering of *securities* and implements the EU Prospectus Directive and will soon be replaced by the Prospectus Regulation which will have immediate effect, and
- German Investment Products Act (*Vermögensanlagengesetz*) stipulates a prospectus requirement for the public offering of investment products (*Vermögen-sanlagen*) and is a national regulation

In detail, the applicable prospectus regime depends on whether the foreign company / project offers transferable securities (which is often the case in foreign (EU) countries, e. g. France) or other financial products. In the latter case it is most likely that the offered financial products are investment products within the meaning of the (then applicable) German Investment Products Act (*Vermögensanlagengesetz*).

As a principle, the respective prospectus regime is applicable which means that the company / project must prepare a prospectus.

In case the foreign company / project intends to benefit from the Crowdfunding Exception it is limited to the offering of subordinated profit-participating loans (*partiarischen Nachrangdarlehen*) since only these investment products (*Vermögensanlagen*) may benefit from the Crowdfunding Exception.

## **(2) Other financial regulation**

Foreign companies / projects that issue securities might – in exceptional cases – be subject to additional information / compliance regulation (German Securities Trading Act (*Wertpapierhandelsgesetz*)), e.g. in case the foreign company / project issues securities that are admitted to trading on an organised market.

In contrast, foreign companies / projects which issue subordinated profit-participating loans (*partiarische Nachrangdarlehen*) are – as a rule – not addressees of other additional (information or compliance) obligations (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*))

German anti-money laundering regulation is not applicable to the foreign issuing entities –companies / projects – since they or any branches are not based in Germany.

### **4.2.2 Foreign Crowdfunding platform addresses German companies**

Again German regulatory law can apply to the

- Crowdfunding platform (mainly licence and information obligations)

- and / or
- company / project intending to be funded on the Crowdfunding platform (mainly prospectus and information obligations).

As mentioned above BaFin considers several criteria in order to assume that the German market is approached and (therefore) German regulatory law is applicable. The main criterion of BaFin is whether the German language is used to present the investment opportunities. Other criteria may be that here German companies / projects are involved. However, this criterion alone will (most likely) not be sufficient for BaFin to conclude that German regulatory law is applicable.

Therefore, in case the investment opportunities are not presented in German language BaFin will (most likely) come to the conclusion that German regulatory law does not apply. This is because the offer is presented on a foreign website / language (e. g. French) by a foreign Crowdfunding platform.

#### **4.2.2.1 Crowdfunding platform**

##### **(1) Licence obligations**

Here, the foreign Crowdfunding platform does not approach German investors. Since in this case German regulatory law does not apply there are no licence requirements (e. g. pursuant to the German Banking Act (*Kreditwesengesetz*)).

##### **(2) Other financial regulation**

German companies / projects (almost never) issue equity-based securities in the Crowdfunding market. This is because German companies / projects are (almost always) structured as limited liability companies (*GmbH*) or entrepreneurial companies (*UG*). The shares of such corporate structures do not constitute securities.

However, as a general rule the information and compliance obligations (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*)) may be applicable to the foreign Crowdfunding platform in case it provides services related to debt-based securities (e. g. bonds) which also constitute securities. In this case the foreign Crowdfunding platform might be subject to other German regulation (e. g. German Securities Trading Act (*Wertpapierhandelsgesetz*)).

E. g. when providing investment broking (*Anlagevermittlung*) pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*) the Crowdfunding platform must provide investors with information about itself, the provided services and the financial instruments to which the services are related; conduct an appropriateness test (*Angemessenheitsprüfung*) vis-à-vis investors, etc.

In case the company / project does not offer securities, but other investments (shares / loans) – as a general rule – there are no additional financial regulations applicable to the foreign Crowdfunding platform except from the case it holds a MiFID licence (then generally the German Securities Trading Act (*Wertpapierhandelsgesetz*) might be applicable).

Further, the foreign Crowdfunding platform is not subject to German anti-money laundering regulation.

#### **4.2.2.2 Company / project**

##### **(1) Prospectus regulation**

Both, the German Securities Prospectus Act (*Wertpapierprospektgesetz*) and the German Investment Products Act (*Vermögensanlagengesetz*) establish a prospectus requirement only in case the financial products are offered *in Germany*.

As mentioned above according to BaFin – as a general rule – German financial regulation does not apply here since the investment opportunities are not presented in German language

In addition (and in contrast to the licence obligations above), pursuant to BaFin with regard to the prospectus regulation it is required to place a disclaimer on the website (in German) stating that the offer is not intended to be offered to German investors.

##### **(2) Other financial regulation**

In case the German companies / projects might issue debt-based securities (e. g. bonds) these will constitute securities. In this case the German companies / projects might be subject to other German regulation (e. g. German Securities Trading Act (*Wertpapierhandelsgesetz*)). This might comprise information and / or compliance obligations if it – in exceptional cases – issues securities which are admitted to trading on an organised market.

The issuing entities – German companies / projects – generally are within the areal applicability since they are based in Germany. However, they do not constitute an obliged person within the meaning of the German Act on Money Laundering (*Geldwäschegesetz*). Therefore, they are not required to comply with German anti-money laundering law.

### **4.3 Outbound**

In this situation a German Crowdfunding platform enters foreign (European) markets and therefore addresses foreign investors.

Again, two different alternatives must be considered:

- German Crowdfunding platform approaches foreign (EU) investors or
- German Crowdfunding platform approaches German investors and presents a company / project from another EU member state on its platform

#### **4.3.1 German Crowdfunding platform addresses foreign (EU) investors**

As mentioned above BaFin considers several criteria in order to assume that the German market is approached and (therefore) German regulatory law is applicable.

Here, only foreign investors (e.g. a German platform addresses French investors) are addressed.

Nevertheless, here the Crowdfunding platform and the companies / projects are based in Germany and therefore the main actors have a German reference. If several further indicators – e. g. German contact persons and details or investment opportunities are clearly adjusted to German regulatory law – tend to the assumption that the German market is approached and – in addition – the investment opportunity is presented in English language, BaFin might come to the conclusion that the German market is approached and German regulatory law is applicable. This is due to the fact that English language – as a world-wide spoken language – is – meanwhile – spoken and understood by the majority of Germans and this criterion alone will not be sufficient for BaFin to exclude that the German market is approached.

However, within the overall view of all criteria BaFin will – anyway – (most likely) come to the conclusion that German regulatory law is not applicable in this case. This is because only foreign investors are addressed and only foreign (e. g. French) language is used. Therefore, German regulatory law will (likely) not be applicable.

##### **4.3.1.1 Crowdfunding platform**

###### **(1) Licence obligation**

As mentioned above German regulatory law will not be applicable to the German Crowdfunding platform. This is due to the fact that the German Crowdfunding platform exclusively addresses foreign investors and also does not use German (but e. g. French) language. Therefore, the German Crowdfunding platform will (likely) not have licence requirements (e. g. pursuant to the German Banking Act (*Kreditwesengesetz*)).

###### **(2) Other financial regulation**

In addition, - in exceptional cases – the German Crowdfunding platform might be subject to other regulation which constitutes additional (information or compliance) obligations (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*)).

E. g. in case the German Crowdfunding platform provides services related to equity-based / debt-based securities (*Wertpapiere*). This situation seems to be likely when foreign companies / projects are involved which often issue securities (unlike in Germany). In this case the German Crowdfunding platform might comply with information and compliance obligations with regard to its provided services. E. g. when providing investment broking (*Anlageberatung*) pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*) it must provide investors with information about itself, the provided services and the financial instruments to which the services are related; conduct an appropriateness test (*Angemessenheitsprüfung*) vis-à-vis investors, etc.).

As a general rule the German Crowdfunding platforms provide investment broking (*Anlagevermittlung*). Therefore, they do not constitute an obliged person under the German Act on Anti-Money Laundering (*Geldwäschegesetz*). Only financial firms that provide investment advice (*Anlageberatung*) constitute obliged persons. In conclusion, German Crowdfunding platforms do not have to comply with the respective identification (and other) obligations pursuant to the German Act on Anti-Money Laundering (*Geldwäschegesetz*).

#### **4.3.1.2 Company / project**

##### **(1) Prospectus regulation**

Both, the German Securities Prospectus Act (*Wertpapierprospektgesetz*) and the German Investment Products Act (*Vermögensanlagengesetz*) establish a prospectus requirement only in case the financial products are offered *in Germany*.

In case that a company / project only addresses foreign investors (e.g. a French platform addresses French investors) the company / project does not target the German market / German investors. The German prospectus regulation is – as a general rule – not applicable.

Please note that in any case, it is required by BaFin to (e. g.) place a disclaimer on the website (in German) stating that the offer is not intended to be offered to German investors.

##### **(2) Other financial regulation**

Companies / projects that issue securities might – in exceptional cases – be subject to additional information / compliance regulation (German Securities Trading Act (*Wertpapierhandelsgesetz*)), e.g. in case the company / project issues securities that are admitted to trading on an organised market.

In contrast, companies / projects which issue subordinated profit-participating loans (*partiarische Nachrangdarlehen*) or shares of a limited liability company (*GmbH*) /

entrepreneurial company (*UG*) are – as a rule – not addressees of other additional (information or compliance) obligations (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*)).

German anti-money laundering regulation is not applicable to the foreign issuing entities since they or any branches are not based in Germany. German issuing entities generally do not constitute an obliged person within the meaning of the German Act on Money Laundering (*Geldwäschegesetz*). Therefore, any companies / projects are not required to comply with German anti-money laundering law.

#### **4.3.2 German Crowdfunding platform addresses foreign companies / projects**

As mentioned above BaFin considers several criteria in order to assume that the German market is approached and (therefore) German regulatory law is applicable. The main criterion of BaFin is whether the German language is used to present the investment opportunities. There-fore, in case the investment opportunities are presented in German language BaFin will (most likely) come to the conclusion that German regulatory law applies.

Here, German investors are approached – German language will be used. BaFin will come to the conclusion that German regulatory law will be applicable.

##### **4.3.2.1 Crowdfunding platform**

###### **(1) Licence obligation**

In case the German Crowdfunding platform approaches German investors and presents foreign companies / projects, e. g. French companies, on its platform it – as already stated – must have a licence – either pursuant to section 32 KWG (mainly when providing services related to securities) or the small (local) licence pursuant to section 34f of the Commerce and Industry Regulation Act (*Gewerbeordnung*). The latter small licence is only sufficient in case the German Crowdfunding platform provides services related to investment products (*Vermögensanlagen*) pursuant to the German Investment Products Act (*Vermögensanlagegesetz*) – especially subordinated profit-participating loans (*partiarische Nachrangdarlehen*). Additionally, only in this case the German Crowdfunding platform may make use of the Crowdfunding exception.

###### **(2) Other financial regulation**

In addition, - in exceptional cases where the German Crowdfunding platform provides services mainly related to (equity- / debt-based) securities – it might be subject to other additional regulation which constitutes additional (information or compliance) obligations (e. g. German Securities Trading Act (*Wertpapierhandelsgesetz*). E. g. when providing investment broking (*Anlageberatung*) pursuant to the German Securities

Trading Act (*Wertpapierhandelsgesetz*) it must provide investors with information about itself, the provided services and the financial instruments to which the services are related; conduct an appropriateness test (*Angemessenheitsprüfung*) vis-à-vis investors, etc.).

As a general rule the German Crowdfunding platforms provide investment broking (*Anlagevermittlung*) and therefore do not constitute an obliged person under the German Act on Anti-Money Laundering (*Geldwäschegesetz*). Only financial firms that provide investment advice (*Anlageberatung*) constitute obliged persons in the aforementioned meaning. Therefore, German Crowdfunding platforms do not have to comply with the respective identification (and other) obligations of the German Act on Anti-Money Laundering (*Geldwäschegesetz*).

#### 4.3.2.2 Company / project

##### (1) Prospectus regulation

As mentioned above the European prospectus regulation and the implementing German Securities Prospectus Act (*Wertpapierprospektgesetz*) only apply to securities within the meaning of MiFID / MiFID II.

Since foreign companies / projects often offer equity-based or debt-based securities (e. g. bonds) the (European and German) prospectus regulation is applicable to these financial products offered on the German Crowdfunding market. Also the upcoming European Prospectus Regulation that provides for an exemption from the prospectus requirement up to EUR 1 mio. will in this case apply to securities within the meaning of MiFID / MiFID II.

In the unlikely case that the foreign company / project will issue subordinated profit-participating loans (*partiarische Nachrangdarlehen*), the company / project will then be subject to the German Investment Products Act (*Vermögensanlagengesetz*) and its prospectus (and additional) obligation.

Moreover, the foreign company / project might face (local) prospectus requirements pursuant to its home (EU) country. We cannot assess whether a (local) prospectus requirement exists if the German Crowdfunding platform presents foreign companies / projects in a campaign to German investors. However, it may be that the foreign (EU) country / the respective financial regulation authority might not follow the marketing focussed approach (*vertriebsbezogener Ansatz*) of BaFin but another approach (e. g. simply connected to the seat / place of residence of the foreign (EU) country). Here, a double regulation cannot be excluded.

## (2) Other financial regulation

Foreign companies / projects that issue securities might – in exceptional cases – be subject to additional information / compliance regulation (German Securities Trading Act (*Wertpapierhandelsgesetz*)), e.g. in case the company / project issues securities that are admitted to trading on an organised market.

Foreign companies / projects that issue subordinated profit-participating loans (*partiarische Nachrangdarlehen*) are – as a rule – not addressees of additional obligations (e. g. pursuant to the German Securities Trading Act (*Wertpapierhandelsgesetz*)).

Since the issuing entities – German companies / projects – generally do not constitute an obliged person within the meaning of the German Act on Money Laundering (*Geldwäschegesetz*) they are not required to comply with German anti-money laundering law.

### 4.4 Impact of EU regulation

#### 4.4.1 Prospectus rule / regimes

As stated above, in Germany there exist two prospectus regimes:

- German Securities Prospectus Act (*Wertpapierprospektgesetz*) based on the European Prospectus Directive and provides for a prospectus requirement for the public offering of securities and
- German Investment Products Act (*Vermögensanlagengesetz*) stipulates a prospectus requirement for the public offering of investment products (*Vermögensanlagen*). The Investment Products Act (*Vermögensanlagengesetz*) is not based on any European regulation at all – but is simply a German regulation.

In Germany, only the prospectus regime regarding the offering of securities is harmonized on a pan-European level since the Prospectus Directive (and in the near future the Prospectus Regulation) and the implementing German regulation only cover transferable securities within the meaning of MiFID / MiFID II. Therefore, only a very limited amount of the German Crowdfunding market is covered by harmonized European legislation implemented into German law.

Rather, almost all Crowdfunding campaigns in Germany are not affected by European prospectus regulation but (pure) national prospectus regulation pursuant to the German Investment Products Act (*Vermögensanlagengesetz*).

#### 4.4.2 AIFM-Directive

The AIFM-Directive and the implementing German Capital Investment Act (*Kapitalanlagegesetzbuch*) mainly affect equity-based Crowdfunding and especially Crowdfunding for renewable energy projects (especially in case the renewable energy project is structured as cooperative (*Genossenschaft*)).

In case Project Companies do not operate the facility or production themselves or by means of an outsourcing company leaving the day-to-day discretion to the "Project Companies" they are no operating companies and – as a general rule – fall under the extensive fund regulation. Only in case the Project Company is structured as a cooperative (*Genossenschaft*) and issues its shares it will most likely be outside of the fund regulation since BaFin and the German legislator stated that cooperatives (*Genossenschaften*) are outside the scope of the fund regulation – due to their specific promoting purpose (*Förderzweck*).

Apart from the above, there might exist a (regulatory) barrier since the AIFM-Directive might apply to the company / project. This might cause a real barrier for cross-border offerings since the interpretation whether there exists a collective investment undertaking (and therefore an AIF) or not remains with the respective local authorities (e. g. BaFin in Germany). It cannot be excluded that if a local supervisory authority comes to the conclusion that an entity is *not* considered as an AIF, another local supervisory authority might come to another conclusion and classify this company / project as an AIF.

Further, also the fact that the definition and the requirements regarding retail AIF (*Publikums-AIF*) are not harmonized on a European level might lead to frictions in the intensity of regulation: In some EU member states there exist lower / higher regulation for retail AIF whereas in some EU member states retail AIF are completely prohibited.

#### 4.4.3 MiFID / MiFID II

Since MiFID and MiFID II i. a. are restricted to transferable securities (and equal financial instruments) the scope of application on the German Crowdfunding market remains very limited. Since most German Crowdfunding platforms facilitate the offering of subordinated profit-participating loans (*partiarische Nachrangdarlehen*) which are not covered by MiFID / MiFID II they are not impacted by MiFID / MiFID II. Rather, they are – in this case – able to use the small local licence which is not based on MiFID / MiFID II but rather local regulation.

The main scope of application of MiFID and MiFID II for Crowdfunding in Germany is the general possibility to apply for a MiFID (II) licence to generally operate in each EU member state (for the description of frictions between European and German regulation see above).

#### 4.4.4 PSD / PSD II

The Payment Services Directive was implemented by the Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz*) in 2009. The Payment Services Directive II (entered into force in 2016) must be implemented until January 2018. Payment services in Europe are generally harmonized, but regarding the details there is still room for interpretation of the national legislators and (especially) financial regulation authorities which does not lead to a fully harmonized single market in Europe

Regarding Crowdfunding especially the money remittance services (*Finanztransferschäfte*) come into consideration:

Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services within the meaning of the Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz*). Such transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform which then passes the funds to the company / project. In this context BaFin has decided that operators of internet platforms (such as Crowdfunding platforms) in general are not covered by the exemption for commercial agents.

In order to avoid such licencing requirements the operator of a Crowdfunding platform may cooperate with a bank or a licenced payment institution for the handling of payments rather than acting as an intermediary itself. However, the structure of this cooperation must meet detailed requirements by BaFin.

Therefore these two directives have a great impact for Crowdfunding regarding the transaction of the investments.

#### 4.5 Summary

With the growing number of countries implementing specific Crowdfunding regulation it is be-coming more burdensome for European market participants to develop a pan-European Crowd-funding business and for foreign Crowdfunding platforms to enter into the European market. This development is contrary to the aim of establishing a European single market and promoting Crowdfunding as a method of financing on a European level.

Especially the following (regulatory and subsequent practical or factual) barriers hinder cross-border activities of Crowdfunding platforms from a German perspective:

- wide scope of application of German regulatory law with BaFin following its marketing focussed approach (*vertriebsbezogener Ansatz*)
- inbound as well as outbound: frictions regarding the scope of MiFID licence and local (German) licence with regard to covered financial instruments and usage of the EU Passport which at least leads to uncertainty of Crowdfunding

market participants – especially the question remaining unresolved whether subordinated profit-participating loans (*partiarische Nachrangdarlehen*), which are predominantly used in Germany, are covered by the MiFID licence / can be offered in the host (EU) country

- foreign Crowdfunding platforms face factual and practical barriers when applying for local licences in Germany (no base in Germany and proof of expertise)
- German Crowdfunding platforms cannot passport local licences within the EU
- almost every investment in companies / projects by means of Crowdfunding in Germany is made through subordinated profit-participating loans (*partiarische Nachrangdarlehen*) which are not covered by MiFID / MiFID II or the European prospectus regulation. Therefore, German Crowdfunding platforms do not have access – especially – to the European prospectus regulation
- the same applies to usual structures of start-ups that are structured as limited liability companies / entrepreneurial companies which do not fall under MiFID / MiFID II or the European prospectus regulation since they do not constitute transferable securities or equal financial instruments. Therefore, almost the whole German Crowdfunding market is excluded from the possibilities of the European prospectus regulation (EU Passports, etc.) but is restricted to the local prospectus regulation.
- foreign companies / projects might face different (or even double) local prospectus regimes in case they approach German investors and also investors of their home (EU) country

## 5 Lessons learned from Germany's regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model ("dos")

Considering the aim of the Retail Investors' Protection Act (*Kleinanlegerschutzgesetz*) to protect investors from dubious and risky investment products, it is certainly a positive signal that the German legislator recognised the importance of Crowdfunding as a new kind of funding and is willing to grant Crowdfunding the possibility to establish in the market.

For a possible harmonised European the following aspects can serve as a role model:

- exception of Crowdfunding from most regulatory requirements (in particular prospectus requirement)

- three-page fact sheet (Vermögensanlageninformationsblatt - VIB) for investors
- only lighter regulation of the Crowdfunding platform
- unlimited investment amounts for "professional" investors

## 5.2 Aspects that should be avoided ("don'ts")

However, the predominant part of the German Crowdfunding regulation should not build the basis for a possible European Crowdfunding regulation.

In particular, the following aspects should not be inherited:

- limitation of the Crowdfunding Exception only to (profit-participating) subordinated loans (*partiarische Nachrangdarlehen*) or commercially comparable investments (*wirtschaftlich vergleichbare Anlagen*)
- limitation of EUR 1.000 per investor without additional statements regarding income / wealth for retail investors – should be increased
- ban of combination (*Kombinationsverbot*) – makes parallel investments of professional investors and the Crowd difficult
- limitation of EUR 2.5 million threshold regarding prospectus requirement instead of harmonisation with European Prospectus Directive (EUR 5 million)

## 6 Conclusion

In conclusion, the (regulatory) barriers deriving from the frictions between European and German regulation as well as the partial European regulation hinder all participants to extend their activities also to cross-border situations.

The increasing fragmentation of the European Crowdfunding regulation due to the introduction of national Crowdfunding regulation even aggravates the barriers for cross-border Crowdfunding.

The following measures on a European legislative / administrative level should be taken in order to create a level playing field around the EU from a German perspective:

- regulation of all types of financial instruments used in Crowdfunding (especially also non-transferable financial instruments) and not only securities (*Wertpapiere*) – with regard to MiFID (II) as well as European prospectus regulation
- clarification that MiFID (II) licence (and the EU Passport) covers all financial instruments covered by national legislation in the host EU member state when crossing border

- consistent definitions of terms based on European legislation (e. g. collective investment undertaking, financial instruments) by means of European authorities

## 7 Summary – Crowdfunding regulation

| Country   | Germany  |
|---|--|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• first Crowdfunding regulation (Retail Investors' Protection Act - <i>Kleinanlegerschutzgesetz</i>) entered into force on 10 July 2015</li> <li>• revised Investment Products Act (<i>Vermögensanlagengesetz</i>) centrepiece of the new regulation and subject to the most changes</li> <li>• evaluation of German Crowdfunding exception does (likely) not lead to facilitation of German Crowdfunding regulation (and especially the Crowdfunding exception)</li> <li>• new amendments to the Crowdfunding regulation of Investment Products Act (<i>Vermögensanlagengesetz</i>) entered into force in August 2017</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>                            |  |
| <b>General regulation</b>   | <ul style="list-style-type: none"> <li>• if Crowdfunding platform facilitates offering of securities, investment products (<i>Vermögensanlagen</i>) or shares in collective investment undertakings (<i>Investmentvermögen</i>), the operator of the platform provides financial services <ul style="list-style-type: none"> <li>- BaFin authorisation required</li> </ul> </li> <li>• qualification of subordinated loans (<i>Nachrangdarlehen</i>), profit-participating loans (<i>partiarische Darlehen</i>) and commercially comparable investments (<i>wirtschaftlich vergleichbare Anlagen</i>) as investment products (<i>Vermögensanlagen</i>)</li> <li>• exemption for investment broking (<i>Anlagevermittlung</i>) (and investment advice (<i>Anlageberatung</i>)) only regarding investment products (<i>Vermögensanlagen</i>) or shares in collective investment undertakings (<i>Investmentvermögen</i>) <ul style="list-style-type: none"> <li>- straight forward licence sufficient for operator of Crowdfunding platform</li> </ul> </li> </ul> |
| <b>Prospectus requirement</b>   | <ul style="list-style-type: none"> <li>• prospectus requirement for offering of securities or investment products (<i>Vermögensanlagen</i>)</li> <li>• general threshold: EUR 100,000 per issuer within 12 months (i. a.)</li> <li>• qualification of subordinated loans (<i>Nachrangdarlehen</i>) profit-participating loans (<i>partiarische Darlehen</i>) and commercially comparable investments (<i>wirtschaftlich vergleichbare Anlagen</i>) as investment products (<i>Vermögensanlage</i>)</li> </ul>  |

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|   | <ul style="list-style-type: none"> <li>• increased regulatory requirements for prospectus for all investment products (<i>Vermögensanlagen</i>)</li> <li>• exception from prospectus requirement for Crowdfunding and P2P lending – under specific conditions             <ul style="list-style-type: none"> <li>- total offering maximum: EUR 2.5 million;</li> <li>- offering only of profit-participating loans (<i>partiarische Darlehen</i>), subordinated loans (<i>Nachrangdarlehen</i>) or commercially comparable investments (<i>wirtschaftlich vergleichbare Anlagen</i>) (the latter relevant for P2P lending in Germany);</li> <li>- total amount for each investor per investment product (<i>Vermögensanlage</i>) of one issuer (project initiator) is restricted as follows:                 <ul style="list-style-type: none"> <li>⇒ up to EUR 1,000: no restrictions</li> <li>⇒ more than EUR 1,000: cash deposits or financial instruments of the investor must exceed EUR 100,000 or maximum investment up to two monthly net incomes</li> <li>⇒ EUR 10,000: absolute maximum investment per investor</li> <li>⇒ Corporations: no restrictions</li> </ul> </li> <li>- three-page fact sheet (VIB) prior approved by BaFin</li> </ul> </li> </ul> |
| <p><b>AIFMD-regulation</b></p>              | <ul style="list-style-type: none"> <li>• typical start-up company in general does not constitute an AIF</li> <li>• "Project Company" might constitute AIF             <ul style="list-style-type: none"> <li>- extensive AIFMD regulation for AIF and its manager (AIFM)</li> <li>- AIFM requires BaFin authorisation</li> </ul> </li> <li>• "Project Companies" that constitute operating companies are no AIF</li> <li>• funding by means of subordinated loans (<i>Nachrangdarlehen</i>), profit-participating loans (<i>partiarische Darlehen</i>) or commercially comparable investments (<i>wirtschaftlich vergleichbare Anlagen</i>) does not entail an AIF</li> <li>• Cooperatives (<i>Genossenschaften</i>) shall – according to BaFin – not constitute a collective investment undertaking and therefore fall outside the AIFMD regulation</li> </ul>  |
| <p><b>Payment service regulation</b></p>    | <ul style="list-style-type: none"> <li>• transfer of funds through operator may constitute money remittance service (<i>Finanztransfersgeschäft</i>)             <ul style="list-style-type: none"> <li>- BaFin authorisation required</li> </ul> </li> <li>• cooperation with a payment institute / bank is required</li> </ul>   |
| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• German Trade, Commerce and Industry Regulation Act (<i>Gewerbeordnung</i>)</li> <li>• German Act on Money Laundering (<i>Geldwäschegesetz</i>)</li> <li>• German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)</li> </ul>   |
| <p><b>Regulatory barriers</b></p>           |  |
| <p><b>Inbound</b></p>                       | <p><b>Foreign Crowdfunding platform addresses German investors</b></p>   |

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|  | <ul style="list-style-type: none"> <li>- German regulatory law is applicable since German investors are approached by presenting the investment opportunities in German language</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- The platform has a foreign MiFID / MiFID II licence and intends to address German investors</li> <li>- as a general rule, a platform with a foreign MiFID licence can conduct business in Germany without applying for a licence and without having a presence in Germany (so-called notification procedure / EU Passport)</li> <li>- however, MiFID (MiFID II) and the German implementation – German Banking Act (<i>Kreditwesengesetz</i>) – do not have the same scope. Therefore, e.g. shares of a German limited liability company or entrepreneurial company are covered by the scope of the German Banking Act (<i>Kreditwesengesetz</i>) but not by MiFID (II)'s scope. The same applies to subordinated profit-participating loans (<i>partiarische Nachrangdarlehen</i>).</li> <li>- It remains an open question whether a Crowdfunding platform with a foreign MiFID / MiFID II licence can offer financial instruments in Germany which are covered by the scope of the German Banking Act (<i>Kreditwesengesetz</i>) but not from MiFID</li> <li>- therefore, it cannot be excluded that a Crowdfunding platform with a foreign MiFID licence might need – in addition – a (local) German licence – in order to be allowed to offer all kinds of company shares as well as subordinated profit-participating loans in Germany</li> <li>- Generally, the foreign Crowdfunding platform might be subject to other German regulation in exceptional cases (e.g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>). It is not subject to the German Act on Money Laundering (<i>Geldwäschegesetz</i>).</li> </ul> </li> <li>- The platform has no MiFID / MiFID II licence and intends to address German investors             <p style="margin-left: 40px;">The Crowdfunding platform must apply for a licence:</p> <ul style="list-style-type: none"> <li>- generally: according to section 32 of the German Banking Act (<i>Kreditwesengesetz</i>) if the platform targets the German market in order to offer financial services, or</li> <li>- in exceptional cases: under section 34f German Trade, Commerce and Industry Regulation Act (<i>Gewerbeordnung</i>) if the platform only conducts investment broking and only offers profit-participating loans (<i>partiarische Darlehen</i>), subordinated loans (<i>Nachrangdarlehen</i>) or commercially comparable investments (<i>wirtschaftlich vergleichbare Anlagen</i>) publicly for the first time.</li> </ul> </li> </ul> |
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|  | <ul style="list-style-type: none"> <li>• Foreign Company / project <ul style="list-style-type: none"> <li>- German prospectus regimes are applicable since the foreign companies / projects offer investment opportunities in Germany</li> <li>- applicable prospectus regime depends on whether the foreign company / project offers transferable securities (which is often the case in foreign (EU) countries, e. g. France) or other financial products, which most likely are investment products within the meaning of the German Investment Products Act (<i>Vermögensanlagegesetz</i>)</li> <li>- in case foreign company / project intends to benefit from the Crowdfunding exception it is limited to offering of subordinated profit-participating loans (<i>partiarischen Nachrangdarlehen</i>) since only these investment products (<i>Vermögensanlagen</i>) may benefit from Crowdfunding exception.</li> <li>- in exceptional cases other regulation (e. g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)) might be applicable constituting information and compliance obligations (mainly if (equity / debt) securities are involved). The German Act on Money Laundering (<i>Geldwäschegesetz</i>) is – as a general rule – not applicable to the companies / projects.</li> </ul> </li> </ul> <p><b>Foreign Crowdfunding platform addresses German companies / projects</b></p> <ul style="list-style-type: none"> <li>- BaFin will (most likely) come to the conclusion that German regulatory law does not apply in case the investment opportunities are not presented in German language</li> </ul> <ul style="list-style-type: none"> <li>• Crowdfunding platform <ul style="list-style-type: none"> <li>- as a general rule since the foreign Crowdfunding platform will not target the German market / German investors, German regulatory law is not applicable – no licence requirements pursuant to German regulatory law</li> <li>- Generally, the foreign Crowdfunding platform might be subject to other German regulation in exceptional cases (e. g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)). It is not subject to the German Act on Money Laundering (<i>Geldwäschegesetz</i>).</li> </ul> </li> <li>• German Company / project <ul style="list-style-type: none"> <li>- also the German company / project will – as a general rule – not be subject to obligations pursuant to the German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>) but is required to provide for a disclaimer stating that it does not address German investors</li> <li>- in case German companies / projects issue debt-based securities (e. g. bonds) they might – in exceptional cases – be subject to other German regulation (e. g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>))</li> </ul> </li> </ul> |
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|                        | <ul style="list-style-type: none"> <li>- issuing entities – German companies / projects – generally are no obliged person within the meaning of the German Act on Money Laundering (<i>Geldwäschegesetz</i>)</li> </ul>  |
| <p><b>Outbound</b></p> | <p><b>German Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>- Here, only foreign investors (e.g. a German platform addresses French investors) are addressed. However, if several further indicators – e. g. German contact persons and details or investment opportunities are clearly adjusted to German regulatory law, English language – tend to the assumption that the German market is approached BaFin might come to the conclusion that German market is approached and German regulatory law is applicable.</li> <li>- However, within the overall view of all criteria BaFin will (most likely) come to the conclusion that German regulatory law is not applicable in this case. This is because only foreign investors are addressed and only foreign (e. g. French) language is used.</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- as a general rule since the Crowdfunding platform will not target the German market / German investors, German regulatory law is not applicable – no prospectus requirements</li> <li>- Crowdfunding platform might be subject to other German regulation in exceptional cases (e. g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>). It is not subject to the German Act on Money Laundering (<i>Geldwäschegesetz</i>).</li> </ul> </li> <li>• Company / project             <ul style="list-style-type: none"> <li>- Both, the German Securities Prospectus Act (<i>Wertpapierprospektgesetz</i>) and the German Investment Products Act (<i>Vermögensanlagengesetz</i>) are not applicable since the financial products are not offered <i>in Germany</i>. In any way, it is required to place a disclaimer on the website (in German) stating that the offer is not intended to be offered to German investors.</li> <li>- companies / projects that issue securities might – in exceptional cases – be subject to additional information / compliance regulation (German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)), e.g. in case the company / project issues securities that are admitted to trading on an organised market.</li> <li>- in contrast, companies / projects which issue subordinated profit-participating loans (<i>partiarische Nachrangdarlehen</i>) are – as a rule – not addressees of other additional (information or compliance) obligations (e. g. pursuant to the German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)).</li> <li>- since issuing entities – German companies / projects – generally do not constitute obliged persons within the meaning of the German Act on Money Laundering (<i>Geldwäschegesetz</i>) they are not required to comply with German anti-money laundering law.</li> </ul> </li> </ul> |

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|                                       | <p><b>German Crowdfunding platform addresses foreign companies / projects</b></p> <ul style="list-style-type: none"> <li>- here, German investors are approached – German language will be used. BaFin will come to the conclusion that German regulatory law will be applicable.</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- regular German regulation applies to the Crowdfunding platform (licence obligation)</li> <li>- Crowdfunding platform might be subject to other German regulation in exceptional cases (e. g. German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>))</li> <li>- they are not subject to the German Act on Money Laundering (<i>Geldwäschegesetz</i>).</li> </ul> </li> <li>• Company / project             <ul style="list-style-type: none"> <li>- German prospectus regimes are applicable since the foreign companies / projects offer investment opportunities in Germany</li> <li>- applicable prospectus regime depends on whether the foreign company / project offers transferable securities (which is often the case in foreign (EU) countries, e. g. France) or other financial products, which most likely are investment products (<i>Vermögensanlagen</i>) within the meaning of the German Investment Products Act (<i>Vermögensanlagegesetz</i>)</li> <li>- in case foreign company / project intends to benefit from the Crowdfunding Exception it is limited to offering of subordinated profit-participating loans (<i>partiarische Nachrangdarlehen</i>) since only these investment products (<i>Vermögensanlagen</i>) may benefit from Crowdfunding Exception.</li> <li>- in addition to the German regulation, the company / project might face (local) prospectus requirements pursuant to its home (EU) country, e. g. in case the home (EU) country / financial regulation authority follow another approach than BaFin (marketing focussed approach)</li> <li>- in this case the prospectus requirements of the host (EU) country as well as the German regulation might apply to the company / project which might lead to double regulation</li> <li>- companies / projects that issue securities might – in exceptional cases – be subject to additional information / compliance regulation (German Securities Trading Act (<i>Wertpapierhandelsgesetz</i>)), e.g. in case the company / project issues securities that are admitted to trading on an organised market.</li> <li>- The German Act on Money Laundering (<i>Geldwäschegesetz</i>) is – as a general rule – not applicable to the companies / projects.</li> </ul> </li> </ul> |
| <p><b>Impact of EU regulation</b></p> |  |

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| <p><b>Prospectus regulations</b></p> | <p>Due to the fact that most of the German start-ups are no stock corporation, but constitute limited liability companies (<i>GmbH</i>) whose shares are no securities (which are subject to the EU prospectus regulation), these EU regulations have no great impact to Crowdfunding in Germany</p>  |
| <p><b>AIFM-Directive</b></p>         | <ul style="list-style-type: none"> <li>• AIFM-Directive and its implementation in German law have a very small impact on Crowdfunding since the “typical” company (start-up) or project seeks funding for its general operative activity (commercial business) by means of a Crowdfunding platform</li> <li>• only so called Project Companies that do not operate the business themselves and do not constitute a cooperative (<i>Genossenschaft</i>) might be subject to the fund regulation.</li> <li>• Different interpretations of local authorities regarding the definition of collective investment undertaking (constituting an AIF) might lead to different application of AIFM-D and local implementations             <ul style="list-style-type: none"> <li>- severe consequences for company / project as well as (at least economically) for Crowdfunding platforms.</li> <li>- also retail AIFs are regulated differently across the EU which complicates cross-border situations.</li> </ul> </li> </ul> |
| <p><b>MiFID / MiFID II</b></p>       | <p>In Germany most of the Crowdfunding platforms facilitate the offering of subordinated profit-participating loans (<i>partiarische Nachrangdarlehen</i>) which do not fall under MiFID / MiFID II. In doing so they are able to use an exception to the German Banking Act (<i>Kreditwesengesetz</i>) and need a small (local) licence. This local licence has less requirements, but is not passportable into other EU member states.</p>  |
| <p><b>PSD / PSD II</b></p>           | <ul style="list-style-type: none"> <li>• Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services (<i>Finanztransfersgeschäft</i>) within the meaning of the Payment Services Supervision Act (<i>Zahlungsdiensteaufsichtsgesetz</i>), the German implementation of PSD / PSD II in German law</li> <li>• Great impact for Crowdfunding regarding the transaction of the investments</li> </ul>  |

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# Greece

## 1 Recent developments in the market of Crowdfunding in Greece

During the last 12 months, no significant developments in the market of Crowdfunding took place in Greece. More specifically:

### 1.1 The Donations/ Rewards Model

In Greece the Donations or Rewards model is mainly used to finance initiatives, projects and actions of non-profit non-governmental organizations (NGOs), of start-up companies, as well as of schools and local communities which are related to cultural and artistic events, apparel, movie and documentary production, archaeology, music, publications, photography, theatre, sports etc. Contrary to the other models, the Donations/Rewards model involves the donation of an amount for either no return (Donations model) or, in the case of Rewards model, of non-monetary return or of return of symbolic value only (e.g. T-shirts, tickets to concert etc.). Due to lack of regulation, there are currently numerous platforms using the Donations/Rewards model operating in Greece, set up either by individuals or credit institutions, and the number thereof has increased significantly over the past years.

Noteworthy is the current and continuing trend that well established market players – like credit institutions museums, as well as other companies, NGOs and non-profit organizations developed platforms for donations and/or rewards based Crowdfunding in order to support the economy and innovation, by providing financial support of innovative projects in the sectors of arts, welfare, health and solidarity, social economy, cultural entrepreneurship, research and education, athletic events and activities, environment and sustainability, energy, information technology, agriculture etc.

### 1.2 The Lending Model

Given the fact that the provision of loans and credit continues to be highly regulated in Greece, and that no legislative development has taken place over the past years, there has been no development as to this model, and no lending platforms may legally operate in Greece.

### 1.3 The Equity Model

Although significant developments have taken place to the respective legislation affecting the equity model, and more specifically the recent introduction on September 6, 2016 of a bespoke regime for investment-based Crowdfunding, such developments do not have a significant impact in the market yet. Although, to our knowledge, a couple of applications for the operation of equity Crowdfunding platforms have been submitted to the competent regulatory authorities, until today no equity platform lawfully operates in Greece.

### 1.4 Real Estate Crowdfunding/ Renewable Crowdfunding

Real estate Crowdfunding does not exist in Greece whereas renewable Crowdfunding exists only in the framework of the donations/rewards model set out above.

## 1.5 International approach

Law 4416/2016 was only recently enacted, and as mentioned above, so far there are no equity platforms operating in Greece, through which foreign projects or companies could enter the Greek market. As regards the platforms operating under the donations or rewards model, to the best of our knowledge, these host usually the projects of Greek companies, artists and organizations, as well as initiatives and projects of Greek schools and local communities.

## 2 Recent developments regarding Crowdfunding regulation in Greece

### 2.1 Exemption of security offers made through Crowdfunding platforms from prospectus publication requirements

On September 6 2016, law 4416/2016 came into force introducing an exemption from the obligation to draft and publish a prospectus for public offers which are made through electronic platforms provided that certain conditions are met.

In order for the companies/issuers to be exempted from drafting and publishing a prospectus, the following conditions must be met cumulatively:

- The public offer must be performed exclusively through an electronic system (platform), operated by: 1) a local investment firm (AEPEY) licensed to provide at least the investment services of a) reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments and b) the ancillary service of safe-keeping and administration of financial instruments on behalf of clients, including custody and related services, such as money and collateral administration or 2) a local alternative investment fund manager (AEDOOE) licensed to provide the ancillary (non-core) services of a) provision of investment advice, b) safe-keeping and administration in relation to shares or units of collective investment undertakings (UCITs) and c) reception and transmission of orders in relation to financial instruments or 3) a credit institution licensed to provide the investment service of reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments.
- The total value of the securities offered must be less than five hundred thousand Euro (EUR 500,000.00) per issuer per year; and
- The participation of a retail (a non-professional) investor cannot exceed the amount of five thousand Euro (EUR 5,000.00) and in any case ten percent (10%) of the average of its declared tax income of the past three years, per issuer, and the amount of thirty thousand Euro (EUR 30,000.00) per year, per AEPEY or credit institution.

## 2.2 Organizational requirements for investment firms, alternative investment fund managers and credit institutions operating Crowdfunding platforms

Law 4116/2016 amended also law 3606/2007 implementing in Greece Directive 2004/39/EC (“MiFID”) introducing provisions for the organizational and informational requirements that local investment firms, alternative investment fund managers and credit institutions must meet when operating Crowdfunding platforms which benefit from the aforementioned exemption of prospectus publication requirements.

More specifically according to the newly introduced paragraph 14 of art. 12 of law 3606/2007, local AEPEYs, local AEDOOEs as well as credit institutions must notify either the Hellenic Capital Markets Committee (“HCMC”) or the Bank of Greece (“BoG”) respectively of their intention to operate Crowdfunding platforms submitting on the same time a file with information on such activity. Such information includes indicatively the resolution of the board of directors of the relevant firm or institution on taking up the specific activity of operating Crowdfunding platforms, a new organization chart, the names of the persons to be employed for such activity as well as their qualifications, the internal rules describing the way the activity will be organized, the criteria to be followed for the choice of the companies-issuers whose securities will be offered through the platform, as well as the monitoring and compliance procedures with the investors’ information requirements (see below under section 2.1.3). The HCMC or the BoG respectively can oppose to the above intention of the regulated entities to operate Crowdfunding platform within two (2) months as of the filing of above notification, if they find that the organization requirements mentioned above are not met.

Subject to the aforementioned notification requirements, no further licensing of the firms or institutions which operate the Crowdfunding platforms is required.

## 2.3 Minimum investors’ informational requirements

The law provides for the minimum information to be provided by AEPEYs, AEDOOEs and credit institutions to investors wishing to invest to the Crowdfunding platforms that such entities operate. Such minimum information includes the following:

- information on the legal situation of the issuers, their business activity and their potential investment projects;
- information on the shareholders / partners of the issuers holding more than five percent (5%) of the issuers as well as information on the capital of the issuers and a description of any agreements known to the issuer, the entry into force of which could, at a subsequent date, result in a change of control in the issuer;
- information on the administration of the issuer, on any possible conflict of interests between the administration, the shareholders of the issuer and the AEPEY or credit institution that acts as an intermediary;
- information on where the annual financial statements of the issuer are published (e.g. the website of the issuer, General Commercial Registry or GEMI, etc.);

- information on the securities offered and the terms of the offer (e.g. allocation of the securities in case the offer is over-covered, delivery of the securities etc.),
- description of the rights (voting rights, information rights) that the investor will acquire;
- prominent disclosure of risk factors that are specific to the issuer, its industry and the securities being offered,
- warning that the investment is not realizable immediately and that there is a risk of total loss of the invested capital;
- disclosure of the persons responsible for the aforementioned information;
- warning that the aforementioned information is not approved by the HCMC;

The HCMC is authorized by the new law to further specify the information obligations that the entities which operate Crowdfunding platforms have towards potential investors but no such decision has been issued to date.

Although the legislative framework for Crowdfunding platforms in Greece is very new, many doubts have been already expressed by market participants as to the suitability of such framework for enhancing actually the conditions for business development of the Crowdfunding sector in Greece. The legislator has adopted a conservative approach allowing the operation of Crowdfunding platforms only to licensed entities which have not demonstrated a particular interest yet for this market yet. The new regime has also received a severe criticism for imposing unnecessarily high regulatory compliance costs to Crowdfunding platform operators as opposed to the potential profit that the same will be receiving from the operation of the platforms.

### 3 Current Regulation of Crowdfunding in Greece

#### 3.1 Financial Services license requirements

##### 3.1.1 Equity Model

According to Law 3606/2007 implementing in Greece Directive 2004/39/ EC (“MiFID”), the offering of investment services and the performance of investment activities in Greece, in a professional capacity, is allowed in principle to investment firms licensed in Greece by the HCMC or to investment firms from other European Union countries having the benefit of the European “passport” (i.e. following the notification procedure) to offer services either through a branch or on a cross-border basis without an establishment in Greece.

The provision of investment services includes, inter alia, the receipt, transmission and execution of orders on behalf of clients for performing transactions in financial instruments, the placement of financial instruments without commitment to take up those instruments and the provision of investment advice.

Financial instruments are, inter alia, securities, money market instruments, units in collective investment funds, options, futures, swaps, futures and other derivatives.

Where a Crowdfunding platform facilitates the offering of securities to the public and/or provides advice to investors on investment in securities, the operator of the platform may be considered to be providing the investment services of placing of financial instruments and/or investment advice, services which require the license by the HCMC.

Recently enacted law 4416/2016 amends law 3606/2007 by enabling the public offering of securities through electronic platforms, and thus opens the way for the operation of equity Crowdfunding platforms, under specific terms and requirements. As mentioned above, in order for said platforms to be lawful, they have to be operated by local investment firms (namely AEPEYs, AIFMs or credit institutions) which are licensed by the HCMC or the BoG respectively, and more specifically: by either: 1) a local investment firm (AEPEY) licensed to provide at least the investment services of a) reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments and b) the ancillary service of safe-keeping and administration of financial instruments on behalf of clients, including custody and related services, such as money and collateral administration or 2) a local alternative investment fund manager (AEDOOE) licensed to provide the ancillary (non-core) services of a) provision of investment advice, b) safe-keeping and administration in relation to shares or units of collective investment undertakings (UCITs) and c) reception and transmission of orders in relation to financial instruments or 3) a credit institution licensed to provide the investment service of reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments.

Said firms and credit institutions are the only ones entitled to operate equity Crowdfunding platforms, provided that they notify in advance to the HCMC or the BoG their intention to operate such platforms and provide adequate information thereto on the way the activity is organized and will be performed. Furthermore, the law obliges investment firms and credit institutions to provide specific information regarding the issuers and their companies hosted in the platform to the investors, so that the latter are duly informed. For more information regarding the notification to be made to the HCMC or the BoG and the information to be provided to investors please refer to section 2.1.1 above.

To be noted that law 4416/2016 provides the conditions for the operation of Crowdfunding platforms in Greece on securities, within the meaning of Art. 2 L. 3401/2005 repeating the definition of securities set out in the respective provision of the Prospectus Directive, as amended by Directive 2010/73/EU. Thus, the operation of Crowdfunding platforms on investments which do not qualify as securities within the meaning of the Prospectus Directive is not subject to any license or other regulatory requirement under Greek law.

### 3.1.2 Lending Model

Although the Lending Model is not currently offered in Greece, the general rule is that according to Law 4261/2014 (implementing in Greek legislation EU Council Directive 2013/36/EC), the provision of loans or other credits, in a professional capacity, is allowed only to credit institutions and certain financial institutions (i.e. credit companies) licensed by BoG,

or alternatively to credit institutions and certain financial institutions established in other European Union (EU) countries having the benefit of the European “passport” to offer services either through a branch or on a cross-border basis without establishment in Greece. Third country credit institutions and financial institutions may operate and provide loans or other credits in Greece only by establishing a branch, which must be approved by the BoG, on conditions of reciprocity and provided, inter alia, that such activity is covered by their operation license issued in their country of origin.

### 3.1.3 Donations or Rewards Model

The structure of the Donations or Rewards Model is based on non-monetary returns/giveaways to the investors or on no return at all and no investment is involved. Based on said structure, the platforms operating this model are not considered to be offering investment or banking services and thus fall outside the scope of the relevant regulations.

## 3.2 Prospectus requirements

Law 3401/2005 implementing in Greece Directive 2003/71/EC (the “Prospectus Directive” as amended by Directive 2010/73/EE), provides that the public offer of securities in Greece requires the prior publication of a prospectus, which must be approved by the HCMC.

Following the enactment of law 4416/2016, the public offer of securities through Crowdfunding platforms operated by duly licensed firms is now explicitly exempted from prospectus publication requirements under the following conditions which have to be met cumulatively:

- The public offer must be performed exclusively through an electronic system (platform), operated by a 1) local investment firm (AEPEY) licensed to provide at least the investment services of a) reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments and b) the ancillary service of safe-keeping and administration of financial instruments on behalf of clients, including custody and related services, such as money and collateral administration or 2) a local alternative investment fund manager (AEDOOE) licensed to provide the ancillary (non-core) services of a) provision of investment advice, b) safe-keeping and administration in relation to shares or units of collective investment undertakings (UCITs) and c) reception and transmission of orders in relation to financial instruments or 3) a credit institution licensed to provide the investment service of reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments.
- The total value of the securities offered must be less than five hundred thousand Euro (EUR 500,000.00) per issuer per year; and
- The participation of an individual (a non-professional) investor cannot exceed the amount of five thousand Euro (EUR 5,000.00) and in any case ten percent (10%) of the average of their declared income of the past three years, per issuer, and the amount of thirty thousand Euro (EUR 30,000.00) per year, per AEPEY or credit

institution. The latter condition is entered so that the investment risk for investors is reduced or spread.

As regards the offers of investments which do not qualify as “securities” or other regulated products (such as UCITs or deposits etc), within the meaning of Law 3401/2005, these are not subject to any regulatory requirements.

### **3.3 Regulation of Crowdfunding under the AIFMD regime**

In Greece, Directive 2011/61/EE on Alternative Investment Funds Managers (“AIFMD”) has been implemented through the Law 4209/2013 (the “AIFMD Law”).

According to Article 4 of the AIFMD Law, an AIF is defined as any collective investment under-taking, including investment compartments thereof, which:

- raises capital from investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and
- does not require authorisation pursuant to Article 4 of Law 4099/2012 on UCITS or pursuant to Article 5 of Directive 2009/65/EC (UCITS).

On the basis of the aforementioned definition, Crowdfunding platforms could be subject to the provisions of the AIFMD law, if they qualify as collective investment undertakings which raise capital from investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors and are not UCITS. Under the AIFMD Law, the management of an AIF in Greece is currently subject, apart from certain exemptions set out in Article 3 and to the transitional provisions set out in Article 53 of AIFMD Law, to the prior authorization from the HCMC or other EU competent authority.

### **3.4 License under the Payment Services Directive**

As a general rule, any transfer of funds made by the operators of Crowdfunding platforms to the companies/projects could constitute money remittance services within the meaning of law 3862/2010 implementing Directive 2007/64/EC on payment services. Such transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform who then passes the funds to the entrepreneur.

The provision of payment services in Greece is a regulated activity that may only be undertaken by specific categories of service providers, which are subject to prudential supervision, such as banks, e-money institutions, payment institutions etc. Companies which provide payment services in Greece are required either to be licensed as payment services providers by the BoG or to be duly passported (i.e. operating through a Greek branch or on a cross-border basis).

It is not clear whether the platform operator could rely on the exemption for commercial agents under point b) of article 3 of Law 3862/2010. The applicability of such exemption should be confirmed with the BoG on an ad hoc basis.

As an alternative – in order to avoid such licensing requirements – the operator of a Crowdfunding platform could use an external provider or partner for processing payments rather than acting as an intermediary itself. However, even in this case the structure should be coordinated in cooperation with the BoG.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Law 3691/2008 on money laundering prevention;
- Laws 2472/1997 and 3471/2006 on data protection;
- Law 2251/1994 on consumer protection and sales performed from a distance;
- Law 2121/1993 on intellectual property;
- Law 3862/2010 on payment services.

## 4 Regulatory barriers for Crowdfunding crossing borders

The recently introduced legislative framework for the public offer of securities through Crowdfunding platforms and the exemption of such offer from the prospectus publication requirements, under certain conditions, applies only to offers of securities which take place in Greece. Accordingly, any offer of securities which is made through a Crowdfunding platform operating in Greece in another state, including another EU member state is subject to the laws of the specific state and therefore may not benefit from the specific exemption provided by law 4416/2016.

Equally, a Crowdfunding platform operating in another EU member state or a third country, through which an offer of securities is made to investors in Greece must meet the requirements of law 4416/2016 in order to benefit from the exemption of the prospectus publishing requirement.

It is noteworthy that the operation of Crowdfunding platforms which are addressed to investors in Greece and benefit from the prospectus publishing exemption of law 4416/2016 is currently allowed only to local investment firms, investment fund managers and credit institutions licensed to provide the investment service of reception and transmission of orders. Thus, any offer of securities which is made in Greece by a Crowdfunding platform operated by an investment firm or an investment fund manager or a credit institution which is licensed in another EU member state and is passported to provide the investment service of reception and transmission of orders in Greece may not benefit from the prospectus publishing exemption of law 4416/2016 and is therefore subject to the general provisions of law 3401/2005 on public offers.

Therefore, the new bespoke regime introduced in Greece for investment-based Crowdfunding has a limited scope of application, covering only offers of securities made in

Greece through platforms operated by local investment firms, investment fund managers and credit institutions.

#### 4.1 Applicable law

The HCMC has not officially expressed an opinion on when a public offer is taking place in Greece and/or when investment services are provided in Greece.

However, the HCMC seems to follow an investor-based approach, according to which if an offer of securities is addressed to investors in Greece (i.e. the documents are in Greek, the domain name is Greek etc.), then such offer is subject to the Greek law prospectus requirements. Equally, if an investment services provider targets clients in Greece for the provision of investment services, such as investment advice (in the case of investors) or placement of securities (in the case of issuers), such provider will be subject to Greek rules on the provision of investment services in Greece.

#### 4.2 Inbound

##### 4.2.1 Crowdfunding platform from another EU country addresses investors in Greece

In case a crowdfunding platform from another EU country addresses investors in Greece, it will be subject to the regulatory restrictions set out in section 3 related to the provision of investment services and the public offer of securities in Greece.

If such platform is operated by: a 1) local investment firm (AEPEY) licensed to provide at least the investment services of a) reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments and b) the ancillary service of safe-keeping and administration of financial instruments on behalf of clients, including custody and related services, such as money and collateral administration or 2) a local alternative investment fund manager (AEDOEE) licensed to provide the ancillary services of a) provision of investment advice, b) safe-keeping and administration of UCIT shares or units and c) reception and transmission of orders in financial instruments or 3) a credit institution licensed to provide the investment service of reception and transmission of orders on behalf of clients for the execution of transactions in financial instruments, such platform may benefit from the exemption of law 4416/2016 from the prospectus publishing requirements provided that the conditions of law 4416/2016 are met.

On the other hand, a Crowdfunding platform operating in another EU member state or a third country, which presents offers of investments other than securities is not currently subject to regulatory restrictions.

##### 4.2.2 Crowdfunding platform from another EU country addresses companies/projects in Greece

In case a Crowdfunding platform from another EU country addresses companies/projects in Greece, it will be subject to the regulatory restrictions set out in section 3 related to the

provision of investment services in Greece. It is not clear whether the passport for providing the services of reception and transmission of investment orders in Greece will be sufficient for Crowdfunding platform from another EU country addressing companies/projects in Greece or whether the HCMC will conclude that other investment services are also provided in connection with the operation of the Crowdfunding platform. The solicitation of companies/projects to participate in Crowdfunding platforms from another EU country may imply the provision of investment services (such as placement of securities without firm commitment) to such companies or not, depending on the services which are actually provided to such companies and whether such services are offered in relation to financial instruments or not.

### 4.3 Outbound

#### 4.3.1 Crowdfunding platform from Greece addresses investors in another EU country.

In case a Crowdfunding platform from Greece which benefits from the exemption from the Greek public offer rules recently introduced by law 4416/2016 addresses investors in another EU country, it will be subject to the securities laws applicable in such country on public offers and on the provision of investment services. Although the operator of the Greek Crowdfunding platform will be a duly licensed investment firm or alternative investment fund manager or credit institution and will be able to passport its services (such as reception and transmission of investment orders) to such EU country), the offer of securities which will be made through such platform to such EU country will be still subject to the public offer restrictions of the relevant EU country.

#### 4.3.2 Crowdfunding platform from Greece addresses companies/projects in another EU country

In case a Crowdfunding platform from Greece which benefits from the exemption from the Greek public offer rules recently introduced by law 4416/2016 addresses companies/projects in another EU country, it will be subject to the rules of the relevant EU country on the provision of investment services. Although the operator of such platform will be a duly licensed investment firm or alternative investment fund manager or credit institution and will be able to passport its services to such EU country, the solicitation of companies/projects to participate in the platform may involve the provision of one or more investment services, for which the operator does not have a license. For example, the operator of the Crowdfunding platform from Greece will be necessarily licensed to provide the service of reception and transmission of investment orders in financial instruments whereas the services which will be provided to companies which participate in the platform may be classified as the investment service of placement of financial instruments without firm commitment. This is, in our opinion, one of the handicaps of the new bespoke regime in Greece for investment-based Crowdfunding, i.e. the fact that the legislator is focused on the investment services which may be provided by the operator of the platform to investors and remains silent on the investment services that the operator usually provides to the companies/issuers. It may also be the case that the other EU

country has adopted a bespoke regime for the operation of Crowdfunding platforms, in which case the Greek platform will have to comply with the requirements of such regime.

It goes without saying that the classification and the characterization of the services that the operator of the platform is providing to companies/issuers in another EU member state will be made by the competent regulatory authority of such EU member state.

On the other hand, companies/projects from another EU country which will participate in the Greek platform may well benefit from the exemption from the Greek public offer rules under the conditions of law 4416/2016.

#### **4.4 Impact of EU regulation**

##### **4.4.1 Prospectus rule / regimes**

The prospectus regime regarding the offering of securities is harmonized on a pan-European level since the Prospectus Directive (and in the near future the Prospectus Regulation) and the implementing Greek legislation only covers transferable securities within the meaning of MiFID / MiFID II.

In Greece, most of the companies which have demonstrated interest to participate in Crowdfunding platforms are organized in the form of a company limited by shares (“anonymi etairia”) and the shares of such companies are classified as transferable securities. The Greek bespoke regime has introduced an exemption from the prospectus regime, under conditions but only for offers addressed to investors in Greece.

There are, however, other types of companies which are organized in the form of partnerships. Such companies are not covered by the European prospectus regulation but there are currently no domestic regulatory restrictions in the public offer of investment in such companies.

##### **4.4.2 AIFM-Directive**

The interpretation whether there exists a collective investment undertaking (and therefore an AIF) or not remains with the respective local authorities (e. g. HCMC in Greece). It cannot be excluded that if a local supervisory authority comes to the conclusion that an entity is not considered as an AIF, another local supervisory authority might come to another conclusion and classify this company / project as an AIF.

Further, also the fact that the definition and the requirements regarding retail AIF are not harmonized on a European level might lead to frictions in the intensity of regulation: In some EU member states there exist lower / higher regulation for retail AIF whereas in some EU member states, retail AIF are completely prohibited. AIFs may not be currently marketed to retail investors in Greece.

#### 4.4.3 MiFID / MiFID II

The main scope of application of MiFID and MiFID II for Crowdfunding in Greece is the general possibility to apply for a MiFID (II) licence to generally operate in each EU member state.

However, as mentioned above the service of reception and transmission of investment orders, on which law 4416/2016 has focused, does not seem to cover the investment services that the operators will be actually providing to companies/projects. In addition to the above, each EU member-state may have adopted a bespoke regime covering services and investments which are out of scope of MiFID and MiFID II.

On the basis of the above, the MiFID passport of the operators of Greek platforms may prove to be insufficient in practice.

#### 4.4.4 PSD / PSD II

The Payment Services Directive was implemented in Greece by law 3862/2010. The Payment Services Directive II (entered into force in 2016) must be implemented by Greece until January 2018. Payment services in Europe are generally harmonized, but regarding the details there is still room for interpretation of the national legislators and (especially) financial regulation authorities which does not lead to a fully harmonized single market in Europe.

Regarding Crowdfunding, especially the money remittance services come into consideration:

Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services within the meaning of law 3862/2010. Such transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform which then passes the funds to the company / project.

Therefore, these two directives have a great impact for Crowdfunding regarding the transaction of the investments.

### 4.5 Summary

The currently applicable EU legislation is clearly not sufficient to cover the operation of Crowdfunding across Europe. Specific European legislation should be, in our opinion, adopted in order to create a level playing field for Crowdfunding operators and uniform protection of investors in the European Union.

## 5 Lessons learned from Greek regulation for a possible harmonized European Crowdfunding regulation

### 5.1 Role model (“dos”)

Taking into account the continuing financial crisis and the difficult access of start-up and small and medium companies to traditional sources of funding in Greece, the Greek legislator

recognizing the need for development of alternative sources of funding for such companies by introducing a bespoke regime for the operation of Crowdfunding platforms aiming to ensure primarily a minimum level of protection for investors.

Although law 4416/2016 has been recently enacted and has not been tested in practice yet, the following aspects could serve as a role model for a possible harmonized Crowdfunding regulation:

- Exemption of Crowdfunding from prospectus publication requirement
- Investors' minimum informational requirements

## 5.2 Aspects that should be avoided (“don’ts”)

On the other hand, the following aspects should not be, in our opinion, inherited by a harmonized European Crowdfunding regulation:

- Operation of platforms only by licensed investment firms, alternative investment fund managers and credit institutions
- Disproportionate regulatory costs compared to the potential profit from the operation of the platform
- Vagueness regarding organizational requirements of platform operators

## 6 Conclusion

In conclusion, measures should be adopted at European legislative/administrative level establishing a specific exemption of Crowdfunding platforms from most regulatory requirements, including prospectus and MiFID licensing requirements but ensuring at the same time minimum investors protection requirements.

## 7 Summary - Crowdfunding regulation

| Country  | Greece  |
|--|---|
| Summary  |   |
| Recent developments in Crowdfunding regulation   | <p>Law 4416/2016 came into force on September 6, 2016, enabling the public offering of securities through equity Crowdfunding platforms without a prospectus, so long as the platforms are operated by licensed investment firms, local AIFMs following prior notification to the HCMC or the BoG, respectively.</p>  |
| <b>Current / planned Crowdfunding regulation</b> |   |
| General regulation                               | <p><u>Equity Model</u>: Equity Crowdfunding platforms through which securities are offered, can be operated only by local licensed investment firms (namely AEPEY, AIFMs or credit institutions) which are licensed by the HCMC or the BoG respectively, provided that:</p> <ul style="list-style-type: none"> <li>(a) they notify in advance to the HCMC or the BoG their intention to operate such platforms and provide adequate information thereto on the way the activity is organized and will be performed;</li> <li>(b) specific information regarding the issuers and their companies hosted in the platform is provided to the investors, so that the latter are duly informed.</li> </ul> <p><u>Lending Model</u>: The provision of loans or other credits can be performed only by licensed credit institutions and certain financial institutions, or alternatively by “passported” financial institutions established in other EU countries that offer their services either through a branch or on a cross-border basis without establishment in Greece.</p> <p><u>Rewards or Donation Model</u>: platforms may not be considered to be offering investment or banking services -&gt; no regulatory requirements.</p> |
| Prospectus requirement                           | <ul style="list-style-type: none"> <li>• As a principle, the public offer of securities in Greece requires the prior publication of a prospectus, which must be approved by the HCMC.</li> <li>• Exceptionally, no prospectus is required for the public offer of securities through Crowdfunding platforms operated by duly licensed firms when: <ul style="list-style-type: none"> <li>- The public offer is performed exclusively through electronic platforms operated by AEPEYs or AEDOOEs or credit institutions (duly licensed to provide specific services),</li> <li>- Total value of securities offered: less than EUR 500,000.00 per issuer per year; and</li> <li>- Participation of an individual (non-professional) is equal or less than EUR 5,000.00 and in any case equal or less than 10% of the average of their declared income of the past 3 years, per issuer, and equal or less than EUR 30,000.00 per year, per AEPEY or credit institution.</li> </ul> </li> </ul>   |

|                                      |  |
|--------------------------------------|--|
|                                      | <ul style="list-style-type: none"> <li>The offer of investments which do not qualify as “securities” or other regulated products (such as UCITs or deposits etc) → not subject to regulatory requirements.</li> </ul>  |
| <b>AIFMD-regulation</b>              | <ul style="list-style-type: none"> <li>According to the definition of AIF in Law 4209/2013, Crowdfunding platforms could be subject to the provisions of the AIFMD law, if they qualify as collective investment undertakings which raise capital from investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors and are not UCITS.</li> <li>Under Law 4209/2013, the management of an AIF in Greece is currently subject, apart from certain exemptions, to the prior authorization from the HCMC or other EU competent authority.</li> </ul>   |
| <b>Payment service regulation</b>    | Transfer of funds made by operators of Crowdfunding platforms to companies/projects could constitute money remittance services within meaning of law 3862/2010 -> license is required, not clear whether commercial agent exemption applies  |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>Law 3691/2008 on money laundering prevention;</li> <li>Laws 2472/1997 and 3471/2006 on data protection;</li> <li>Law 2251/1994 on consumer protection and sales performed from a distance;</li> <li>Law 2121/1993 on intellectual property;</li> <li>Law 3862/2010 on payment services</li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <ul style="list-style-type: none"> <li><b>Foreign Crowdfunding platform addresses Greek investors</b> <ul style="list-style-type: none"> <li>Greek regulatory law is applicable since Greek investors are approached; The HCMC has not officially expressed its view as to when Greek investors are approached. The platform may benefit from the exemption of law 4416/2016 from the prospectus publishing requirements provided that the conditions of law 4416/2016 are met. This practically means that the operation of the platform must be performed by local investment firm or alternative investment fund manager or credit institution. Otherwise the platform may not benefit from the exemption of law 4416/2016.</li> <li>On the other hand, a Crowdfunding platform operating in another EU member state or a third country, which presents offers of investments other than securities, is not currently subject to regulatory restrictions.</li> </ul> </li> <li><b>Foreign Crowdfunding platform addresses companies/projects in Greece</b> <ul style="list-style-type: none"> <li>The solicitation of companies/projects to participate in Crowdfunding platforms from another EU country may imply the provision of investment services (such as placement of securities without firm commitment) to such</li> </ul> </li> </ul> |

|                                       |   |
|---------------------------------------|---|
|                                       | <p>companies or not, depending on the services which are actually provided to such companies and whether such services are offered in relation to financial instruments or not.</p>   |
| <p><b>Outbound</b></p>                | <ul style="list-style-type: none"> <li>• <b>Crowdfunding platform from Greece addresses foreign investors</b> <ul style="list-style-type: none"> <li>- In case a Crowdfunding platform from Greece which benefits from the exemption from the Greek public offer rules recently introduced by law 4416/2016 addresses investors in another EU country, it will be subject to the securities laws applicable in such country on public offers and on the provision of investment services.</li> <li>- Although the operator of the Greek Crowdfunding platform will be a duly licensed investment firm or alternative investment fund manager or credit institution and will be able to passport its services (such as reception and transmission of investment orders) to such EU country), the offer of securities which will be made through such platform to such EU country will be still subject to the public offer restrictions of the relevant EU country.</li> </ul> </li> <li>• <b>Crowdfunding platform from Greece addresses foreign companies/projects</b> <ul style="list-style-type: none"> <li>- In case a Crowdfunding platform from Greece which benefits from the exemption from the Greek public offer rules recently introduced by law 4416/2016 addresses companies/projects in another EU country, it will be subject to the rules of the relevant EU country on the provision of investment services. Although the operator of such platform will be a duly licensed investment firm or alternative investment fund manager or credit institution and will be able to passport its services to such EU country, the solicitation of companies/projects to participate in the platform may involve the provision of one or more investment services, for which the operator does not have a license.</li> <li>- It may also be the case that the other EU country has adopted a bespoke regime for the operation of Crowdfunding platforms, in which case the Greek platform will have to comply with the requirements of such regime.</li> <li>- On the other hand, companies/projects from another EU country which will participate in the Greek platform may well benefit from the exemption from the Greek public offer rules under the conditions of law 4416/2016.</li> </ul> </li> </ul> |
| <p><b>Impact of EU regulation</b></p> |   |
| <p><b>Prospectus regulations</b></p>  | <ul style="list-style-type: none"> <li>• Prospectus regime regarding the offering of securities is harmonized on a pan-European level since the Prospectus Directive (and in the near</li> </ul>  |

|                                |  |
|--------------------------------|--|
|                                | <p>future the Prospectus Regulation) and the implementing Greek legislation only covers transferable securities within the meaning of MiFID / MiFID II.</p> <ul style="list-style-type: none"> <li>• In Greece, most of the companies which have demonstrated interest to participate in Crowdfunding platforms are organized in the form of a company limited by shares (<i>anonymi etairia</i>) and their shares are classified as transferable securities.</li> <li>• The Greek bespoke regime has introduced an exemption from the prospectus regime, under conditions but only for offers addressed to investors in Greece.</li> <li>• Other types of companies organized in the form of partnerships are not covered by the European prospectus regulation but there are currently no domestic regulatory restrictions in the public offer of investment in such companies.</li> </ul> |
| <p><b>AIFM-Directive</b></p>   | <ul style="list-style-type: none"> <li>• Local authorities (in Greece the HCMC) responsible to interpret whether there exists a collective investment undertaking (and therefore an AIF) or not and thus an entity may be considered as an AIF by one domestic authority and not an AIF by another.</li> <li>• Requirements regarding retail AIF- not harmonized on a European level, which might lead to frictions in the intensity of regulation: In some EU member states there exist lower / higher regulation for retail AIF whereas in some EU member states, retail AIF are completely prohibited.</li> <li>• AIFs may not be currently marketed to retail investors in Greece.</li> </ul>  |
| <p><b>MiFID / MiFID II</b></p> | <ul style="list-style-type: none"> <li>• Main scope of application of MiFID and MiFID (II) for Crowdfunding in Greece is the general possibility to apply for a MiFID (II) license to generally operate in each EU member state.</li> <li>• However, the service of reception and transmission of investment orders, on which current law focuses, does not cover the investment services that the operators may be providing to companies/projects.</li> <li>• Also, each EU member-state may have adopted a bespoke regime covering services and investments which are out of scope of MiFID and MiFID (II).</li> <li>• Thus, the MiFID passport of the operators of Greek platforms may prove to be insufficient in practice.</li> </ul>  |
| <p><b>PSD / PSD II</b></p>     | <ul style="list-style-type: none"> <li>• The PSD already implemented by law in Greece.</li> <li>• PSD (II) must be implemented by Greece until January 2018.</li> <li>• Payment services in Europe are generally harmonized, but regarding the details there is still room for interpretation of the national legislators and (especially) financial regulation authorities—thus, there is no fully harmonized single market in Europe.</li> <li>• Regarding Crowdfunding, especially <b>money remittance services</b> are important:</li> </ul>   |

|  |   |
|--|---|
|  | <p>→ Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services within the meaning of Greek law which implemented the PSD;</p> <ul style="list-style-type: none"><li>• Great impact for Crowdfunding regarding the transaction of the investments.</li></ul> |
|--|---|

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# Gibraltar

## 1 Recent developments in the market of Crowdfunding in Gibraltar

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Although there have been no significant developments in the Gibraltar market in relation to the Equity Model during the last 12 months and the Equity Model not yet having any substantive presence in the Gibraltar market, there has been some work in assessing the options available within the jurisdiction for developing such a model. The regulatory regime for offering securities is currently subject to European regulation in the form of MiFID and the Prospectus Directive.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There are a small number of operators in the market currently operating a lending model. However there have been no significant developments in the Gibraltar market in relation to the Lending Model during the last 12 months.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

There were no significant developments in the Gibraltar market in relation to the Donations or Rewards Model during the last 12 months. The Donations or Rewards Model has a limited presence in the Gibraltar market, as local consumers are becoming increasingly aware and involved in funding projects which are governed by EU and third country regulatory frameworks and platform operators which are based outside of Gibraltar.

### 1.4 Real Estate Crowdfunding and Renewable Crowdfunding

There were no significant developments in the Gibraltar market in relation to Real Estate Crowdfunding and Renewable Crowdfunding. However, the Government currently investing in renewable energy projects, as well as providing tax concessions/reliefs to companies operating in this sector, with particular emphasis on solar energy. We therefore predict some possible momentum being gathered in the area of Renewable Crowdfunding over the next two to three years. Current construction projects are making use of photovoltaic cells as well as vertical gardens or “Green Walls” to reduce carbon footprint.

### 1.5 International Approach

Although there is discussion and certain enquiries have materialised from the UK market for entry into the Gibraltar market to establish Crowdfunding platforms, the lack of a pan-European harmonised regime is a barrier to automatic entry, and also to a platform operator seeking to establish itself in Gibraltar and operating on a wider pan-European basis.

## 1.6 Regulatory Guidance

The Gibraltar Financial Services Commission (GFSC) has published a set of questions and answers but no detailed guidance is available. However the GFSC does operate an Innovate division which meets and discusses possible applications on a case by case basis and is able to provide feedback and consider the specifics of any particular project.

## 1.7 Social Awareness

Although Gibraltar law generally follows UK law there is no equivalent to the specific regulated activity of ‘operating an electronic system in relation to lending’ as introduced in the UK under their Financial Services and Markets Act 2000. There is an awareness of Crowdfunding as an alternative financing solution for certain projects but no developed market.

## 2 Recent developments regarding Crowdfunding regulation in Gibraltar

There are no specific recent developments regarding Crowdfunding regulation that have taken place in Gibraltar during the last 12 months. However, there has been some legal analysis in respect of the UK regime, and whether an equivalent Gibraltar regime could be developed in Gibraltar as a primarily UK facing platform. This would be primarily in respect of the lending model, and on the basis that the operation of the platform itself would not be subject to UK rules if conducted from Gibraltar, and that promoting loans to consumer borrowers or communicating financial promotions (which would require a local presence) could be carried out through an established network of specialist credit brokers, debt administrators, collectors and other service providers. It is possible that in a post Brexit scenario, and subject to the various implications and possible eventual outcomes that Gibraltar could develop itself as an entry point to the UK in this and other markets.

## 3 Current Regulation of Crowdfunding in Gibraltar

### 3.1 How the Crowdfunding models fit into Gibraltar’s regulatory regime

#### 3.1.1 Equity Model

Crowdfunding platforms under this Model may be perceived as offering “*financial instruments*”, as defined in Schedule 1 of Gibraltar’s Financial Services (Markets in Financial Instruments) Act 2006 (the “MiFI Act”), which include, *inter alia*, transferable securities and units in collective investment undertakings. Transferable securities could be stocks, bonds and other debt or equity securities, and from a Crowdfunding perspective, a platform operator may well be requested to act as a facilitator for the transfer of such securities issued by companies seeking to raise finance from Crowdfunding. In these circumstances it is highly likely the platform operator would be required to be suitably licenced under the Financial Services (Investment and Fiduciary Services) Act (the “FS Act”), which is the principal Act in Gibraltar under which most financial services providers are licenced to carry out “*controlled*

*activities*” and regulated by one of the main independent Regulatory Authorities in Gibraltar—the Gibraltar Financial Services Commission (the “GFSC”).

As Crowdfunding begins to gather momentum in Gibraltar, a key consideration for platform operators should also be that they are not seen to be offering investment advice, as this is also a controlled activity and within the ambit of the FS Act and the MiFID Act.

Parallel to the above, a platform operator may not necessarily be advising but may be considered to be purely as a mediator or arranger; notwithstanding this it could be perceived to be actively managing investors’ money, and automatically invests their money (using its own discretion, even if under the terms of an open mandate or other Crowdfunding agreement) then it may fall under the Financial Services (Collective Investment Schemes) Act 2011 (the “CIS Act”) and therefore be regulated as a collective investment scheme provided that it is a collective investment undertaking with the aim of raising capital for a number of investors in accordance with a defined investment policy

### 3.1.2 The Lending Model

The Lending Model includes peer-to-peer (“P2P”) lending, peer-to-business (“P2B”) lending, business-to-peer (“B2P”) lending and finally business-to-business (“B2B”) lending. All these forms of Crowdfunding have a market in Gibraltar which is still developing with a few operators, but because of a lack of bespoke regulation in this area, each of these sub-categories of lending will be subject to different rules and regulations.

Unsurprisingly, P2P lending is the type of lending most susceptible to regulation in Gibraltar, as it most often involves what is effectively the general public; namely, inexperienced investors lending directly –albeit via a platform operator acting as intermediary– to entrepreneurs subject to little or no regulation in their chosen markets. Lending in this manner and the method of regulation in Gibraltar does not derogate from the basic EU framework of Directives mentioned herein and the relevant local laws that apply these. In other words there is no bespoke regulation of the Lending Model in Gibraltar, and this form of Crowdfunding’s susceptibility to regulation is therefore dependent on how consumers (lenders and borrowers) are approached, how the platform operator structures itself, and how it actually transfers the debt securities.

Again, the CIS Act may apply to the Lending Model subject to the same conditions being satisfied as described above.

Under the Lending Model, a platform operator may also be required to hold funds received from lenders for varying lengths of time whilst it locates suitable borrowers. Such funds are categorised as client money and various safeguards are imposed by local legislation to ensure the protection of consumers and of the good reputation of Gibraltar.

The local framework is largely comprised of regulations made under the FS Act, including the Financial Services (Accounting & Financial) Regulations 1991 (the “FSAF Regulations”), but the FSAF Regulations and the FS Act only apply to entities licenced by the GFSC to carry

out *controlled activities* as specified in Schedule 3 of the FS Act. Persons exempted from such regulations that frequently hold client monies (such as legal firms for example) are governed by the rules of their relevant oversight or other professional body and/or regulator. The common denominator is the concept of customer or client money being held on trust and therefore platform operators should ensure that adequate safeguards are in place, regardless of whether they can innovative ways to escape the regulatory net, as they will still be subject to equitable principles of common law applicable in Gibraltar, as well as the full extent of the criminal law if they mishandle any client monies.

### 3.1.3 Donations or Rewards Model

There is no regulation of the Donations or Rewards Model in Gibraltar

There is an argument that certain rewards based Crowdfunding projects could qualify as investment products, depending on the manner in which they are marketed and the type of instrument used in the project. The GFSC has not yet made any official statement over this issue and will likely treat licencing on a case by case basis.

## 3.2 Prospectus requirements

Under certain circumstances, the Gibraltar Prospectuses Act 2005 (the “Prospectuses Act”) may subject undertakings and/or intermediaries who are offering or issuing securities, or marketing investment products to the public to a requirement to publish a prospectus which meets the minimum requirements prescribed by the Prospectuses Act, and which must be approved by the GFSC before any marketing takes place.

Under section 6 of the Prospectuses Act, certain types of offers are not deemed to be offers of securities to the public:

- offers addressed only to qualified investors
- offers addressed to fewer than 150 persons (other than qualified investors) per Member State
- where the minimum consideration payable by any person for the offer is at least EUR 100,000 (or other currency equivalent)
- where the total consideration payable in the European Union is less than EUR 100,000 which limit is calculated over a period of 12 months
- where the actual securities themselves are denominated in amounts of at least EUR 100,000 (or other currency equivalent)

Placing these obligations in the context of Crowdfunding, one may appreciate that most forms of Crowdfunding where no more than EUR 100,000 is raised by the Crowdfunding platform per person may indeed fall outside the scope of the Prospectuses Act. However, section 4 of the Prospectuses Act is also relevant here, as it lists more specifically the types of instruments that fall outside the scope of this piece of legislation:

- units issued by collective investment undertakings other than the closed-end type

- non-equity securities (think Lending Model) by a regional / local authority, public international body, by the European Central Bank or central banks of Member States
- shares in the capital of central banks of the Member States
- securities unconditionally and irrevocably guaranteed by a Member State or by one of a Member State's regional or local authorities
- securities issued by associations with legal status or non-profitmaking bodies to achieve their non-profitmaking objectives
- non-equity securities issued in a continuous or repeated manner by credit institutions (subject to further caveats e.g. subordination not being allowed, must not link to a derivative instrument)
- non-fungible shares of capital whose main purpose is to provide the holder with a right to occupy immovable property or a part thereof, where the shares cannot be sold on without this right being given up
- securities included in an offer where the total consideration of the offer in the European Union is less than EUR 5,000,000, which limit shall be calculated over a period of 12 months
- “*bostadsobligationer*” issued repeatedly by credit institutions in Sweden whose main purpose is to grant mortgage loans (subject to further caveats e.g. terms and conditions of the “*bostadsobligationer*” are not changed during the issuing period)
- non-equity securities issued in a continuous or repeated manner by credit institutions where the total consideration for the offer in the European Union is less than EUR 75,000,000, which limit shall be calculated over a period of 12 months (subject to further caveats e.g. subordination not being allowed, must not link to a derivative instrument)

Regardless of whether the Prospectuses Act applies a Prospectus may nevertheless be recommended and an offer or a person asking for admission to trading on a regulated market shall be entitled to draw up a prospectus as stated in Section 4(3).

Therefore a Crowdfunding platform will find additional hurdles in the Prospectuses Act; not all have been covered here. ISOLAS can provide further assistance where there is any doubt over whether a prospectus is required.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

The Alternative Investment Fund Managers Directive 2011/61/EU (“AIFMD”) was transposed into Gibraltar legislation via the Financial Services (Alternative Investment Fund Managers) Regulations 2013 (the “AIFM Regulations”). The European Commission has supplemented the AIFMD with a Delegated Regulation, more commonly known as the level 2 implementing measures (Level 2) which also applies to Gibraltar.

The definition of an Alternative Investments Funds (AIF) is contained in section 4 of the AIFM Regulations. Essentially an AIF is defined as:

*“a collective investment undertaking (including any investment compartments) which–*

- A. Raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and*
- B. [is not a UCITS]”*

Given AIFMD and the AIFM Regulations are designed to regulate fund managers (“AIFMs”), this definition is also worth noting:

*“AIFM” means a legal person whose regular business is managing one or more AIFs*

The wide scope of these definitions, coupled with the divergent Models of Crowdfunding, we would not rule out the possibility that a platform operator could be acting as an AIFM under certain circumstances; the Equity Model is particularly relevant here, as the method of raising capital from investors could be interpreted as an AIF under a number of circumstances where there are no applicable exemptions or carve outs available.

We would conclude that Crowdfunding under the Equity Model is likely to be caught by this definition in Gibraltar and we have dealt with various other potential applications where ultimately the view formed in Gibraltar was that the proposed business would be captured under AIFMD. One of the reasons for this is that the exemption available in certain jurisdictions in respect of body corporates was not available at the time. However, Gibraltar has also developed an ‘out of scope’ small AIFM regime which could in principle be used were the platform to be captured by the definition of an AIF, so long as the assets in question were below the thresholds defined under AIFMD.

### **3.4 Regulation under the Payment Services Directive (and implementing local regulation)**

The Payment Services Directive (2007/64/EC) became law in Gibraltar via the Financial Services (EEA) (Payments Services) Regulations 2010, and has been amended by the Financial Services (EEA) (Payment Services) (Supplemental) Regulations 2015 (together, the “Payment Services Regulations”). The Payment Services Regulations cover all types of electronic and non-cash payments – credit transfers, card payments (including credit card payments), direct debits; standing orders, money remittance, mobile payments, and online payments; they therefore do not cover cash and cheque payments. Platform operators who make a market using electronic and non-cash payments will therefore fall under the remit of the Payment Service Regulations, and could be seen to be acting as custodians and further subject to applicable requirements.

### 3.5 Possible additional regulatory scope

#### 3.5.1 Consumer Credit

The Consumer Credit Directive 2008/48/EC has been transposed into local legislation through Gibraltar's Financial Services (Consumer Credit) Act 2011 (the "Consumer Credit Act") with effect from 16th June 2011.

If a Crowdfunding platform is providing loans to consumers exceeding EUR 200 but less than EUR 75,000 to individuals for purposes which are outside trade, business or profession, and not in relation to the purchase of immovable property (as well as certain other exceptions contained in the Consumer Credit Act) then the platform operator could be required to be licenced by the Government of Gibraltar under the Financial Services (Moneylending) Act (the "Moneylending Act". Both the Consumer Credit Act and the Moneylending Act contain various restrictions and prohibitions with regard to protection of consumers, such as how a lender may advertise, the content of credit agreements and other information to be provided, the use of specific calculations in reaching an annual percentage rate, provisions on assignments of debt and cancellation rights to name a few.

#### 3.5.2 Additional relevant Gibraltar legislation

In addition to the above pieces of primary (Acts) and secondary legislation (Regulations), Crowdfunding platform operators would be subject to several more of these as well as guidance issued by Gibraltar Financial Services Commission. Below are the ones we believe to be most relevant but the list is not exhaustive by any means.

- Companies Act 2014
- Data Protection Act 2004
- Proceeds of Crime Act 2015
- Terrorism Act 2005
- "Guidance Notes on Systems of control to prevent the financial system from being used for money laundering or terrorist financing activities" (more commonly referred to as the "FSC's AML Guidance Notes") published by Gibraltar Financial Services Commission
- The Electronic Commerce Act 2001
- The Fair Trading Act 2015

### 3.6 EU regulation and influence over local regulation

For the avoidance of doubt, unless otherwise specifically stated the above Acts are all sourced from EU Directives and other sources of European Community law, which such modifications as are necessary to take into account Gibraltar's circumstances whilst remaining compliant with the basic requirements of EU membership and adhering to the standard expected (or a higher standard where possible) by the EU from its members following the transposition / adoption process.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

Gibraltar law mirrors UK law to a large extent. UK common law as well as Gibraltar common law applies, together with persuasive authority from the Commonwealth jurisdictions such as Canada, New Zealand etc.

Financial regulation law applies to entities performing controlled activities as defined in the FS Act, as well as other key pieces of legislation aimed at regulating the banking and insurance sectors. The decisive factors in what law applies is ultimately determined by which Crowdfunding Model is used and particularly what investors and/or consumers are targeted and the manner in which they are targeted as described in section 3 above.

Gibraltar taxation applies on a territorial basis on income accrued in Gibraltar and/or derived from Gibraltar sources. Gibraltar benefits from exemption from the customs union which means there is no VAT and this together with a low corporate tax rate of 10% and no capital gains, withholding, wealth or inheritance tax as well as other attractive tax concessions and specialist regimes aimed at attracting high net worth individuals (“HNWIs”) and high executive possession specialists skills (“HEPSS”). We remain hopeful that such incentives will encourage platform operators to relocate and set up business in the jurisdiction.

### 4.2 Inbound

#### 4.2.1 Crowdfunding platform from another EU country addresses investors in Gibraltar

Depending on the kind of activity that is deemed to be taking place in Gibraltar, and the type of offer **being made, there are a number of possible implications for a platform that is deemed to be making** an offer to investors in Gibraltar. This would need to be considered on a case by case basis.

##### 4.2.1.1 Barriers for Crowdfunding platforms addressing Gibraltar investors

The most likely barriers for foreign Crowdfunding platforms marketing to Gibraltar investors are going to be from a MiFI Act perspective as touched upon in 3.1 above, where financial advice is deemed to be given, and licencing with the GFSC would be required. Gibraltarian regulatory law could extend to the Crowdfunding platform itself and/or the company/project seeking the funding. For the Crowdfunding platform it would be licencing and compliance obligations that would be applied and for the company it would be prospectus and information obligations.

If the Crowdfunding platform is licenced under MiFID, then it will be able to take advantage of the EU passporting capability and conduct business in Gibraltar without applying for a licence and without having a presence in Gibraltar. If it has no such authorisation in another EU Member State then as stated above, it would need to apply for a licence.

#### **4.2.1.2 Barriers for companies / projects addressing Gibraltar investors**

The prospectus regime under the Prospectuses Act (see 3.2 above) is likely to apply here and this depends on whether the foreign company / project offers transferable securities or other financial products – i.e. the key question becomes “is the entity offering or issuing securities, or marketing investment products to the public?” If so a prospectus must be prepared.

#### **4.2.2 Crowdfunding platform from another EU country addresses companies / projects in Gibraltar**

As above, depending on the kind of activity that is deemed to be taking place in Gibraltar, and the type of offer being made, there are a number of possibly implications for a platform that is deemed to be making an offer to investors in Gibraltar. This would need to be considered on a case by case basis.

##### **4.2.2.1 Barriers for Crowdfunding platforms addressing Gibraltar companies / projects**

Although there is only a limited number of Crowdfunding companies / projects for an EU Crowdfunding platform to address in Gibraltar, if a hypothetical approach were to be made, then the key difference is that licencing considerations are unlikely to apply if Gibraltarian investors are not being approached. Gibraltar law could apply in the scenario that the Gibraltar FSC feel that Gibraltar investors are being approached but there are no defining criteria that determine when this is taking place. If investment opportunities are being marketed or presented to Gibraltar investors specifically, that relate to securities or equity interests it is possible that the platform could be deemed to be conducting a licencable activity in Gibraltar.

##### **4.2.2.2 Barriers for companies / projects addressing Gibraltar companies / projects**

The Prospectuses Act will apply only to the extent addressed in 4.2.1.2 above.

### **4.3 Outbound**

#### **4.3.1 Crowdfunding platform in Gibraltar addresses investors in another EU country**

Given that there are a limited number of Crowdfunding platforms in Gibraltar and the market is not specifically unregulated, the lack of regulation, and the lack of a pan-European regime or passport is in and of itself a practical and regulatory barrier that discourages platforms from setting up in Gibraltar.

##### **4.3.1.1 Barriers for (hypothetical) Crowdfunding platforms addressing investors in another EU country**

Hypothetically speaking, if a Crowdfunding platform were to set up in Gibraltar, regulatory barriers would arise in much the same way as above; ultimately it would depend

on the type of Crowdfunding Model used. In an Equity Model Crowdfunding it is likely to be caught under the MiFI Act discussed in 3.1 and 4.2.1.1 above; in a Lending Model it will be caught by the additional licencing layer of the Government of Gibraltar for moneylenders as discussed in 3.5 above.

#### **4.3.1.2 Barriers for Gibraltar companies / projects addressing investors in another EU country**

Carrying out investment advisory activities in or “from within” Gibraltar also constitutes licencable activity and simply because an entity is addressing non-Gibraltar investors does not mean it is outside the regulatory remit of the GFSC. Again, if the company is offering transferrable securities then the Prospectuses Act regime will apply to the extent addressed in 4.2.1.2 above.

#### **4.3.2 Crowdfunding platform in Gibraltar addresses companies / projects in another EU country**

As above, depending on the kind of activity that is deemed to be taking place in Gibraltar, and the type of offer being made, there are a number of possible implications for a platform that is deemed to be making an offer to investors, even if those investors are based outside Gibraltar in another EU country. This would need to be considered on a case by case basis.

It is important to note that there are only a limited number of Crowdfunding companies or projects in Gibraltar as the law has not yet developed sufficiently in this area.

##### **4.3.2.1 Barriers for (hypothetical) Crowdfunding platforms addressing companies/projects in another EU country**

A Crowdfunding platform that wishes to establish itself in Gibraltar, perhaps to take advantage of tax benefits not offered in other Member States (see 4.1 above), would find regulatory barriers when attempting to do so. It would likely need to be licenced depending on the activity it is undertaking, and as discussed above in 3.1 and 3.5, the relevant licence(s) will need to be issued under one or more of the following Acts:

- MiFI Act
- CIS Act
- Prospectuses Act
- Consumer Credit Act
- Moneylending Act

##### **4.3.2.2 Barriers for Gibraltar companies / projects addressing EU (and domestic) companies/projects**

The Prospectuses Act will apply only to the extent addressed in 4.2.1.2 above. A key concept here is not whether the companies are located in Gibraltar or abroad, but the type of instrument / transferrable security (e.g. debt-security or subordinated profit-participating loan, shares etc.) being offered. This will be treated on a case by case basis and it is highly

likely that the Prospectuses Act will be triggered in the majority of cases. As mentioned above, ISOLAS is pleased to offer assistance to those making this determination.

#### **4.4 Impact of EU regulation and Summary**

##### **4.4.1 Prospectus regime**

In Gibraltar, following implementation of the Prospectus Directive (and upcoming Prospectus Regulation) via local implementing regulations, there is limited scope given that the regulation only covers transferrable securities within the meaning of MiFID / MiFID II; several threshold exceptions also exist that would avoid the requirement to issue a prospectus.

##### **4.4.2 AIFM-Directive**

As stated above, Gibraltar's AIFM Regulations implement the wide-ranging definitions of AIF and AIFM and mainly affects Equity Model Crowdfunding, and particular attention has to be given as to whether an investment strategy is in place and whether a collective investment scheme has been created which would fall under the Gibraltar CIS Act or AIFMD.

##### **4.4.3 MiFID / MiFID II**

The main scope of application of MiFID and MiFID II for Crowdfunding in Gibraltar is the general possibility to apply for a MiFID (II) licence to generally operate in each EU member state. However this would only apply to certain activities and certain elements of Crowdfunding activity.

##### **4.4.4 PSD / PSD II**

As stated above the PSD applies via the Financial Services (EEA) (Payments Services) Regulations 2010, as amended by the Financial Services (EEA) (Payment Services) (Supplemental) Regulations 2015 (together, the "Payment Services Regulations"). Transfer of funds by electronic means through platform operators where there is non-cash/cheque consideration generally constitute money remittance services. A key question not answered by the GFSC is whether such operators will benefit from any exemptions as commercial agents. What is clearer is that adequate safeguards will be needed to ensure a harmonious compliance with the well-established pan-European payment services and money remittance framework already in place.

#### **4.5 Summary**

EU regulation currently provides the framework that typically governs Crowdfunding activity in Gibraltar. Elements of the Prospectus Directive, AIFMD, MiFID/MiFID II and PSD/PSD II are all relevant in capturing activity that falls within the Crowdfunding umbrella, highlighting in and of itself the importance for a small jurisdiction in having such a framework built at an EU level.

## 5 Lessons learned from Gibraltar regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model (“dos”)

There are currently no lessons that may be learned from Gibraltar’s regulation for a possible harmonised European Crowdfunding regulation.

### 5.2 Aspects that should be avoided (“don’ts”)

There are currently no lessons that may be learned from Gibraltar’s regulation for a possible harmonised European Crowdfunding regulation.

## 6 Conclusion

In conclusion, the need for a pan-European regime has become increasingly clear. However for Gibraltar, the focus will be to mould a regime that is UK facing and ensures continued access to the UK market within a competitive environment. Crowdfunding in Gibraltar is expected to increase in certain areas. In our view, at present Gibraltar’s regulatory requirements are likely to capture Equity and Lending Model Crowdfunding, but not within a specifically defined. In addition we would comment that;

- Depending on the manner in which the platform operator is structured it could be subjected to payment services and consumer credit requirements
- Depending on the manner in which the platform operator offers its service and targets consumers, it could be subject to prospectus requirements, and also be carrying out licencable “controlled activity” in the areas of collective investment undertakings and/or MiFI-type activity.
- Depending on the manner in which the platform operator holds money it could be subjected to custodial service requirements.

Given the current regulatory landscape is still in its embryonic stage, Crowdfunding platforms would have no access to compensation schemes in Gibraltar. The financial services regulator, the GFSC, therefore encourages any prospective platform operators and also consumers to err on the side of caution and if unsure about whether a proposed Crowdfunding activity would constitute licencable activity one should seek legal or professional advice in order to determine this, as ultimately it is the firm’s responsibility to ensure that, if required, it obtains the relevant authorisation(s).

Given its small size, its base as a financial services jurisdiction, its access to Gibraltar and its speed to market, Gibraltar is well positioned to develop a Crowdfunding community.

Gibraltar also has the benefit of hindsight from the observable developments in other EU and non-EU jurisdictions where Crowdfunding appears to resemble a *cul-de-sac*; although partially regulated and giving the appearance of a harmonised regime in some respects, certain jurisdictions have become partly inward looking. Gibraltar not only has the advantage of having a blank canvass in how it chooses to regulate Crowdfunding, but also how it can

potentially develop this regime in a post-Brexit environment to cater for the UK market as well as the Single Market. Of course, it is difficult to predict at this stage how the Single Market will react after the UK (and with it Gibraltar) finally does exit, but the silver lining here has to be the ability for Gibraltar to ensure UK access which may be significant in the event that the passporting of services out of (and therefore into) the United Kingdom is not available.

Indeed there is scope for Gibraltar to create a straightforward and proportionate regulatory regime which compares favourably to the UK regime and focuses on any perceived issues that exist with that existing framework, as well as a favourable tax regime for the market players and market makers in this space.

## 7 Summary – Crowdfunding regulation

| Country   | Gibraltar   |
|---|---|
| <b>Summary</b>  |   |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Appetite for Crowdfunding is beginning to emerge; local events and marketing initiatives have been held.</li> <li>• no recent developments in the area of Crowdfunding regulation in the last 12 months</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |   |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Where Crowdfunding platform offers securities to the public,</li> <li>• authorisation under Financial Services (Investment and Fiduciary Services) Act for “controlled activities” as defined in Schedule 3 thereof.</li> <li>• Relevant regulator is the Gibraltar Financial Services Commission (“GFSC”)</li> <li>• Additional licencing may be required from Government in respect of money lending (loans EUR 200 – EUR 75,000) if activity falls under scope of Financial Services (Consumer Credit) Act 2011</li> </ul>  |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• prospectus requirement for offering of securities or marketing investment products to the public</li> <li>• certain exemptions under Prospectuses Act 2005               <ul style="list-style-type: none"> <li>– offers addressed only to qualified investors</li> <li>– offers addressed to fewer than 150 persons (other than qualified investors) per Member State</li> <li>– where the minimum consideration payable by any person for the offer is at least EUR 100,000 (or other currency equivalent)</li> <li>– where the total consideration payable in the European Union is less than EUR 100,000 which limit is calculated over a period of 12 months</li> <li>– where the actual securities themselves are denominated in amounts of at least EUR 100,000 (or other currency equivalent)</li> </ul> </li> </ul> |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Extensive AIFMD regulation for AIF and its manager (AIFM)</li> <li>• AIFM requires GFSC authorisation</li> <li>• Equity Model Crowdfunding likely to be caught under such regulations</li> <li>• Gibraltar developed ‘out of scope’ small AIF regime which could be applied so long as assets below AIFMD thresholds, and in the</li> </ul>  |

|                                      |  |
|--------------------------------------|--|
|                                      | situation where the Platform operator to be classes as an AIFM or the Crowdfunding Model used classed as an AIF  |
| <b>Payment service regulation</b>    | Financial Services (EEA) (Payment Services) Regulations 2010 + Financial Services (EEA) (Payment Services) (Supplemental) Regulations 2015 may apply to Crowdfunding platforms holding client money  |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• <i>Companies Act 2014</i></li> <li>• <i>Data Protection Act 2004</i></li> <li>• <i>Proceeds of Crime Act 2015</i></li> <li>• <i>Terrorism Act 2005</i></li> <li>• <i>“Guidance Notes on Systems of control to prevent the financial system from being used for money laundering or terrorist financing activities” (more commonly referred to as the “FSC’s AML Guidance Notes”) published by Gibraltar Financial Services Commission</i></li> <li>• <i>The Electronic Commerce Act 2001</i></li> <li>• <i>The Fair Trading Act 2015</i></li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addresses Gibraltar investors</b></p> <p><i>EU Crowdfunding platform</i></p> <ul style="list-style-type: none"> <li>• Gibraltar regulatory law applicable</li> <li>• What legislation applies depends on Equity Model or Lending Model</li> <li>• Equity Model likely caught by MiFI Act</li> <li>• MiFID licenced Crowdfunding platform will be able to passport services and not require additional licencing</li> <li>• Non-MiFID licenced Crowdfunding platform will require licencing</li> </ul> <p><i>EU companies / projects</i></p> <ul style="list-style-type: none"> <li>• Prospectus may be required under Prospectuses Act</li> <li>• Key question is – “is entity offering or issuing securities or marketing investment products to the public?”</li> <li>• Exceptions for certain types of securities and investment products and thresholds levels covered in 3.2</li> </ul> <p><b>Foreign Crowdfunding platform addresses Gibraltar companies / projects</b></p> <p><i>EU Crowdfunding platform</i></p> |

|                        |  |
|------------------------|--|
|                        | <ul style="list-style-type: none"> <li>• Currently limited number of companies in Gibraltar due to regulatory landscape not having yet matured to a sufficient level</li> <li>• Difference from licencing perspective is that if investors not being approached, unlikely to require a licence, but if deemed to be providing investment services, then may require a licence.</li> </ul> <p><i>EU companies / projects</i></p> <ul style="list-style-type: none"> <li>• Prospectus may be required under Prospectuses Act (see above)</li> </ul>  |
| <p><b>Outbound</b></p> | <ul style="list-style-type: none"> <li>• Limited number of Crowdfunding platforms in Gibraltar</li> <li>• Jurisdiction needs to regulate the market before such outbound approaches are made into foreign markets</li> <li>• Lack of regulation in and of itself a regulatory barrier</li> </ul> <p><b>Crowdfunding platform in Gibraltar addresses investors in another EU country</b></p> <p><i>Gibraltar Crowdfunding platform (hypothetical)</i></p> <ul style="list-style-type: none"> <li>• Limited number of platforms in Gibraltar</li> <li>• In hypothetical case, regulatory barriers would arise depending on Crowdfunding Model chosen.</li> <li>• Equity Model will bring about MiFI Act issues and licencing criteria</li> <li>• Lending Model will bring about additional licencing layer of Gibraltar Government as platform may be seen as a moneylender</li> </ul> <p><b>Gibraltar companies / projects addressing investors in another EU Country</b></p> <ul style="list-style-type: none"> <li>• Licensable activity to carry out advisory activities “from within” Gibraltar, even if targeting non-Gibraltar residents.</li> <li>• Licencing issues apply depending on what is being offered and how it is being marketed</li> <li>• Prospectuses Act may be required under Prospectuses Act (see above)</li> </ul> <p><b>Crowdfunding platform in Gibraltar addresses foreign (and domestic) companies / projects</b></p> <p><i>Gibraltar Crowdfunding platform (hypothetical)</i></p> <ul style="list-style-type: none"> <li>• Several barriers may be encountered as discussed above depending on the activity and one or more licences may be required under following Acts:             <ul style="list-style-type: none"> <li>- MiFI Act</li> <li>- CIS Act</li> <li>- Prospectuses Act</li> <li>- Consumer Credit Act</li> <li>- Moneylending Act</li> </ul> </li> </ul> |

|                                |  |
|--------------------------------|--|
|                                | <p><b>Gibraltar companies / projects addressing foreign (and domestic) companies / projects</b></p> <ul style="list-style-type: none"> <li>• Prospectuses Act may be required under Prospectuses Act (see above)</li> <li>• Not so dependent on location of companies but rather what type of Crowdfunding Model has been chosen and accordingly what type of instrument is on offer and whether an exemption from Prospectuses Act is applicable</li> </ul>   |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | <ul style="list-style-type: none"> <li>• Gibraltar start-ups are usually private companies limited by shares</li> <li>• Prospectus regulations could apply where certain threshold levels met and depending on method of engaging investors as well as type of investors</li> </ul>  |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• Applicable in Gibraltar</li> <li>• wide scope and minimum carve-outs in Gibraltar law result in platform operators being potentially classes as AIFMs and subject to GFSC licencing requirements</li> <li>• Key questions are whether an investment strategy is in place and whether a collective investment scheme has been created</li> </ul>   |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• Applicable in Gibraltar</li> <li>• Where investment advice is provided by the platform operator this could fall within the scope of MiFID</li> <li>• Main application and benefit is ability to passport out of Gibraltar and into the EU</li> </ul>  |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• Any non-cash/electronic transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services which are caught by the the Financial Services (EEA) (Payments Services) Regulations 2010, and has been amended by the Financial Services (EEA) (Payment Services) (Supplemental) Regulations 2015 (together, the “Payment Services Regulations”)</li> <li>• Constitutes a significant impact on Crowdfunding and platform operators will need to put adequate measures in place to ensure compliance with the Payment Services Regulations.</li> </ul> |

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# Hungary

## 1 Recent developments in the market of Crowdfunding in Hungary

In summary, there have been no significant developments in Hungary regarding Crowdfunding since December 2015. Neither the Equity Model, nor the Lending Model has any presence in the Hungarian market. The same is true in relation to “Real Estate Crowdfunding” and “Renewable Crowdfunding”, i.e. none of these Crowdfunding models has any presence in the Hungarian market.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

There were no significant developments in the Hungarian market in relation to the Equity Model since December 2015. The Equity Model still does not yet have any presence in the Hungarian market.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There were no significant developments in the Hungarian market in relation to the Lending Model since December 2015. The Lending Model still does not yet have any presence in the Hungarian market.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

Although there were no significant developments in the Hungarian market in relation to the Donations or Rewards Model since December 2015, there have been certain changes in the market (e.g. certain previously active online platforms became inactive and new market participants appeared on the market), the over-all market has not been changed significantly.

There are few online platforms that use the Donations or Rewards Model in Hungary. Those online platforms collect and handle a relatively limited amount of funds.

### 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

There were no significant developments in the Hungarian market in relation to Real Estate Crowdfunding and Renewable Crowdfunding since December 2015. Neither the Real Estate Crowdfunding, nor the Renewable Crowdfunding has any presence in the Hungarian market.

### 1.5 International approach

We are not aware of any major developments in terms of foreign US/Canadian or other EU platforms planning to enter the Hungarian market or establish international Crowdfunding platforms here in Hungary. However, the other way around is more common, i.e. Hungarian

project managers usually seek funding for their projects on international and/or US, Canadian or other European platforms.

## 2 Recent developments regarding Crowdfunding regulation in Hungary

No legislative changes have been implemented in Hungary in relation to Crowdfunding since December 2015. Therefore, there is still no regulatory regime specifically addressing Crowdfunding in Hungary.

The only recent development that has relevance in connection with Crowdfunding is that the National Bank of Hungary has issued and made publicly available, non-binding guidelines on its interpretation of the Hungarian financial regulatory laws that may apply to certain Crowdfunding structures, i.e. Lending Model and Equity Model. Under these non-binding guidelines, the National Bank of Hungary has made it clear that given that there is no legislation specifically applicable to Crowdfunding, any Crowdfunding structure has to be assessed based on the currently applicable financial regulatory and investment regulatory laws of Hungary without any specific exemption applicable to Crowdfunding in general. Therefore, in summary, if any of the activities of the individual investor, Crowdfunding platform or the crowdfunded business qualifies as the provision of a financial service or an investment service in a business-like manner, such activity would trigger licensing requirements in Hungary. On the same token, if the activity of either the individual investor or the crowdfunded business qualifies as the provision of a financial service or an investment service in a business-like manner, the activity of the Crowdfunding platform may qualify as an intermediary activity, which would, in turn, trigger regulatory requirements in Hungary applicable to agents and intermediaries.

## 3 Current Regulation of Crowdfunding in Hungary

### 3.1 General licensing requirements

#### 3.1.1 Equity Model

If the online Crowdfunding platform facilitates the offering of financial instruments in a business-like manner, such activity of the platform operator is likely to qualify as a licensable investment service under the Hungarian Investment Services Act.

“Financial instruments” under the Hungarian Investment Services Act include, inter alia, transferable securities, such as stocks in public limited companies and private limited companies and debt securities.

Therefore, if the platform operator offers securities held in companies seeking Crowdfunding or bonds issued by such companies, such platform operators would very likely have to obtain an investment services licence from the Hungarian regulator. Similarly, if the individual investors may acquire securities, bonds or other financial instruments issued by the crowdfunded businesses, the Crowdfunding platform may need to obtain an investment

services licence depending on the actual services performed by the Crowdfunding operator. However, the National Bank of Hungary has confirmed in its non-binding public guidelines that if a given Crowdfunding structure does not involve securities, bonds or other financial instruments (e.g. the individual investors are not offered and, cannot acquire, securities, bonds or other financial instruments), such Crowdfunding structure will likely not constitute an investment service and, as such, will not trigger licensing requirements under the Hungarian Investment Services Act.

Furthermore, structures in which the offering/placement of securities is involved would likely require the publication of a prospectus approved by the Hungarian regulator in connection with such offering/placement, provided that no exemption is available under the Hungarian Capital Markets Act.

If the online Crowdfunding platform is structured as a collective investment scheme it would be subject to regulatory requirements applicable to collective investment funds and their managers.

Furthermore, depending on the structure used by the Crowdfunding platform, Hungarian payment services requirements and custodial services requirements referred to in paragraph 3.3 below could also apply to platforms applying the Crowdfunding Equity Model in Hungary.

### **3.1.2 Lending Model**

Lending is a regulated financial service under the Hungarian Banking Act. Therefore, a licence is required for the purposes of providing such regulated lending activities in Hungary in a business-like manner. Such licensing requirements apply to both legal entities and private individuals. It follows that if the activity of a private investor using the Crowdfunding platform qualifies as a lending activity conducted in a business-like manner, such activity would trigger licensing requirements in Hungary. In such case, the activity of the Crowdfunding platform operator may likely qualify as an intermediary activity, which would, in turn, likely trigger regulatory requirements in Hungary applicable to agents and intermediaries.

Therefore, while structuring a platform applying the Lending Model in Hungary, careful consideration should be given to avoid any licensing requirements that could apply either to the individuals lending to the crowdfunded business or to the operating platform which acts as an intermediary in such lending structure.

Lending is a licensable activity under Hungarian law only if it is carried out in a “business-like manner”, i.e. a business activity carried out on a regular basis in the framework of an economic operation. The terms ‘business activities carried out on regular basis’ and ‘economic operation’ are not specifically defined under the Hungarian Banking Act. According to the non-binding public guidelines of the National Bank of Hungary, an activity qualifies as being performed in the framework of business activities carried out on regular basis if the activity is carried out on a regular basis, with the aim of entering into transactions that are not

specified at the outset and with the aim of making a profit. The Hungarian supervisory authority has historically followed a rather conservative approach as to the qualification of licensable financial services and in several cases qualified financial services as being conducted on a regular basis, even if the relevant transaction was only a one-off transaction. According to the public guidance of the Hungarian financial supervisory authority, if the relevant entity expects future similar transactions to be realised at later dates and the entity takes measures to fulfil such transactions on a regular basis, even a one-off transaction may qualify as an activity carried out on a regular basis.

Based on the non-binding public guidelines issued by the National Bank of Hungary in relation to Crowdfunding, it seems that the National Bank of Hungary follows the above, rather conservative interpretation as to the qualification of the activities of the individual investors lending money to the crowdfunded business as well, i.e. no special exemption is applicable to individual investors lending money to a crowdfunded business through a Crowdfunding platform. Therefore, if the activity of an individual investor lending money to a crowdfunded business qualifies as a lending activity conducted in a business-like manner (e.g. the individual investor provides several interest bearing-loans to one or more crowdfunded business), such activity of the individual investor would likely trigger licensing requirements in respect of the individual investor, which would, in turn, trigger regulatory requirements applicable to intermediaries and agents from the perspective of the platform operator as well.

However, the Crowdfunding platforms using the Lending Model could possibly structure their services so as to eliminate or limit the risk of triggering Hungarian licensing requirements in relation to the lending element. For example, such models could stipulate that individual investors do not receive interest on the loans provided to the crowdfunded business (thereby eliminating the profit oriented element), which would in turn limit the risk of triggering licensing requirements. Further-more, the Crowdfunding platform could limit the number of the lending transactions that could be initiated by the individual. It may effectively limit the applicability of the regularity element of the activity which would, in turn, also limit the risk of triggering licensing requirements.

In addition to above, the National Bank of Hungary confirmed under its non-binding public guide-lines that the activity of the crowdfunded business and/or Crowdfunding platform under the lending Model may fall under the regulated financial service of “collection and acceptance of deposits or other repayable funds from the public”. This is because in such case, the crowdfunded businesses and/or the Crowdfunding platform (depending on the structure of the given Crowdfunding platform) would, in essence, collect funds from the general public that must be repaid by the crowdfunded business later on. Therefore, the National Bank of Hungary is of the opinion that such activity may qualify as a licensable financial service as well if it is provided in a business-like manner. However, the Crowdfunding platforms using the Lending Model could possibly structure their services so as to eliminate or limit the risk of triggering Hungarian licensing requirements in relation to the deposit taking element. For

example, such models could stipulate that individual investors do not receive interest on the loans provided to the crowdfunded business (thereby eliminating the profit oriented element), which would in turn limit the risk of triggering licensing requirements.

Furthermore, depending on the structure used by the Crowdfunding platform, the Hungarian payment services requirements and custodial services requirements referred to in paragraph 3.3 below could also apply to platforms applying the Crowdfunding Donations or Rewards Model in Hungary.

### 3.1.3 Donations or Rewards Model

The Donations or Rewards Model is used in Hungary for financing creative projects, art and design projects or civil initiatives. Although no monetary return is involved in such financing, in most cases, the company or person carrying out the project offers non-monetary rewards in return for the donations (e.g. a product sample, tickets).

In general, Donations or Rewards Models do not raise any specific Hungarian regulatory issue. However, depending on the structure used by the Crowdfunding platform, the Hungarian payment services requirements and custodial services requirements referred to in paragraph 3.3 below could also apply to platforms applying the Crowdfunding Donations or Rewards Model in Hungary.

## 3.2 Prospectus requirements

Companies issuing securities to the public in Hungary might be subject to Hungarian prospectus requirements. According to the Hungarian Capital Markets Act, in such case a prospectus and a notice must be issued and approved by the competent Hungarian regulator.

However, in the case of Lending Model and Donations or Rewards Model, a Crowdfunding platform operator is normally not subject to such a prospectus requirement as it will not be responsible for the offering/placement of securities.

However, Equity Model Structures in which the platform operator is involved in the offering/placement of securities may require the publication of the prospectus/notice and approval by the Hungarian regulator in connection with such offering/placement, provided that no exemption is available under the Hungarian Capital Markets Act.

Such exemptions might include the following:

- A. the offer of securities is addressed to fewer than 150 natural or legal persons in each Member State; and/or
- B. an offer of securities where the a total consideration for securities in the European Union is less than EUR 100,000, which limit must be calculated over a period of 12 months.

However, even if an exemption is available, the offer/placement of securities in Hungary might constitute a private placement in Hungary triggering capital market requirements

under the Hungarian Capital Markets Act (e.g. notification must be submitted to the Hungarian regulator, formality requirements may apply to the documents relating to the offer/placement).

### **3.3 Regulation of Crowdfunding under the AIFMD regime**

The European Union Alternative Investment Fund Managers Directive has been implemented under the Hungarian Collective Investment Schemes Act. The Collective Investment Schemes Act is applicable in general to all collective investment schemes, including alternative investment funds. An ‘alternative investment fund’ is defined under the Collective Investment Schemes Act as a collective investment scheme which does not qualify as ‘Undertakings for Collective Investment in Transferable Securities’ (UCITS).

The Collective Investment Schemes Act provides licensing and regulatory requirements applicable to the alternative investment funds and its managers (e.g. licences required for the provision of collective portfolio management services; registration and marketing of the relevant alternative investment funds). Therefore, if a Crowdfunding undertaking wants to structure its operation as an alternative investment fund (or manager thereof) it must comply with the requirements under the Collective Investment Schemes Act.

### **3.4 Licence under the payment services and custodial services regulations**

In most of the Crowdfunding structures, the individual investors transfer money to the platform operator and not directly to the crowdfunded businesses. The platform operator first collects the payments from the individual investors and distributes such funds only if the aggregated amount of the payments reaches or exceeds a specific threshold limit, or upon the satisfaction of other specified financing criteria. Therefore, in such cases the platform operator acts as an intermediary which collects funds from individual investors, holds such funds until the specified financing criteria are fulfilled and then transfers such funds to the crowdfunded businesses.

There is a risk that the collection, holding and handling of such funds by platform operators may constitute a custodial service and/or payment service requiring a licence under the Hungarian Banking Act, provided that it is carried out in a business-like manner. However, Crowdfunding plat-forms could possibly avoid licensing requirements if the platforms structure their activities so as to rely on exemptions from the relevant financial services licensing requirements, or by using an external financial institution or payment services provider for holding the amounts on escrow.

Once the financing criteria are fulfilled, the platform operator transfers the collected funds to the crowdfunded business. There is a risk that such transfer through the platform operator may qualify as a monetary remittance service or other form of payment service and be subject to Hungarian payment services regulations if it is carried out in a business-like manner. If so, the platform operator would require a licence from the Hungarian regulator to carry out payment services in Hungary. However, Crowdfunding platforms could possibly avoid

payment services licensing requirements if they can rely on exemptions from the payment services licensing requirements (e.g. the commercial agent exemption) or by using an external financial institution or payment services provider for processing payments.

### 3.5 Possible additional Regulations

The platform operator may be subject to further Hungarian regulations, in particular:

- laws applicable to on-line marketing and contracts;
- laws applicable to electronic commerce and information society;
- anti-money laundering laws;
- data privacy and data protection laws;
- consumer credit regulations; and
- consumer protection regulations.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

In general, Hungarian financial and investment regulatory laws are applicable to financial services and investment services that are provided in Hungary or to Hungary on a cross-border basis.

Based on non-binding public guidelines of the National Bank of Hungary, if any 'material' element of the whole activity/service is in Hungary (it is not defined by the regulator what those 'material' elements are, but includes e.g. collateral in Hungary, credit check, document preparation, signing of agreements, opening of accounts, exposure monitoring, contacts, enforcement, etc.), or the product/service is marketed, proposed, offered, initiated, solicited or pitched by a foreign entity to clients in Hungary, such activity/service would likely qualify as being provided in Hungary and, as such, would trigger licensing requirements in Hungary.

In this regard, the Hungarian regulator follows both a territorially focused approach and a marketing focused approach in the sense that if any material activity of the given financial, payment and/or investment service is conducted in Hungary and/or if a client in Hungary is targeted by marketing of a financial, payment and/or investment service, such service would likely qualify as being provided in Hungary or on a cross-border basis to Hungary and, as such, would trigger licensing requirements in Hungary.

The following indicators would likely be taken into account by the National Bank of Hungary in the assessment of whether an entity targets the Hungarian market and/or clients in Hungary:

- marketing or soliciting via email, fax or letters;
- cold calls to Hungarian clients;
- using web banners and/or links in Hungarian websites leading to the website of the service provider;

- maintaining a website targeting clients in Hungary, e.g. among others, the following factors would likely be taken into account:
  - domain name or extension refers to Hungary
  - indication of Hungarian contact details/representative office
  - contents on website are in Hungarian language (probably the most decisive factor)
  - product description
  - prices are in Hungarian Forint
  - Hungarian bank accounts may be used for money transfers
  - fact that financial services are actually being sold to Hungarian clients

In summary, also foreign entities not having their registered seat or domicile in Hungary may be captured by the Hungarian financial regulatory regulations in the event that they approach or otherwise target investors or prospects in Hungary.

## 4.2 Inbound

### 4.2.1 Foreign Crowdfunding platforms address Hungarian investors

Hungarian law may apply to the Crowdfunding platform; and/or the company and the project seeking funding.

As explained above, if a Crowdfunding platform from a foreign (EU) country is providing financial services, investment services and/or payment services (please see section 3 above) in Hungary or to Hungary on a cross-border basis in a business-like manner and/or marketing such regulated services in Hungary or to prospects in Hungary, such activity would likely trigger licensing requirements in Hungary. In general, there are several criteria that must be considered when assessing whether a given activity is considered to be provided in Hungary or on a cross-border basis to Hungary (please see subsection 4.1 above). In any case, if the investment opportunities of a Crowd-funding platform were presented in Hungarian, the services/investment opportunities offered on such platform would likely constitute a service provided to Hungary on a cross-border basis which could potentially trigger Hungarian licensing requirements in relation to either or both the Crowdfunding platform and/or the company/project seeking funding.

#### 4.2.1.1 Crowdfunding platform

If the services offered via a Crowdfunding platform qualify as financial services, investment services and/or payment services in Hungary or to Hungary on a cross-border basis in a business-like manner and/or marketing such regulated services in Hungary or to prospects in Hungary, such activity would likely trigger licensing and/or regulatory requirements in Hungary with respect to the Crowdfunding platform (please see section 3 above).

Therefore, for the purposes of conducting such activity, an EU Crowdfunding platform should either establish a subsidiary or branch in Hungary and obtain a licence from the

National Bank of Hungary in relation to the given financial service/investment service or passport its existing regulatory licence obtained in its home EU country (if any) to Hungary pursuant to the relevant single-passport EU directives (e.g. CRD, MiFID and PSD).

#### **4.2.1.2 Company / project**

Similarly to Clause 4.2.1.1 above, if the activity of a foreign crowdfunded business qualifies as a regulated service carried out in Hungary or to Hungary on a cross-border basis in a business-like manner (please see section 3 above and, in particular, subsections 3.2 and 3.3), the same requirements would be applicable to such crowdfunded business as well.

In addition to the above, structures where the crowdfunded business offers/places securities to Hungarian investors or prospects would likely require the publication of a prospectus approved by the Hungarian regulator in connection with such offering/placement, provided that no exemption is available under the Hungarian Capital Markets Act.

#### **4.2.2 Foreign Crowdfunding platform addresses Hungarian companies**

Again, Hungarian law may apply to the Crowdfunding platform and/or the company or the project seeking funding.

As explained above, if a Crowdfunding platform from a foreign (EU) country is providing financial services, investment services and/or payment services (please see section 3 above) in Hungary or to Hungary on a cross-border basis in a business-like manner and/or marketing such regulated services in Hungary or to prospects in Hungary, such activity would likely trigger licensing requirements in Hungary. In general, there are several criteria that must be considered when assessing whether a given activity is considered to be provided in Hungary or on a cross-border basis to Hungary (please see subsection 4.1 above). In any case, if the investment opportunities of a Crowd-funding platform were presented in Hungarian, the services/investment opportunities offered on such platform would likely constitute a service provided to Hungary on a cross-border basis which could potentially trigger Hungarian licensing requirements in relation to either or both the Crowd-funding platform and/or the company/project seeking funding.

##### **4.2.2.1 Crowdfunding platform**

If the services offered via a Crowdfunding platform qualify as financial services, investment services and/or payment services in Hungary or to Hungary on a cross-border basis in a business-like manner and/or marketing such regulated services in Hungary or to prospects in Hungary, such activity would likely trigger licensing and/or regulatory requirements in Hungary with respect to the Crowdfunding platform (please see section 3 above).

Therefore, for the purposes of conducting such activity, an EU Crowdfunding platform should either establish a subsidiary or branch in Hungary and obtain a licence from the National Bank of Hungary in relation to the given financial service/investment service or

passport its existing regulatory licence obtained in its home EU country (if any) to Hungary pursuant to the relevant single-passport EU directives (e.g. CRD, MiFID and PSD).

#### **4.2.2.2 Company / project**

Similarly to Clause 4.2.1.1 above, if the activity of a foreign (EU) crowdfunded business qualifies as a regulated service carried out in Hungary or to Hungary on a cross-border basis in a business-like manner (please see section 3 above and, in particular, subsections 3.2 and 3.3), the relevant licensing / regulatory requirements would be applicable to such crowdfunded business as well.

In addition to the above, structures where the crowdfunded business offers/places securities to Hungarian investors or prospects would likely require the publication of a prospectus approved by the Hungarian regulator in connection with such offering/placement, provided that no exemption is available under the Hungarian Capital Markets Act.

### **4.3 Outbound**

In this situation, a Hungarian Crowdfunding platform enters foreign (EU) markets and therefore addresses foreign investors.

Again, two different alternatives may need to be considered:

- Hungarian Crowdfunding platform approaches foreign (EU) investors; or
- Hungarian Crowdfunding platform approaches Hungarian investors and presents a company / project from another EU member state on its platform.

#### **4.3.1 Hungarian Crowdfunding platform addresses foreign (EU) investors**

As explained in Clause 4.1 above, if any 'material' element of the whole regulated activity/service is in Hungary, such activity/service would likely qualify as being provided in Hungary and, as such, would trigger licensing requirements in Hungary.

##### **4.3.1.1 Crowdfunding platform**

If a Crowdfunding platform operates in Hungary, it will be subject to Hungarian licensing and regulatory requirements. Accordingly, as explained above, depending on the structure used, Crowd-funding platform operators using the Equity Model and/or the Lending Model would require a licence from the National Bank of Hungary to conduct such regulated services in Hungary depending on the relevant activity (please see section 3 above). However, once the Crowdfunding platform operator has obtained its licence from the National Bank of Hungary, it should be free to passport such licence to another EU member state where it wishes to provide such services pursuant to the relevant single-passport EU directives (e.g. CRD, MiFID and PSD) in accordance with the local laws of the host member state.

#### **4.3.1.2 Company / project**

Similarly to Clause 4.3.1.1 above, if the activity of a Hungarian crowdfunded business qualifies as a regulated service carried out in Hungary in a business-like manner (please see section 3 above and, in particular, subsections 3.2 and 3.3), the relevant licensing requirements would be applicable to such crowdfunded business as well.

#### **4.3.2 Hungarian Crowdfunding platform addresses foreign companies/projects**

As explained in subsection 4.1 above, if any 'material' element of the whole a regulated activity/service is in Hungary, such activity/service would likely qualify as being provided in Hungary and, as such, would trigger licensing requirements in Hungary.

##### **4.3.2.1 Crowdfunding platform**

As explained above, if a Crowdfunding platform operates in Hungary, it will be subject to Hungarian licensing and regulatory requirements. Accordingly, as explained above, depending on the structure used, Crowdfunding platform operators using the Equity Model and/or the Lending Model would require a licence from the National Bank of Hungary to conduct such regulated services in Hungary depending on the relevant activity (please see section 3 above). However, once the Crowdfunding platform operator has obtained its licence from the National Bank of Hungary, it should be free to passport such licence to another EU member state where it wishes to provide such services pursuant to the relevant single-passport EU directives (e.g. CRD, MiFID and PSD) in accordance with the local laws of the host member state.

##### **4.3.2.2 Project/ company**

Similarly to subsection 4.3.2.1 above, if the activity of a Hungarian crowdfunded business qualifies as a regulated service carried out in Hungary in a business-like manner (please see section 3 above and, in particular, subsections 3.2 and 3.3), the relevant licensing/regulatory requirements would be applicable to such crowdfunded business as well.

In addition to the above, structures where the crowdfunded business offers/places securities or financial instruments to Hungarian investors or prospects would likely require the publication of a prospectus approved by the Hungarian regulator in connection with such offering/placement, provided that no exemption is available under the Hungarian Capital Markets Act.

#### **4.4 Impact of EU regulation**

Hungary, being a member of the European Union, is subject to the EU legislation applicable to financial services and investment services. In particular, Hungary has implemented EU single market directives of CRD, MiFID and PSD. In general, given that the relevant EU single market directives are applicable to each EEA Member State, the regulatory and pass-porting rules applicable to the establishment of a branch in another EEA Member State under 'the freedom of establishment' or providing the services on a cross-border basis in

another EEA Member State using ‘the freedom of services’ are governed by the same EU legislation, i.e. in principle, the same EU legislation is applicable to both Hungarian regulated entities subject to CRD, MiFID and PSD establishing or operating in another EEA Member State, and to foreign EEA entities subject to CRD, MiFID and PSD establishing or operating in Hungary.

In addition to the above, Hungary has also implemented the Prospectus Directive and the AIFMD-Directive.

#### **4.4.1 Prospectus rule/regime**

As we previously stated in point 3.2., should a company operating in an Equity Structure wish to issue securities, its activity might fall within the scope of the Prospectus Directive implemented in the Hungarian Capital Markets Act. The National Bank of Hungary set out in its non-binding guide-line that Crowdfunding activities should be evaluated in terms of the effective Hungarian laws, and there is no regulatory regime adapted to Crowdfunding in Hungary. As a consequence of the above, the Hungarian legal regime implemented under the EU Prospectus Directive and the EU Prospectus Regulations may be applicable to companies operating in an Equity Model and/or issuing securities to investors in Hungary.

#### **4.4.2 AIFM Directive**

As previously set out in subsection 3.3. should an entity using the Equity Model qualify as an alternative investment fund or its manager, its activity might fall within the scope of the AIFM Directive implemented in the Collective Investment Scheme Act under Hungarian law. The National Bank of Hungary set out in its non-binding guideline that Crowdfunding activities should be evaluated based on the effective Hungarian laws, and there is no regulatory regime adapted to Crowdfunding in Hungary. As a consequence of the above, the Hungarian law implementation of the AIFM Directive might be applicable to entities operating in an Equity Model in Hungary in the form of an alternative investment fund or its manager or offer financial instruments held in alternative investment funds to Hungarian investors.

#### **4.4.3 MiFID/MiFID II**

As explained in subsection 3.1 above, there is a possibility that operation a Crowdfunding platform may qualify as an investment service in Hungary and may therefore trigger licensing requirements. The Hungarian Investment Service Act is harmonized with MiFID. Therefore, in the event such licensing requirements are triggered, it is possible to passport the license to the National Bank of Hungary as set out above under the respective EU regulation.

#### **4.4.4 PSD/PSD II**

As we explained in point 3.4 above, there is a possibility that operation of certain payment services through a Crowdfunding platform may qualify as a payment service/custodial service in Hungary and may therefore trigger licensing requirements. The Hungarian laws are harmonized with the PSD. Therefore, if such licensing requirements are triggered, it is

possibility to passport the license to the National Bank of Hungary as set out above under the respective EU regulation.

#### **4.5 Summary**

There is no regulatory regime adapted to Crowdfunding in Hungary. However, depending on the structure used by the relevant platform operator, both the Lending Model and the Equity Model might trigger regulatory requirements in Hungary, including, inter alia, financial services requirements, investment services requirements, prospectus requirements and payment services requirements. Nevertheless, Hungary, being a member of the European Union, is subject to the EU legislation applicable to financial services and investment services and has implemented EU single market directives of CRD, MiFID and PSD and the Prospectus Directive and the AIFMD-Directive as well.

### **5 Lessons learned from Hungary's regulation for a possible harmonized European Crowdfunding regulation**

#### **5.1 Role model ("dos")**

Given that there is no regulatory regime adapted specifically to the Crowdfunding models in Hungary and due to the legal uncertainties and potential legal impediments referred to above, we do not recommend following the Hungarian legal framework applicable to Crowdfunding for a possible harmonized European Crowdfunding regulation.

#### **5.2 Aspects that should be avoided ("don'ts")**

With reference to the above, we believe that the lesson that could be learned from the current Hungarian legal framework that there is a need for a harmonized European Crowdfunding regulation or directive applicable to each model of the Crowdfunding concept, on the basis of which the local regulators can implement detailed domestic regulations applicable to Crowdfunding activities and/or the local platform operators and their clients can pursue Crowdfunding activities without having to face substantial legal impediments and/or legal uncertainties.

### **6 Conclusion**

There are only a few Crowdfunding platforms in Hungary and those which exist rather use the Do-nations or Rewards Model. The Lending Model and the Equity Model currently have no really significant role in Hungary.

There is no regulatory regime adapted to Crowdfunding in Hungary. However, depending on the structure used by the relevant platform operator, both the Lending Model and the Equity Model might trigger regulatory requirements in Hungary, including, inter alia, financial services requirements, investment services requirements, prospectus requirements and payment services requirements. Nevertheless, we believe that the platform operators seeking to intermediate Crowd-funding based on the Equity Model or the Lending Model could

possibly structure their activities and business terms so as to limit and/or eliminate the risk of triggering Hungarian licensing requirements.

In our view, the Donations or Rewards model is generally exempted from the Hungarian regulatory requirements. However, depending on the structure used by the platform and service provided by the company, they might trigger payment services and custodial services requirements.

Given the above uncertainties of the Hungarian regulatory requirements with regard to the Crowd-funding activities, unless the relevant Hungarian laws and regulations are amended we recommend to seek guidance from the Hungarian regulator on the interpretation of the relevant laws to clarify such ambiguities before using certain Crowdfunding methods and/or structures.

## 7 Summary – Crowdfunding regulation

| Country   | <b>Hungary</b>  |
|---|---|
| <b>Summary</b>  |   |
| <b>Recent developments in Crowdfunding regulation</b> | There have been no recent developments in the Hungarian Crowdfunding regulation, except the non-binding guidelines of the Hungarian National Bank in relation to Crowdfunding   |
| <b>Current / planned Crowdfunding regulation</b>      |   |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• If the Crowdfunding platform facilitates the offering of securities, the operator of the platform may be subject to investment services requirements<br/>→ licence from the Hungarian supervisory authority required</li> <li>• If the Crowdfunding platform facilitates and/or intermediates the granting of loans to the crowdfunded business, such activity may trigger financial services requirements in relation to the platform operator, crowdfunded business and/or individuals granting loans<br/>→ licence from the Hungarian supervisory authority required</li> <li>• Crowdfunding under both the Equity Model and Lending Model could be structured so as to eliminate/limit the risk of triggering licensing requirements</li> <li>• The Donation or Rewards Model do not raise any specific Hungarian regulatory issues</li> </ul> |
| <b>Prospectus requirements</b>                        | <ul style="list-style-type: none"> <li>• Prospectus requirement for the offering of securities and certain other financial instruments (e.g. shares, bonds, certain derivatives)</li> <li>• Threshold: EUR 100,000 aggregated issue value for securities offered in all member states of the European Union within a period of 12 months</li> </ul>   |
| <b>AIFMD-regulation</b>                               | If a Crowdfunding undertaking wants to structure its operation as an alternative investment fund (or manager thereof) it must comply with the requirements under the Collective Investment Schemes Act  |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Transfer of funds through the platform operator may constitute money remittance service → licence from the Hungarian supervisory authority required</li> <li>• Collection and holding of funds as escrow by the platform operator may constitute financial service → licence from the Hungarian supervisory authority required</li> </ul>  |
| <b>Consumer credit regulation</b>                     | Depending on the structure used by the platform, consumer credit regulations may be applicable  |

|                                      |  |
|--------------------------------------|--|
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Laws applicable to on-line marketing and contracts</li> <li>• Laws applicable to e-commerce and information society</li> <li>• Anti-money laundering laws</li> <li>• Data privacy and data protection laws</li> <li>• Consumer credit regulations</li> <li>• Consumer protection regulations</li> </ul> |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | EU entities having a licence to provide the relevant investment services and/or financial services in Hungary may passport their licence to Hungary  |
| <b>Outbound</b>                      | Hungarian entities having a licence to provide the relevant investment services and/or financial services in Hungary may passport their licence to the host EU country   |
| <b>Impact of EU regulation</b>       |  |
| <b>Prospectus regulations</b>        | Applicable if licencing requirements are triggered. Pass-porting the existing relevant EEA license is possible   |
| <b>AIFM-Directive</b>                | Applicable if licencing requirements are triggered. Pass-porting the existing relevant EEA license is possible   |
| <b>MiFID / MiFID II</b>              | Applicable if licencing requirements are triggered. Pass-porting the existing relevant EEA license is possible   |
| <b>PSD / PSD II</b>                  | Applicable if licencing requirements are triggered. Pass-porting the existing relevant EEA license is possible.  |

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# Ireland

## 1 Recent developments in the market of Crowdfunding in Ireland

Crowdfunding is becoming an important sub-sector of the growing Irish FinTech industry. There are almost a dozen different Crowdfunding platforms with a presence in Ireland – some are indigenous start-ups and others are Irish versions of international Crowdfunding providers.

At present there is no bespoke regulatory framework for Crowdfunding in Ireland. On 21 April 2017 the Irish Department of Finance launched a public consultation on the potential regulation of Crowdfunding in Ireland. This may represent a significant step towards the development of a bespoke regulatory framework for Crowdfunding in Ireland. This public consultation is discussed in more detail below.

The most common Crowdfunding models in Ireland are the Donations or Rewards Model and the Lending Model. The Equity Model has perhaps failed to emerge due to the inherent risks of investing in crowd-funded projects and the lack of bespoke regulation governing the industry. Added to this, existing Irish financial services legislation creates a series of legal and regulatory obstacles which make it difficult for any Crowdfunding platform to scale without becoming a regulated entity. Legislation and regulation exists in relation to other areas which may be interpreted in such a way as to be deemed to apply to Crowdfunding operations in certain circumstances.

The Central Bank of Ireland (the "CBI") issued a Consumer Notice on Crowdfunding and Peer-to-Peer Lending in June 2014 detailing the risks currently associated with Crowdfunding, including:

- loss of money due to failure of the Crowdfunding platform;
- loss of money due to failure of the business or default on loan repayments;
- lower than expected return on investment;
- the provision of misleading or inaccurate information;
- lack of consumer understanding of the risks inherent in investments or lending; and
- fraud or money laundering concerns.

In a recent interview the Governor of the CBI, Philip Lane, stated that he is "open-minded" regarding the regulation of new financial technologies, including Crowdfunding. Despite this, there is currently no regulation expected in relation to Crowdfunding in Ireland but it is interesting to note in light of the recently launched public consultation.

### **1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)**

The Equity Model is not actively pursued by many Irish companies and the larger Irish Crowdfunding platforms do not currently focus on the Equity Model. The lack of direct legislation and resulting lack of clarity as to the applicable regulatory framework may explain this market hesitation.

It is important to note that the Prospectus Directive (discussed below) has added implications for any Crowdfunding based on the Equity Model. The Prospectus Directive is due to be replaced by a Prospectus Regulation, the provisions of which may assist the Crowdfunding market.

### **1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

The Lending Model is the most active sector of Crowdfunding in the Irish market. This sector can be divided into lending to consumers (which is regulated) and lending to companies (which is not directly regulated). As lending to consumers is extensively regulated in Ireland, most Irish Crowdfunding platforms using the Lending Model have focused their efforts on arranging credit for corporate entities instead. This regulation is discussed in more detail below.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

While the Donations or Rewards Model currently exists in Ireland it does not operate on any large scale. It is not currently subject to any regulatory regime as it does not involve the provision of investment services or the lending of monies. There is currently no legislation proposed in this area.

### **1.4 Real Estate Crowdfunding / Renewable Crowdfunding**

Real Estate Crowdfunding and Renewable Crowdfunding are only emerging as new Crowdfunding platforms in Ireland. These sectors are not currently regulated and therefore involve the same risks as the traditional Crowdfunding models.

### **1.5 International approach**

Ireland has not been the obvious choice to date for international Crowdfunding companies to establish a European base, with companies instead focussing on the UK market and London in particular. Given the Financial Conduct Authority's approach to Crowdfunding and the Sandbox Initiative's attempt to foster innovative Crowdfunding platforms, the UK market for Crowdfunding has outpaced the Irish market in recent years. However, the UK's vote in June 2016 to leave the European Union could result in Crowdfunding companies reconsidering their strategic decisions on the location of their European headquarters. Given Ireland's pro-business environment, the highly skilled and educated workforce and its geographical position

as a gateway to Europe, Ireland is well positioned to support an emerging Crowdfunding industry in a post-Brexit Europe.

## 2 Recent developments regarding Crowdfunding regulation in Ireland

On 21 April 2017 the Irish Department of Finance (the "Department") launched a public consultation on the potential regulation of Crowdfunding in Ireland. Under the IFS 2020 Action Plan 2017 the Irish Government committed to pursuing this public consultation in the context of the European Commission's Action Plan on Building a Capital Markets Union. As part of this public consultation, the Department is seeking input from various industry stakeholders in order to understand better how to facilitate the development of Crowdfunding in Ireland in a way that benefits the economy while also ensuring adequate protection for small investors and consumers. The objective of the public consultation is:

*"to seek the views of interested parties on whether a regulatory regime would be appropriate for the Crowdfunding sector, or if such a regime (or limited regime) with its inherent obligations and costs would be an impediment to the development of Crowdfunding in Ireland."*

In the public consultation paper published by the Department, certain costs associated with the regulation of Crowdfunding are identified including:

- the cost of CBI resources required to regulate the industry, the costs of which would be recoverable via an industry levy (as with other regulated sectors);
- the costs for industry in terms of obtaining authorisations and complying with ongoing reporting requirements commensurate with the level of industry risk identified by the CBI; and
- the increased costs for users of Crowdfunding platforms, which would reduce returns and increase the cost of equity or credit (as the case may be).

The public consultation will conclude on 2 June 2017 and any submissions received will be used to inform the future development of regulatory policy on Crowdfunding in Ireland.

Other than this public consultation, there have been no significant recent developments regarding the regulation of Crowdfunding in Ireland in the last 12 months. However, as noted above the Governor of the CBI, Philip Lane, recently stated that he is "open-minded" regarding the regulation of new financial technologies, including Crowdfunding. This may be particularly relevant in light of the recently launched public consultation and the European Commission's report "Crowdfunding in the EU Capital Markets Union" published in April 2016, which concluded that "*given the predominantly local nature of Crowdfunding, there is no strong case for EU level policy intervention*". Subject to the outcomes of the public consultation and in the absence of any legislation at the European level, the CBI may consider actively moving to regulate Crowdfunding in Ireland, however there is currently no indication of this occurring in the short term.

### 3 Current Regulation of Crowdfunding in Ireland

At present there is no bespoke regulatory framework for Crowdfunding in Ireland and Irish law has yet to formally recognise it as a distinct means of finance. While there is a lack of direct legislation, it should be noted that there is a large body of related financial services legislation that is not expressly intended to apply to Crowdfunding but may nevertheless be applicable to Crowdfunding platforms in certain circumstances. The main issue is that Crowdfunding cuts across several distinct and onerous regulatory frameworks. As a result, it is currently difficult for Crowdfunding platforms to expand unless they become regulated businesses.

Existing financial services legislation in Ireland has created a series of legal and regulatory obstacles which make it difficult in practice for any Crowdfunding platform to scale significantly without first obtaining certain authorisations or even becoming a regulated financial services provider. In the absence of a bespoke regulatory regime for Crowdfunding platforms, it is possible that several regulatory authorisations may in fact be required to operate a Crowdfunding platform in Ireland, depending on the business model used.

#### 3.1 Banking / Financial Service licence requirements

The term "banking business" is broadly defined in Section 7(1) of the Central Bank Act 1971 and involves the acceptance of deposits and lending on account. Furthermore, a person shall be deemed to hold himself out as a banker if the name of the body includes any of the words "bank", "banker" or "banking" or any word which is a variant, derivative or translation of or is analogous to any of those words.

Unless a person holds a banking licence, Irish law contains a very broadly worded prohibition which states that a person shall not carry on a banking business, hold himself out or represent himself as a banker or as carrying on banking business, or accept deposits or other repayable funds from the public. Breach of this prohibition is a criminal offence.

A Crowdfunding platform could potentially be required under Irish law to obtain a banking licence if it is engaged in deposit taking from customers. It is therefore very important that any Crowdfunding platform does not engage in the regulated activity of a "banking business" without the necessary authorisation. Furthermore, Crowdfunding platforms should also take care to avoid using any brand name or trading name that could create the impression that they are engaged in some form of banking business.

#### 3.2 Prospectus requirements

The Prospectus (Directive 2003/71/EC) Regulations 2005 implement in Ireland the Prospectus Directive (2003/71/EC) which sets out the requirements for prospectuses relating to securities offered to the public or admitted to trading on a regulated market within the EU and aims to harmonise the requirements for the drawing up, approval and distribution of a prospectus in this context. This is most likely to apply to Crowdfunding platforms where they

facilitate the offering of securities to the public through the Equity Model or the Lending Model.

The European Commission, Parliament and Council have now reached agreement on a new Prospectus Regulation, which is designed to repeal and replace the existing body of European prospectus law. The two key proposed changes from a Crowdfunding perspective are:

- a higher threshold to determine when companies must issue a prospectus. No EU prospectus will be required for capital raisings and Crowdfunding projects up to EUR 1 million (up from EUR 100,000); and
- smaller issuers who want to access European capital markets will be able to avail of an "EU growth prospectus" aimed at SME's and other small companies, which will be subject to a proportionate disclosure regime.

The new Prospectus Regulation is not yet in force but given these thresholds and the current levels of Crowdfunding activity in Ireland it is unlikely that any Crowdfunding platform in the Irish market will be subject to the prospectus requirements.

### **3.3 Regulation of Crowdfunding under the AIFMD regime**

The Alternative Investment Fund Managers Directive ("AIFMD") regime governs many aspects of the alternative investment market within Europe. AIFMD provides a regulatory framework governing legal, regulatory, risk monitoring and process elements of alternative investment fund management with specific rules on remuneration, valuation, delegation and capital requirements as well as rules governing risk and liquidity management, business conduct, transparency and the depository function. It is implemented in Ireland by the European Union (Alternative Investment Fund Managers) Regulations 2013.

An alternative investment fund ("AIF") is a collective investment vehicle where funds are raised from multiple investors to be invested in accordance with a defined investment policy. Although Crowdfunding activity could potentially be caught by the AIFMD regime, it only applies to funds that manage assets of EUR 100 million or more – a scale which is unlikely to trouble the Irish Crowdfunding industry for the time being. However, certain Crowdfunding business models may be structured in such a way as to be considered AIFs under Irish law.

AIFs must be authorised by the CBI and are subject to strict marketing conditions. The most recent version of the AIF Rulebook was published by the CBI in March 2017 and sets out the conditions applicable to AIFs.

### **3.4 Regulation under the Payment Services Directive (and implementing local regulation)**

The first Payment Services Directive ("PSD 1") was adopted in 2007 and implemented in Ireland in 2009 through the European Communities (Payment Services) Regulations 2009. A new type of regulated entity called a "payment institution" was established under PSD 1. This

legislation (and PSD 2 – its incoming replacement) is relevant to Crowdfunding platforms because aspects of their business models may involve the provision of certain regulated payment services, including for example some or all of:

- operating payment accounts;
- executing payment transactions; and/or
- providing money remittance services.

Due to reliance on one of the exemptions contained in PSD 1, known as the commercial agent exemption, many Crowdfunding platforms have so far avoided the requirement to obtain a regulatory authorisation for the payment services aspects of their businesses. However, remaining outside the scope of payment services regulation is set to become more challenging as the regulatory framework for payment services is being extensively reformed by PSD 2 from 13 January 2018 onwards.

PSD 1 included an exemption from authorisation as a payment institution for payment transactions conducted through a commercial agent authorised to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or payee. This exemption has been applied differently across the EU with some Member States (including Ireland) permitting a commercial agent acting on behalf of both the payer and payee to avail of the exemption and other Member States only permitting its use where a commercial agent acts for either the payer or the payee.

Under PSD 2, the commercial agent exemption is being narrowed to address this inconsistent practice. In future, the exemption will generally only be available when a commercial agent acts on behalf of either the payer or the payee. If a commercial agent acts for both sides the exemption will only be available if the agent does not possess or control client funds at any time.

The revised commercial agent exemption in PSD 2 seeks to standardise the exemptions in order to create a level playing field, reduce risk and provide greater legal protection for payment service users and will have a dramatic impact on the business models of many Crowdfunding platforms which to date have fallen outside the regulatory scope of PSD 1.

Short of choosing to become an authorised payment institution, we expect many Crowdfunding platforms will chose to employ an authorised third-party payment service provider to act on their behalf rather than continuing to process payments between investors and targets directly.

Separately, Part V of the Central Bank Act 1997 regulates a money transmission business, which is "a business that comprises or includes providing a money transmission service to members of the public". A "money transmission service" is defined as a service that involves transmitting money by any means, other than such a service provided by a regulated entity or on an ancillary basis to other business conducted by an entity. While we note that the definition of money transmission service excludes payment services which are regulated by

the European Communities (Payment Services) Regulations 2009, we also recommend that all Crowdfunding platforms consider whether their business model may require them to obtain a regulatory authorisation as a money transmission business.

### **3.5 Possible additional regulations such as anti-money laundering laws, data privacy laws, consumer credit regulation, etc.**

Other additional Irish legislation that may be applicable to Crowdfunding includes:

#### **3.5.1 Anti-Money Laundering**

The compliance requirements of the current anti-money laundering framework in Ireland are set out in The Criminal Justice (Money Laundering and Terrorist Financing) Act 2010, as amended by Part 2 of the Criminal Justice Act 2013.

A draft Criminal Justice (Money Laundering and Terrorist Financing) (Amendment) Bill is currently being prepared to amend this framework and to give effect to the 4th EU Anti-Money Laundering Directive ("AMLD 4"). AMLD 4 will strengthen laws in the EU which combat money laundering and terrorist financing and must be transposed into Irish law by 26 June 2017.

#### **3.5.2 Data Protection**

The Data Protection Acts 1988 and 2003 (the "DPA") contain the Irish legislative provisions concerning the collection, use and disclosure of personal data and sensitive personal data. However, the DPA will soon be replaced by the EU General Data Protection Regulation ("GDPR") which will make businesses more accountable for data privacy compliance and offers citizens extra rights and more control over their personal data. The new rules come into effect on 25 May 2018 and will have a significant impact for all organisations, including Crowdfunding companies.

#### **3.5.3 Consumer Credit**

A person, other than a credit institution or a mortgage lender, who in the course of his business arranges or offers to arrange for a consumer the provision of credit in return for a commission, payment or consideration of any kind from the provider of the credit is considered a "credit intermediary" under the Consumer Credit Act 1995. A "consumer" is defined as a natural person acting outside their business.

A Crowdfunding platform using the Lending Model is most likely to fall within this definition and would therefore be required to obtain a regulatory authorisation as a credit intermediary and comply with the relevant obligations under Part XI of the Consumer Credit Act 1995. The Competition and Consumer Protection Commission (the "CCPC") is the statutory body responsible for the regulation of credit intermediaries in Ireland. The authorisation process is relatively simple to obtain and inexpensive relative to other regulatory authorisations.

However, it is also worth noting that all non-bank lenders of consumer credit operating in Ireland (i.e. any firm other than a credit institution that is engaged in the business of providing credit to natural persons) are required to hold a retail credit firm authorisation issued by the CBI under Part V of the Central Bank Act 1997. This is a much more significant authorisation than a credit intermediary authorisation and should not be entered into lightly as considerable human and financial resources are required to establish and maintain such an authorisation. As lending to consumers is extensively regulated in Ireland, most Irish Crowdfunding platforms using the Lending Model have focused their efforts on arranging credit for corporate entities instead.

#### 3.5.4 Company Law

A Crowdfunding company may be considered to be a "credit institution" under the Companies Act 2014, the definition of which includes:

- a company or undertaking that is the holder of a licence under section 9 of the Central Bank Act 1971; and
- a company or undertaking engaged in the business of accepting deposits or other repayable funds or granting credit for its own account.

The drafting of this definition has caused some confusion in Ireland and the second bullet point above is due to be amended to apply to "a company or undertaking engaged in the business of accepting deposits or other repayable funds from the public and granting credit for its own account".

If a company constitutes a credit institution then it cannot be a simple private limited company limited by shares (LTD) under Irish company law and must instead be registered as a designated activity company (DAC), if it wishes to have the status of a private limited company. The main implications of this for a Crowdfunding company are that:

- a DAC must have a minimum of two directors;
- a DAC must have a memorandum and articles of association, including an objects clause in the memorandum of association; and
- a DAC cannot dispense with holding physical AGMs in the same way as a LTD.

However, any conclusion that a Crowdfunding company was a credit institution under the Companies Act 2014 would need to be assessed on the basis of the applicable business model and the specific circumstances, bearing in mind the upcoming change to the definition.

#### 3.5.5 Investment Services

At its simplest, authorisation from the CBI as a MiFID investment firm enables MiFID firms to provide "investment services" in respect of "financial instruments". For this purpose, "investment services" is defined in Schedule 1 of the European Communities (Markets in Financial Instruments) Regulations 2007 (the "MiFID Regulations"). This legislation (and MiFID II – its incoming replacement) is relevant to Crowdfunding platforms using the Equity

Model because aspects of their business may involve the provision of certain regulated investment services, including some or all of:

- receiving and executing orders for financial instruments;
- executing orders on behalf of clients; and
- providing investment advice to clients.

An alternative course of action would be to apply to the CBI for authorisation as an investment business firm under the Investment Intermediaries Act 1995 ("IIA 1995"). It is important to be aware that the types of regulated activity that an investment business firm is permitted to carry out under IIA 1995 are far more restrictive than for a MiFID investment firm. It would also be necessary for any Crowdfunding platform using the Equity Model to limit its activities in order to avail of an exemption from having to obtain authorisation as a MiFID investment firm under the MiFID Regulations.

Regulation 5(3) of the MiFID Regulations provides that a person whose home Member State is Ireland and whose activities are regulated by the CBI (i.e. a regulated entity such as an investment business firm under the IIA 1995) and who meets the following three criteria is exempt from the MiFID Regulations:

- the person must not be allowed to hold clients' funds or securities and therefore is not allowed at any time to place itself in debit with its clients;
- the person must not be allowed to provide any investment services, except receiving and transmitting orders in transferable securities and UCITS funds and providing investment advice in relation to transferable securities and UCITS funds; and
- in the course of providing those services, the person may only transmit those orders to certain specified entities (e.g. MiFID investment firms, credit institutions, branches of MiFID investment firms or credit institutions, certain collective investment undertakings and their managers and investment companies with fixed capital).

The main advantage of seeking an authorisation under the IIA 1995 is that the application process is a much less complex process than a MiFID authorisation in terms of time (although there is no statutory time limit for the CBI to process these applications) and expense. However, the main drawback is that the scope for even providing investment advice to clients is highly restricted (i.e. to a limited range of financial instruments) and accordingly, any Crowdfunding platform with this limited form of regulatory authorisation would need to be very cautious as to what services it can legally provide.

Obtaining authorisation as a MiFID investment firm is a complex, expensive and lengthy process and holding such an authorisation involves substantial on-going regulatory obligations. The alternative option of authorisation as an investment business firm is also

quite restrictive. In light of this, it is unsurprising that there are so few equity Crowdfunding platforms currently operating in Ireland.

## 4 Regulatory barriers for Crowdfunding crossing borders

A report by the International Organization of Securities Commissions published in December 2015 noted that "despite certain commonalities and divergences in various jurisdiction, and the potential risks and positive rewards, Crowdfunding regimes are in their infancy (or have not yet launched) in most jurisdictions". This report also noted that there is no common international approach to regulating Crowdfunding. In Ireland, a Joint *Oireachtas* (Irish Parliament) Committee on Jobs, Enterprise and Innovation issued a report in July 2014 in which it recommended, among other things, that "the Government should examine how to regulate the crowd-funding sector to afford better protection to both lenders and businesses".

As we have seen, there is no defined regulatory framework for Crowdfunding in Ireland, with it instead involving multiple aspects of Irish and European legislation which may or may not apply on a case-by-case basis. In the absence of a clear regulatory regime specifically addressing Crowdfunding, these laws are likely to act as a strong barrier to the development of Crowdfunding, particularly the Equity Model and Lending Model – both of which have the most potential to create employment and growth.

### 4.1 Applicable Law

It was noted in the European Commission's report "Crowdfunding in the EU Capital Markets Union" published in April 2016, that Crowdfunding is primarily currently carried out on a national basis and that there is a low volume of cross-border activity. Despite this observation, if a person is resident, registered or operating within the jurisdiction of Ireland then they will likely be subject to Irish laws, including financial services legislation. As discussed above, there is a multitude of financial services legislation that could apply to either inbound or outbound Crowdfunding activities. Due to these complications, it is essential that tailored advice be sought by any Crowdfunding platform operating in Ireland as to the applicable legislation and regulatory regimes in order to ensure its activities are fully compliant with Irish law.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addresses Irish investors

If a foreign Crowdfunding platform wishes to address Irish investors then that Crowdfunding platform may be subject to Irish laws if it is deemed to be operating in Ireland. As discussed in detail above, possible regulatory barriers to such situations may include:

- a requirement under the Central Bank Act 1971 to obtain a banking licence if engaged in deposit taking from customers. It is therefore very important that any Crowdfunding platform does not engage in the regulated activity of a "banking business" without the necessary authorisation;

- AIFMD rules, which may be applicable in terms of the legal, regulatory, risk monitoring and process elements of alternative investment fund management;
- a requirement to become an authorised payment institution under PSD 1 (and PSD 2, when applicable);
- a requirement under the Central Bank Act 1997 for certain Crowdfunding platform business models to obtain a regulatory authorisation as money transmission businesses;
- other additional Irish legislation which may be applicable including anti-money laundering and data protection obligations;
- if engaged in lending to consumers, a requirement to obtain a regulatory authorisation as a credit intermediary and comply with the relevant obligations under the Consumer Credit Act 1995; and
- depending on the type of business model a foreign Crowdfunding platform operates, it may need to ensure it is compliant with the MiFID Regulations or seek an authorisation under the IIA 1995.

#### **4.2.2 Foreign Crowdfunding platform addresses Irish companies / projects**

If a foreign Crowdfunding platform wishes to address Irish companies and/or projects then those companies and/or projects may be subject to Irish laws if the companies are incorporated under the laws of Ireland or the projects are deemed to be operating in Ireland. As discussed in detail above, possible regulatory barriers to such situations may include:

- compliance with the Prospectus Directive and the Prospectus Regulation (once implemented) in terms of the requirements for prospectuses relating to securities offered to the public or admitted to trading on a regulated market within the EU;
- other additional Irish legislation which may be applicable including consumer protection and data protection obligations; and
- general company law requirements under the Irish Companies Act 2014.

### **4.3 Outbound**

#### **4.3.1 Irish Crowdfunding platform addresses foreign (EU) investors**

If an Irish Crowdfunding platform wishes to address foreign (EU) investors then that Crowdfunding platform would be subject to all applicable Irish laws which regulate the operation of a Crowdfunding platform, including:

- the Central Bank Act 1971 requirement to obtain a banking licence if it is engaged in deposit taking from customers;
- the Central Bank Act 1997 requirement to obtain a regulatory authorisation as a money transmission business;
- other additional Irish legislation may be applicable including anti-money laundering and data protection obligations; and

- if engaged in lending to consumers, the requirement under the Consumer Credit Act 1995 to obtain a regulatory authorisation as a credit intermediary.

An Irish Crowdfunding platform would also need to comply with the requirements of all applicable European legislation, including AIFMD, PSD 1, PSD 2 (when applicable), MiFID, MiFID II (when applicable), etc. These requirements are discussed in detail above. Finally, it is also possible that an Irish Crowdfunding platform would also be subject to the laws and regulations applicable in whatever jurisdiction it sought to address foreign companies and/or projects.

#### **4.3.2 Irish Crowdfunding platform addresses foreign (EU) companies / projects**

If an Irish Crowdfunding platform wishes to address foreign (EU) companies and/or projects then that Crowdfunding platform would be subject to all applicable Irish laws which regulate such companies and/or projects. As stated above, compliance with all applicable EU and local laws and regulations would also be required.

#### **4.4 Impact of EU regulation**

EU regulation has resulted in several distinct and applicable pieces of Irish legislation, including the Prospectus (Directive 2003/71/EC) Regulations 2005 (which implemented the Prospectus Directive) and the European Communities (Payment Services) Regulations 2009 (which implemented PSD 1). It has also given rise to pan-European legislation such as the MiFID Regulations and AIFMD. There are also several legislative changes expected in the near future, including PSD 2, MiFID II and AMLD 4.

The introduction of this EU regulation has created a series of legal and regulatory obstacles which make it difficult in practice for any Crowdfunding platform, whether in Ireland or another Member State, to scale significantly without first obtaining certain authorisations or even becoming a regulated financial services provider. In the absence of a bespoke regulatory regime for Crowdfunding platforms, it is possible that several regulatory authorisations may in fact be required to operate a Crowdfunding platform in Ireland, depending on the business model used, creating significant regulatory barriers.

#### **4.5 Summary**

There are now significant regulatory barriers to an Irish Crowdfunding platform expanding outside Ireland, or indeed a foreign Crowdfunding platform expanding in to Ireland, given the increasing level of financial services legislation in Ireland, in individual Member States and at a European level. Without a consistent approach to Crowdfunding regulation throughout the EU these regulatory barriers prevent European Crowdfunding platforms from achieving significant scale and competing on a both a European and global basis.

## 5 Lessons learned from Ireland's regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model ("dos")

As Crowdfunding is not specifically regulated in Ireland there are few lessons that can be learned. However, the recent public consultation may prove a useful method of collecting a wide array of industry views which in turn might better inform any potential regulation.

### 5.2 Aspects that should be avoided ("don'ts")

The primary lesson that can be learnt from the Irish market in terms of aspects that should be avoided is that a lack of clear and comprehensive regulation hinders the growth of the Crowdfunding sector as it deprives the industry of the legal certainty, legitimacy and consumer confidence that comes with being a regulated industry.

## 6 Conclusion

As an alternative source of finance for start-ups, charities, projects and more, Crowdfunding has the potential to disrupt the current norms and structures of lending and investment in Ireland, Europe and internationally. The creation of a bespoke regulatory framework could legitimise this emerging sector, address consumer protection concerns, and allow Crowdfunding to enter the mainstream leading to a shift in how finance and early stage funding is obtained.

There is a national and international focus on the importance of Crowdfunding, particularly around developing proper regulation and oversight. In doing so, it will be fundamental to balance the protection of consumers with the requirements of business. Given the limitations on traditional sources of finance in recent years, the regulation and emergence of Crowdfunding as a viable alternative would surely be a welcome development.

## 7 Summary – Crowdfunding Regulation

| Country   | Ireland  |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Currently no bespoke regulation of Crowdfunding in Ireland</li> <li>• Public consultation launched on 21 April 2017 regarding the potential regulation of Crowdfunding in Ireland</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Currently no bespoke regulation of Crowdfunding in Ireland.</li> <li>• Public consultation launched on 21 April 2017 regarding the potential regulation of Crowdfunding in Ireland.</li> <li>• Large body of related financial services legislation that is not expressly intended to apply to Crowdfunding but may nevertheless be applicable to Crowdfunding platforms in certain circumstances.</li> </ul>   |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus (Directive 2003/71/EC) Regulations 2005               <ul style="list-style-type: none"> <li>- Implement the Prospectus Directive (2003/71/EC).</li> </ul> </li> <li>• New Prospectus Regulation               <ul style="list-style-type: none"> <li>- Designed to repeal and replace the existing body of European prospectus law.</li> <li>- The two key changes from a Crowdfunding perspective are:                   <ol style="list-style-type: none"> <li>1. a higher threshold to determine when companies must issue a prospectus – EUR 1 million (up from EUR 100,000); and</li> <li>2. "EU growth prospectus" aimed at SME's and other small companies.</li> </ol> </li> </ul> </li> </ul> |
| <b>AIFMD-regulation</b>                               | <p>European Union (Alternative Investment Fund Managers) Regulations 2013</p> <ul style="list-style-type: none"> <li>- Implements the Alternative Investment Fund Managers Directive ("AIFMD").</li> <li>- Only applies to funds that manage assets of EUR 100 million or more.</li> <li>- Alternative investment funds must be authorised by the CBI and are subject to strict marketing conditions.</li> <li>- The most recent version of the AIF Rulebook was published by the Central Bank of Ireland in March 2017.</li> </ul>  |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• European Communities (Payment Services) Regulations 2009               <ul style="list-style-type: none"> <li>- Implements the first Payment Services Directive.</li> <li>- Aspects of Crowdfunding business models may involve the provision of certain regulated payment services.</li> </ul> </li> </ul>   |

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|---|--|
|   | <ul style="list-style-type: none"> <li>- Exemption from authorisation as a payment institution may be possible if payment transactions are conducted through a commercial agent acting on behalf of both the payer and payee.</li> <li>- Revised commercial agent exemption is much narrower in PSD 2 and may give rise to a requirement to obtain an authorisation as a payment institution from January 2018.</li> <li>• Part V of the Central Bank Act 1997             <ul style="list-style-type: none"> <li>- Regulates a "money transmission business".</li> <li>- Crowdfunding platforms should consider whether their business model may require them to obtain a regulatory authorisation as a money transmission business.</li> </ul> </li> </ul>   |
| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• Anti-Money Laundering             <ul style="list-style-type: none"> <li>- Criminal Justice (Money Laundering and Terrorist Financing) Act 2010, as amended by Part 2 of the Criminal Justice Act 2013.</li> <li>- A draft Criminal Justice (Money Laundering and Terrorist Financing) (Amendment) Bill is currently being prepared to amend this framework to give effect to the 4th EU Anti-Money Laundering Directive.</li> </ul> </li> <li>• Data Protection             <ul style="list-style-type: none"> <li>- The Data Protection Acts 1988 and 2003 are due to be replaced by the EU's General Data Protection Regulation, which will make businesses more accountable for data privacy compliance and offers citizens extra rights and more control over their personal data from 25 May 2018.</li> </ul> </li> <li>• Consumer Credit             <ul style="list-style-type: none"> <li>- Consumer Credit Act 1995.                 <ul style="list-style-type: none"> <li>⇒ Regulates "credit intermediaries" who in the course of business arrange or offer to arrange for a consumer the provision of credit in return for a commission, payment or consideration of any kind from the provider of the credit.</li> <li>⇒ Lending Model is most likely to fall within this definition and would therefore require a regulatory authorisation as a credit intermediary and compliance with the relevant obligations.</li> <li>⇒ The Competition and Consumer Protection Commission (the "CCPC") is the statutory body responsible for the regulation of credit intermediaries in Ireland.</li> <li>⇒ The authorisation process is relatively simple and inexpensive compared to other regulatory authorisations.</li> </ul> </li> <li>- Part V of the Central Bank Act 1997</li> </ul> </li> </ul> |

|                            |   |
|----------------------------|---|
|                            | <ul style="list-style-type: none"> <li>⇒ Regulates all non-bank lenders of consumer credit operating in Ireland known as "retail credit firms".</li> <li>⇒ Must hold a retail credit firm authorisation issued by the CBI.</li> <li>⇒ Significant authorisation and considerable human and financial resources are required.</li> <li>• Company Law <ul style="list-style-type: none"> <li>- Companies Act 2014 <ul style="list-style-type: none"> <li>⇒ May be considered to be a "credit institution"</li> <li>⇒ If a company constitutes a credit institution then it must be registered as a designated activity company (DAC). <ol style="list-style-type: none"> <li>1. DAC must have a minimum of two directors;</li> <li>2. DAC must have a memorandum and articles of association, including an objects clause in the memorandum of association; and</li> <li>3. DAC cannot dispense with holding physical AGMs in the same way as a LTD.</li> </ol> </li> </ul> </li> </ul> </li> <li>• Investment Services <ul style="list-style-type: none"> <li>- European Communities (Markets in Financial Instruments) Regulations 2007 (as amended) <ul style="list-style-type: none"> <li>⇒ Implements the EU Markets in Financial Instruments Directive ("MiFID").</li> <li>⇒ Regulates provision of "investment services" in respect of "financial instruments".</li> <li>⇒ Authorisation as an investment firm from the CBI.</li> <li>⇒ Regulation 5(3) of the MiFID Regulations sets out exemption in specific circumstances.</li> <li>⇒ Complex, expensive and lengthy process.</li> <li>⇒ Substantial on-going regulatory obligations.</li> <li>⇒ MiFID II coming into effect in January 2018.</li> </ul> </li> <li>- Investment Intermediaries Act 1995 <ul style="list-style-type: none"> <li>⇒ Apply to the CBI for authorisation as an investment business firm.</li> <li>⇒ More restrictive authorisation than a MiFID investment firm.</li> </ul> </li> </ul> </li> </ul> |
| <b>Regulatory barriers</b> |   |
| <b>Inbound</b>             | <ul style="list-style-type: none"> <li>• Crowdfunding is primarily currently carried out on a national basis and there is a low volume of cross-border activity.</li> </ul>   |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>• If a foreign Crowdfunding platform wishes to address Irish investors then that Crowdfunding platform may be subject to Irish laws if it is deemed to be operating in Ireland.</li> <li>• If a foreign Crowdfunding platform wishes to address Irish companies and/or projects then those companies and/or projects may be subject to Irish laws if the companies are incorporated under the laws of Ireland or the projects are deemed to be operating in Ireland.</li> <li>• Multitude of financial services legislation that could apply to inbound Crowdfunding activities.</li> </ul>   |
| <b>Outbound</b>                | <ul style="list-style-type: none"> <li>• Crowdfunding is primarily currently carried out on a national basis and there is a low volume of cross-border activity.</li> <li>• If an Irish Crowdfunding platform wishes to address foreign (EU) investors then that Crowdfunding platform would be subject to all applicable Irish, EU and local laws which regulate the operation of a Crowdfunding platform.</li> <li>• If an Irish Crowdfunding platform wishes to address foreign (EU) companies and/or projects then that Crowdfunding platform would be subject to all applicable Irish, EU and local laws which regulate such companies and/or projects.</li> <li>• Multitude of financial services legislation that could apply to outbound Crowdfunding activities.</li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | See above  |
| <b>AIFM-Directive</b>          | See above  |
| <b>MiFID / MiFID II</b>        | See above  |
| <b>PSD / PSD II</b>            | See above  |

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# Israel

## 1 Recent developments in the market of crowdfunding in Israel

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

As will be discussed below, regulations for equity crowdfunding in Israel have been adopted but did not become effective yet. Therefore, the current "equity crowdfunding" market in Israel is limited. There are a few platforms that operate under the current regulatory regime, and offer and sell securities only to accredited investors and to a limited number of individual as permitted under general securities regulations.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There is a number of platforms, operating in Israel since 2013, that offer peer to peer lending. The platforms are not required to cooperate with commercial banks. As of March 2016, the main platforms have loaned a total amount of NIS 100 million (USD 28 million) according to their own reports. The overall amounts of peer to peer lending are still a small fraction of the total consumer credit market in Israel, which is controlled by commercial banks, credit cards companies, pension funds and insurance companies.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

There is a number of platforms, operating in Israel since 2011, that raise money mainly for social or creative projects for no return or for non-monetary rewards. Overall fees, including clearing, range from 3% to 9% from the amounts raised, plus VAT.

### 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

There is no specific legislation in Israel. Lately, the Israeli Securities Authority ("ISA") has been closely monitoring real estate funds that try to raise money from the public, to ensure compliance with securities regulation. We are not aware of any crowdfunding platforms in Israel that focus on renewable technologies.

### 1.5 International approach

Foreign platforms that desire to operate in Israel and approach the Israeli public need to comply with the same regulations as local platforms. For more details refer to Section 4 of this article.

## 2 Recent developments regarding Crowdfunding regulation in Israel

### 2.1 Securities Regulations (Offer of Securities through an Offering Coordinator), 5777-2017

The Securities Law, 5728-1968 (the "Securities Law") was amended to allow equity crowdfunding (Section 15B(4A) of the Securities Law). Nevertheless, without the applicable regulations it had no practical effect. Finally, the Securities Regulations (Offer of Securities through an Offering Coordinator), 5777-2017 (the "Crowdfunding Regulations") were approved on March 2017, published on June 26, 2017, and will become effective six months after they are published. Under the Crowdfunding Regulations, equity crowdfunding will be permitted in Israel, under strict limitations. The Crowdfunding Regulations are discussed in Section 3.2 below.

## 3 Current Regulation of Crowdfunding in Israel

### 3.1 General Legal Framework

Pursuant to the Israeli Securities Law, 5728 - 1968 (the "Securities Law"), an offer of securities to the public in Israel requires a prospectus approved by the ISA. Specifically, Section 15 of the Securities Law provides that "(a) No person shall offer securities to the public other than according to a prospectus, the publication of which has been authorized by the ISA...(b) No person may sell securities to the public other than according to a prospectus, the publication of which has been authorized by the ISA."

An "offer" is defined in Section 1 of the Securities Law as any action intended to induce the public to purchase securities, including, inter alia, any approach to the public to make offers to purchase securities. While the term "offer" has been intentionally interpreted in a wide manner by the courts, it should be noted that the ISA has clarified the term "Public" (for Security Law purposes) to include Israeli residents only, thereby excluding offerings targeting non-Israeli investors.

The approach taken by the Israeli courts with regards to interpretation of the term "offer" is similar to the approach taken by US courts. For example, the court has determined that the mere commencement of a process with the intention to cause the public to purchase securities, including any marketing activities, may be deemed an "offer" under the Securities Law. Since an "offer" includes an invitation to the public to make offers to buy securities, the term "offer", for the purposes of the Securities Law, does not require the same degree of willingness and definitiveness as a contractual offer requires. Such offer may be conditional, subject to changes, or open for further negotiation, and still be considered an offer of securities to the public. The same conclusion can be reached from the fact that under Amendment #24 of the Securities Law an offer to the public can be made, under certain circumstances, under a draft prospectus without the definite terms of the offer. Furthermore, the terms of the offered securities, including price and amount, may be amended after the prospectus is published and

before orders are received. The conclusion is that an "offer" under the Securities Law has a substantially wider scope than an "offer" under contract law.

### 3.2 Exemptions from the Security Law Restrictions

The Securities Law and regulations promulgated thereunder include certain exemptions from the prospectus requirement. Such exemptions include, inter alia:

- When securities are offered to no more than 35 investors during any rolling twelve-month period;
- When securities are offered to certain types of sophisticated investors, including banks, mutual funds, investment managers, investment advisors, underwriters, venture capital funds, and large corporations with equity of at least NIS 50 million (approximately USD 14 million).
- When securities are offered to individuals that meet one of the following criteria:
  - Have liquid assets with total value exceeding NIS 8 million (approximately USD 2.2 million);
  - Have annual income of at least NIS 1.2 million (approximately USD 330,000) in recent two years; or
  - Have liquid assets with total value exceeding NIS 5 million (approximately USD 1.4 million) and annual income of at least NIS 600,000 (approximately USD 166,000) in recent two years.
- Sale for up to NIS 2.6 million (approximately USD 720,000) of up to 5% of the outstanding capital of the issuer in each offering and 10% in the aggregate, for up to 75 investors.

An offer or sale to investors who reside or are incorporated outside of Israel is not deemed an "offer to the public" under the Securities Law and consequently does not require a prospectus. The condition is that, in the opinion of the ISA, the foreign investors are capable of obtaining the information which they require in order to make a decision to invest in the securities and which would have appeared in a prospectus, had a prospectus been published (Section 15A(B)(2) of the Securities Law). It should be noted that non-Israeli securities laws may apply.

### 3.3 Publication

According to the Securities Law (Section 15A(A)(4)), a general publication of the intent to sell securities to no more than 35 investors (to be selected according to a defined procedure) or to certain sophisticated investors shall not be deemed an offering to the public and therefore does not require a prospectus. The publication must NOT include financial information and offering details, including price, interest and return. The publication must state that the offering and sale of securities is limited to a certain number and/or type of investors.

In a position paper dated July 4, 2017, the ISA clarified that this section must not be used to circumvent the prohibition on offer to more than 35 offerees. To achieve this goal, this

section was amended on December 31, 2015, in order to clarify the content of the publication. The ISA clarified that the publication must not include any financial information, both regarding the issuer and the offering. In addition, the ISA determined that the publication must not include (i) scope of previous financing rounds, (ii) expected returns from investments or projects of the issuer, (iii) returns from prior investments of the issuer, (iv) financing and cost of proposed projects of the issuer, and (v) data regarding sales or investments of the issuer. However, it is allowed to provide the minimum investment amount that the issuer will accept. The publication must be general and state only the intent to offer securities. The publication must not ask the public to make offers to purchase securities, as this is deemed an "offer" to the public which is restricted under the Securities Law.

Subject to these strict limitations, an offeror may be able to rely on this provision of the Securities Law in order to promote a proposed offering that will be later sold to a selected group of investors in compliance with the exemptions from the prospectus requirement. The content of the publication and any communication with potential investors should be carefully monitored according to Securities Law and ISA guidelines discussed above.

### **3.4 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)**

Crowdfunding, as any other attempt to raise capital through the issuance of equity, is subject to the Securities Law. Crowdfunding is mainly governed by the Securities Regulations (Offer of Securities through an Offering Coordinator), 5777-2017 (the "Crowdfunding Regulations"). The Crowdfunding Regulations were approved on March 2017, published on June 26, 2017 and will become effective six month after they are published. The Crowdfunding Regulations regulate the crowdfunding process. Some of the terms stipulated in the Crowdfunding Regulations are as follows:

- The offering to the crowd has to be made through an offering coordinator. An offering coordinator must be registered with, and regularly report to, the ISA. The offering coordinator has an obligation to take reasonable steps to ensure compliance with the Crowdfunding Regulations and to prevent fraud.
- The Crowdfunding Regulations govern the information that must be disclosed to the public with respect to an offering of securities, including the number and price of the offered securities, offering period, use of proceeds, prior offerings, financials statements, business plan, risk factors, ownership, directors, and interested party transactions.
- The offering coordinator will pay an annual fee of NIS 50,000 (approximately US D 14,000) plus 2% of the total amount raised through the offering coordinator (1% in the first two years after the Crowdfunding Regulations become effective).
- The maximum amount an issuer may raise in a single offering or a number of offerings during a given rolling 12-month period is limited to NIS 4 million (approximately USD 1.1 million). However, there are exceptions to this rule. If an

issuer that has R&D activity has received a report from the Israeli Innovation Authority (or, for non R&D companies, a report from the Small and Medium Business Authority at the Israeli Ministry of Economy) providing some validation to its business plan, then the maximum amount that the issuer may raise through the offering increases by additional NIS 1 million. If at least one Lead Investor participates in the offer, then the maximum amount increases by another NIS 1 million. A “Lead Investor” is required to invest at least 10% of the total investment amount. The Lead Investor is an individual who is unaffiliated with the issuer and who has made at least five investments in R&D companies in the previous five years, or an institutional investor. All investors will be entitled to participate in future sales of shares by the Lead Investor on a pro-rata basis. This means that the maximum potential amount an issuer may raise in a given 12-month period, if all conditions and qualifications are met, is NIS 6 million (approximately USD 1.66 million).

- Restrictions exist with regards to not only the total amount an issuer may raise within the framework of an offering, but also with regards to how much a single investor may invest. The amount of financing from a single investor is limited to NIS 10,000 (approximately USD 2,800) in a single investment and a total of NIS 20,000 (approximately USD 5,600) during a period of 12 months. However, these amounts increase if the investor's income is above a defined threshold, up to 5% of the investor's annual income.

### **3.5 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

On July 27, 2014, the ISA published a proposal for debt crowdfunding for small and medium businesses. The main principles of the proposed regulations include:

- A company may raise up to NIS 1 million (USD 277,000) of debt in 12 months in crowdfunding campaigns.
- If a “Sophisticated Investor” participates, the maximum amount is increased to NIS 2 million (USD 555,000). A Sophisticated Investor is defined as an institutional investor or a wealthy individual.
- Approval or actual investment by the Small and Medium Businesses Authority at the Israeli Ministry of Economy is required.

Each investor may lend up to NIS 10,000 (Approximately USD 2,800) in 12 months and up to NIS 5,000 (Approximately USD 1,400) in a single transaction.

Lending model platforms may be subject to regulations related to loans. Additionally, if credit data of borrowers is stored and used, a lending model platform may need a license as a credit data service.

### **3.6 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

This model is generally out of the scope of securities laws and no prospectus is required, as it does not involve acquisition of interest, profit sharing or any financial return. There are several platforms in Israel that operate donations or rewards Crowdfunding. The participants do not expect a financial profit. They receive either no return or a non-monetary reward that is not linked to the profit of the project (e.g. a copy of the book created with their support). Based on the operation of these platforms, they may not be subject to any regulation related to sale of equity or debt instruments. Consumer protection regulations may apply.

### **3.7 Real Estate Crowdfunding/Renewable Crowdfunding**

There is no specific legislation in Israel. Any offering will be subject to the regulations discussed above.

## **4 Regulatory Barriers for Crowdfunding Crossing Borders**

### **4.1 Applicable Law**

Israeli securities laws apply to offers of securities to the public in Israel. Therefore, Israeli securities laws do not apply to offers of securities to potential investor outside of Israel (including by Israeli issuers), but apply to offers by foreign issuers to the public in Israel. Amendment 20 to the Securities Law determines that Israeli law applies to all securities offerings addressed to the public in Israel and does not apply to securities offerings addressed to the public out of Israel.

In a position paper from 2015, the ISA stated that if an offering is carried out in Israel, then the number of permitted offerees (35) should include offerees that are not citizens or residents of Israel. If an offering is not carried out in Israel, then the number of offerees in such offering shall be deducted from the number of offerees to which the issuer is permitted to offer securities through an offer carried out in Israel.

In a position paper dated July 4, 2017, the ISA stated that both the characteristics and relation to Israel of the offering and the characteristics and relation to Israel of each offeree need to be reviewed.

A review of an offering shall include, inter alia:

- A. Identification of the location where the marketing and sale of the offered securities actually take place, either through the internet, voicemails, investors conferences, individual meetings etc.
- B. Language of the communication with the offerees.
- C. Language of the offering document and marketing materials.

A review of an offeree shall include, inter alia:

- A. Residency.

## B. Location where the offeree manages his/her business.

To summarize, foreign issuers without a place of business in Israel may be captured by Israeli law in case they target Israeli investors. A potential issuer has to determine if the proposed offering is addressed to the public in Israel. The criteria offered by the ISA in the position paper discussed above can serve as the initial framework. If the offering is deemed to be addressed to the public in Israel, then the offering has to comply with Israeli law, as discussed in Sections 1-3 of this article.

### 4.2 Inbound

The question is whether a foreign crowdfunding platform addresses Israeli investors or presents foreign companies or projects.

#### 4.2.1 Foreign Crowdfunding platform addresses Israeli investors

The question is whether Israeli law applies to issuers or platforms that address the Israeli public. As discussed above, Israeli law applies to any offering of securities that is addressed to the public in Israel. To determine whether an offering is addressed to the Israeli public, the ITA offered the following criteria: (i) location where the marketing and sale of the offered securities actually take place, either through the internet, voicemails, investors conferences, individual meetings etc. and (ii) language of communication, and language of offering and marketing materials. It should be noted that these criteria were offered by the ITA in a different context and not in connection with crowdfunding offerings. In the event that it is determined that a crowdfunding offering is addressed to the public in Israel, the issuer or platform will have to comply with all applicable Israeli law and regulations, including the Crowdfunding Regulations (as defined above). The requirements from a crowdfunding platform under Israeli law are discussed in Section 3 of this article.

##### 4.2.1.1 Crowdfunding Platform

- **License obligation:** An offering coordinator (i.e. the crowdfunding platform) must be an Israeli company. An offering coordinator must be registered with, and regularly report to, the ISA. The offering coordinator will pay an annual fee of NIS 50,000 (approximately USD 14,000) plus 2% of the total amount raised through the offering coordinator (1% in the first two years after the Crowdfunding Regulations become effective). The offering coordinator must have appropriate insurance to cover its liability towards the investors. The offering coordinator shall deposit an amount of at least NIS 100,000 (approximately USD 30,000) in trust to secure its liability under the Securities Law. At least one third of the directors of the offering coordinator shall satisfy independence criteria under the securities law. Therefore, if Israeli law applies to the offering (as discussed in Section 4.2.1 above), the offering to the public must be performed through an offering coordinator that is registered with the ISA and complies with the terms and conditions discussed above.

- **Other regulations:** If Israeli law applies to the offering, additional regulations as discussed in Sections 4.4-4.6 may apply.

#### **4.2.1.2 Foreign company/projects**

- The question is whether Israeli law applies to offerings by foreign companies or of foreign projects. Regardless of the identity of the issuer or project, the question is whether the offering is made to potential investors in Israel. If it is, Israeli securities laws apply, regardless of the identity of the issuer or the project. See the criteria used to determine whether an offering is made to the public in Israel in Section 4.1.

#### **4.2.2 Foreign Crowdfunding platform addresses Israeli companies**

As discussed above, Israeli securities laws apply to offerings to potential investors in Israel. As long as the offering is not addressed to the public in Israel, Israeli securities laws do not apply. This may include offering by foreign crowdfunding platforms of Israeli issuers. Section 4.1 of this article.

### **4.3 Outbound**

The question is whether Israeli law applies to Israeli issuers or platforms that do not address the Israeli public.

As discussed above, Israeli law applies only to an offering of securities that is addressed to the public in Israel. It does not apply if the offering is not addressed to the public in Israel, even if the issuer or platform is an Israeli entity. The determination criteria are discussed in Section 4.1 of this article.

#### **4.3.1 Israeli Crowdfunding platform addresses foreign investors**

Regardless of the identity of the platform or issuer, the criterion is whether the potential investors are in Israel. See discussion in Section 4.3 above.

#### **4.3.2 Israeli Crowdfunding platform addresses foreign companies/projects**

Regardless of the identity of the platform or issuer, the criterion is whether the potential investors are in Israel. See discussion in Section 4.3 above.

### **4.4 Impact of EU regulation**

As Israel is not an EU member-state, the European regulation is not applicable

### **4.5 Possible additional regulations such as anti-money laundering laws, data privacy laws, consumer credit regulation, etc:**

- Prohibition on Money Laundering Law, 5760 – 2000
- Standard Contracts Law, 5743 – 1982
- Consumer Protection Law, 5741 – 1981

- Regulation of Non-Banking Loans Law, 5753 – 1993 and other consumer regulations

## 5 Lessons learned from Israel regulation

### 5.1 Role Model (“dos”)

As the Crowdfunding Regulations have not become effective yet, it is still to be seen how the proposed crowdfunding model will work in practice. It seems that the Israeli model is focused on protecting the public investors, and therefore includes certain elements to that effect:

- A. Limitation on investment amount.
- B. Crowdfunding platforms are subject to registration and reporting requirements.
- C. Professional investors are encouraged participate.
- D. The issuer is encouraged to seek review from regulatory authorities.
- E. Certain periodic reporting requirements.
- F. Crowdfunding platforms have an obligation to take reasonable steps to ensure compliance with the crowdfunding regulations and to prevent fraud
- G. Issuer has to disclose certain information to the public.

### 5.2 Aspects that should be avoided (“don’ts”)

Some critics believe that in the effort to protect the public, the proposed regulations are too burdensome, costly and may cause the entire process not to make financial sense in many cases. The argument is that the combination of the relatively low amounts that may be raised (in the aggregate and from each investor), together with the added costs of platform fees and the reporting requirements, may make this funding route less attractive to issuers. Some issuers may be less inclined to disclose information to the public that private companies are not required to disclose under Israeli law. Some argue that professional investors will not want to participate as “Lead Investors” due to potential exposure. Another argument is that the fees imposed on crowdfunding platforms are too high, especially given the duties imposed on the platforms.

## 6 Conclusion

While the number of high-tech startups per capita in Israel is among the highest in the world, the phenomenon of crowdfunding, which has become an increasingly popular source of alternative financing for high-tech startups, has been slow in making its way to the shores of the "Startup Nation". Recent regulations finally set the regulatory framework for equity crowdfunding in Israel. As the regulations have not become effective yet, it is still to be seen how the proposed crowdfunding model will work.

## 7 Summary – Crowdfunding Regulation

| Country   | Israel   |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | Equity crowdfunding is permitted under the Securities Regulations (Offer of Securities through an Offering Coordinator), 5777-2017 which were approved on March 2017, published on June 26, 2017, and will become effective six month after they are published.  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• If securities are offered, a prospectus is required unless an exemption is available.</li> <li>• Lending Model platforms may be subject to regulations related to loans.</li> <li>• If investment advice is provided, a platform may need an investment advisor license.</li> <li>• A platform may need to register its database if it contains sensitive information of its users.</li> <li>• If credit data of borrowers is stored and used, a Lending Model platform may need a license as a credit data service.</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus is required for offering securities to the public.</li> <li>• Exemptions include: <ul style="list-style-type: none"> <li>• Up to 35 investors in 12 months.</li> <li>• Certain institutional investors.</li> <li>• Wealthy individuals.</li> </ul> </li> </ul>   |
| <b>Crowdfunding requirements</b>                      | <ul style="list-style-type: none"> <li>• Offering must be through an offering coordinator, approved by the Israeli Securities Authority.</li> <li>• Certain information about the issuer and the offering must be disclosed.</li> <li>• Fundraising is limited to NIS 4 million, or NIS 6 million if certain conditions are met.</li> <li>• Investors may invest up to NIS 10,000 in a single investment and NIS 20,000 annually. Wealthy investors may invest higher amounts.</li> </ul>  |
| <b>Consumer credit regulation</b>                     | Regulation of Non-Banking Loans Law, 5753 – 1993 and other consumer regulations may apply to a Lending Model platform.   |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Prohibition on Money Laundering Law, 5760 – 2000</li> <li>• Standard Contracts Law, 5743 – 1982</li> <li>• Consumer Protection Law, 5741 – 1981</li> </ul>  |
| <b>Regulatory Barriers</b>                            | <ul style="list-style-type: none"> <li>• Israeli law applies to any offering of securities that is addressed to the public in Israel, regardless of the identity of the issuer.</li> </ul>   |

|                 |   |
|-----------------|---|
| <b>Inbound</b>  | <ul style="list-style-type: none"> <li>• Foreign crowdfunding platforms addresses Israeli investors - Israeli law applies to any offering of securities that is addressed to the public in Israel, regardless of the identity of the platform.</li> <li>• Crowdfunding platform – must comply with the requirements for an offering coordinator in the Securities Law.</li> <li>• Foreign Company/Project - Israeli law applies to any offering of securities that is addressed to the public in Israel, regardless of the identity of the issuer.</li> <li>• Foreign crowdfunding platforms addresses Israeli companies – same discussion as above, regardless of the identity of the issuer.</li> </ul>         |
| <b>Outbound</b> | <ul style="list-style-type: none"> <li>• Israeli crowdfunding platforms addresses foreign investors - Same discussion as above. Israeli law applies only to an offering of securities that is addressed to the public in Israel. It does not apply if the offering is not addressed to the public in Israel, even if the issuer or platform is an Israeli entity.</li> <li>• Israeli crowdfunding platforms addresses companies/projects - Same discussion as above. Israeli law applies only to an offering of securities that is addressed to the public in Israel. It does not apply if the offering is not addressed to the public in Israel, even if the issuer or platform is an Israeli entity.</li> </ul> |

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# Italy

## 1 Recent developments in the market of Crowdfunding in Italy

During the last years there were the following significant developments in Italy regarding Crowdfunding.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Equity Crowdfunding is mainly regulated by Law no. 221 of 17 December 2012 (Law 221/2012) and by CONSOB Regulation of 26 June 2013 n. 18592 as further amended by the CONSOB decision n. 19520 dated 25 February 2016 (CONSOB Regulation).

The regulation on Equity Crowdfunding has been expanded by the Decree Law n. 76 dated 28 June 2013, also known as “*Decreto Lavoro*” (duly implemented by the Law n. 99 dated 9 August 2013) and more recently by the Decree Law n. 3 dated 24 January 2015 (known as “*Investment Compact*” and duly implemented by the Law n. 33 dated 24 March 2015), that has introduced the possibility to access to equity Crowdfunding also for innovative SMEs (originally granted only for innovative start-ups) and it has granted to such companies some of the facilitations already provided for innovative start-ups by Law 221/2012.

Equity Crowdfunding is so available for: (a) innovative start-ups which meet requisites set forth in Law 221/2012 and that are enrolled in a special section of the Companies Register and for (b) innovative SMEs which meet requisites set forth in Law 33/2015. Such companies may offer their capital to the public through online Crowdfunding platforms registered in a special register held by CONSOB (Register of Platforms), provided that the overall amount of shares or quotas offered does not exceed EUR 5 million.

No MiFID application is required if the single investment is below EUR 500 and the overall investments during the year are below EUR 1.000.

Up to May 2017 there exist 18 authorized web portals in Italy. The offerings have been 99, of which 46 have been successful.

At the moment 19 offerings are still open, 5 of which have already reached the minimum target.

Such campaigns have been promoted, in particular, by 90 innovative start-ups, 6 innovative SMEs, and 1 innovative SMEs.

The total equity capital raised up to now is around EUR 10.328.66.

Some detailed examples: StarsUp, an equity Crowdfunding portal, has published 24 projects from the beginning of 2013 and, up to now, it has collected EUR 2.411 million as equity capital; CrowdFundMe, another equity Crowdfunding portal, has published 17 projects

from the beginning of year 2013 and, up to now, it has collected around EUR 1.301 million as equity capital.

The funding flow and the number of campaigns have been subjected to a rapid growth in the last few years. From the beginning of 2017, the funding flow has reached EUR 2,891 million and the campaigns have been 26, compared to the funding flow of the entire 2014 amounting to EUR 1,308 million with only 10 campaigns.

## **1.2 The Lending Model (individuals lend money to company or project in return for repayment of the loan and interest on their investment)**

According to this model individuals lend money to other individuals or companies (against interest and repayment of the loan) through a platform which acts as point of contact between borrowers and lenders.

At the beginning of 2017, five Italian platforms were active, three of which are addressed to individuals (*consumer lending*) and the remaining two are addressed to companies (*business lending*).

## **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

### **1.3.1 The Reward Model in Italy**

Under the Reward Model, individuals pay money to a company to support a project, or to buy products to be developed later on after completion of the campaign.

The reward could be of different kind: (a) gadgets of small value, (b) products sold at discounted price, (c) special rewards, likewise dedicated products/services.

The main issue faced by this model is concerning taxation of the money collected by means of the campaign, particularly with reference to the VAT application on presale/pre-order of products.

Also the applications of Italian laws and regulations concerning consumer rights protection is under assessment.

There are around 30 Italian platforms operating in the reward Crowdfunding market and the trend is of strong growth.

### **1.3.2 The Donation Model in Italy**

Under this model individuals provide money to a company or project *pro bono*, for charity or for other purposes but, in any case, without any valuable reward.

The Donations Model is mainly used to finance social, charity or creative projects or companies and no financial investment or return is involved.

This market is growing as well as the other Italian Crowdfunding markets, even if it is more difficult to define the trend of growth due to the lacking of available data.

## 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

There are no platforms that are offering real estate or renewable Crowdfunding in the Italian market. The model has not yet been developed, also with the purpose to comply with the existing laws and regulations.

### (1) Other Model

Profit-sharing Model is also allowed by Italian law. This model is under assessment in order to understand its potential benefits and the differences with the equity Crowdfunding, also in light of understanding whether or not it is subject to the same laws and regulations applicable to the equity Crowdfunding campaigns and platforms.

## 1.5 International approach

Finally, many lending platforms from other European countries entered the Italian market by establishing their local platforms.

The Payment Services Directive (directive 2007/64/CE), which has been implemented by the Italian Legislative Decree n. 11 dated 27 January 2010, has made it possible. In particular, PSD has introduced a set of rules which are equal and uniform for all European countries. Such Directive has supported the development of the market of payment services and has granted European countries with the possibility to develop their businesses by entering other European markets thanks to the absence of any regulatory barriers.

## 2 Recent developments regarding Crowdfunding regulation in Italy

### 2.1 Law 33/2015

Law n. 33/2015 has amended the provisions dealing with equity Crowdfunding transactions by allowing also Innovative SMEs and investment funds to raise funds by means of online Crowdfunding platforms.

Innovative SMEs are those referred to by the advice 2003/361/CE and to be allowed to raise online funding shall ask for an independent firm revision of the last available balance sheet; in additions these SMEs cannot have their shares be listed on a regulated market while can have the shares traded on MTF.

To be included in the Innovative SMEs register the companies shall have to meet at least two of the following three requirements:

- A. expenses relating to R&D equal or above the 3% of the higher between turnover and cost of the production;
- B. a part of the employees shall have to be graduated with a three year research experience or with a university research experience;

- C. own IP rights referring to industrial patent, biotech, new plant-related kind or original software code.

Also UE based start-ups and SMEs can be enrolled in the innovative register held by the Companies Register if meeting the above listed requirements and upon condition that the company has a branch or a production facility in Italy.

The law has amended also the Italian Consolidated Financial Act (Law 58/1998) allowing collective investment undertakings (investment funds) and investment companies (holdings) which invest primarily in innovative start-ups and in innovative SMEs to raise online funding by means of equity Crowdfunding platforms.

The last important provisions enforced by this new law is the possibility that shareholders of start-ups and SMEs incorporated as limited liability companies may sell the units representing the share capital by means of the financial intermediaries or online platform so authorised and without the need to follow the provisions of article 2470 of Italian Civil Code and avoiding the payment of the relevant taxes and expenses.

## 2.2 CONSOB regulation

On 25 February 2016, CONSOB (the Italian Authority dealing with financial markets) has issued the decision n. 19520, which amends the Regulation n. 18592/2013 applicable to equity Crowdfunding online platforms.

Such amendments have the main purpose to provide greater effectiveness to the disclosure of information, to expand the protections in relation to the provision of services and to reduce the costs. The main amendments are the followings:

- A. verification of the suitability of the investment with respect to the knowledge and experience of the investor (MIFID assessment) may be carried out, as of now, by the same portal managers if duly organised to do such activity;
- B. the number of those individuals which are authorized to subscribe a part of the bid as professional investors has been increased so that also business angels and venture capitalists have been included;
- C. any platforms authorised by CONSOB which will not be starting its operation within 6 months from the granting of the license will lose the license and be prevented to perform the activity.

## 2.3 Bank of Italy regulation

On November 2016, the Bank of Italy has finally adopted a resolution in accordance to which the P2P and P2B lending activity (so called in Italy *social lending*) has been recognised (Bank of Italy resolution 584/2016).

In particular, the lending activity has been permitted on condition that:

- A. the amount of funds is not significant (please note that the Bank of Italy has not provided neither a definition nor some criteria do determine the relevant threshold);
- B. the acquisition of funds is determined following specific and personalized negotiation between the lenders and the borrowers (please note that the Bank of Italy has not given any specific indications on such negotiation activities. It is, however, considered acceptable if the parties decide the amount of the lending (for the borrower the overall amount to be requested and for the lenders the relevant part of such amount that they intend to lend) and they expressly agree with the specific conditions of the lending, e.g. duration, amortisation plan and interest rate).

For those online platform willing to open and manage payment accounts, the Bank of Italy has set the need to apply for the Payment Service Provider or Electronic Money Issuer license or ask to passport the similar license granted by another European supervisory authority in the relevant home member state.

### 3 Current Regulation of Crowdfunding in Italy

#### 3.1 Licence requirements

##### 3.1.1 Equity Model

##### (1) Innovative start-ups / innovative SMEs

Under the Italian laws the possibility for companies to raise equity funds through a Crowdfunding campaign is limited only to:

- A. innovative start/ups;
- B. innovative SMEs;
- C. collective investment undertakings (investment funds) and investment companies (holdings) which invest primarily in innovative start/ups and in innovative SMEs.

In particular:

- A. innovative start-ups are companies (in general joint stock companies – “*Società per azioni*” and limited liability companies – “*Società a responsabilità limitata*”) which:
  - (i) are not listed on a regulated market;
  - (ii) have started their activity by no more than 60 months;
  - (iii) have their registered office in Italy or a branch or a production facility in Italy;
  - (iv) have total turnover of maximum EUR 5,000,000;
  - (v) have as exclusive company object the manufacturing and marketing of innovative products or services which are highly innovative.
- B. Moreover to be considered as an innovative start-up a company have also comply at least with one of the following three requirements: (i) expenses relating to R&D equal or above the 15% of the higher between turnover and cost of the production; (ii) part of the employees shall have to be graduated with a three year research

- experience or with a university research experience; (iii) ownership of IP rights referring to industrial patent, biotech, new plant-related kind or original software code;
- C. innovative SME's are instead companies (in general joint stock companies – “*Società per azioni*” and limited liability companies – “*Società a responsabilità limitata*”) which. (i) are not listed on a regulated market, but which can have the shares traded on MTF; (ii) have their registered office in Italy or a branch or a production facility in Italy; (iii) have independent firm revision of the last available balance sheet.
- D. In addition to be considered as an innovative SME a company must also comply with at least two of the following three requirements: (i) expenses relating to R&D equal or above the 3% of the higher between turnover and cost of the production; (ii) part of the employees shall have to be graduated with a three year research experience or with a university research experience; (iii) ownership of IP rights referring to industrial patent, biotech, new plant-related kind or original software code.

The law, in order to promote the investments in innovative start-ups and SMEs, also provides for specific derogations to some of the provisions of the Italian Civil Code, such as the possibility to cover the losses which affect the corporate capital within two years (instead of one year) and the possibility for limited liability companies to issue specific class of quotas provided with different rights and, only for innovative start-ups, exemption from the application of the bankruptcy laws.

## (2) Crowdfunding platforms

According to the Italian Consolidated Law on Banking (Legislative Decree 24 February 1998 n. 58 - *Testo unico delle disposizioni in materia di intermediazione finanziaria* – the TUF) the Crowdfunding activity has to be performed only by authorized entities (such as banks and investment companies) and by platform managers expressly authorized by CONSOB and enrolled in a special register held by CONSOB itself.

Article 50-*quinquies* of the TUB, in particular, states that:

- A. “the platform manager is the subject who professionally manages platforms for the raising of capital for innovative start-ups, for innovative SMEs, for collective investment bodies and for companies which invest primarily in innovative start-ups and in innovative SMEs registered” in the special register held by CONSOB (Paragraph 1);
- B. “the activity of platforms for the collection of capital for innovative start-ups, for innovative SMEs, for collective investment bodies and for companies which invest primarily in innovative start-ups and in innovative SMEs is reserved to the investment companies and banks authorised to provide the relative investment services and to the subjects registered on a special register held by CONSOB,

providing that these latter transmit the orders regarding the underwriting and trading of financial instruments representing capital exclusively to banks and investment companies” (Paragraph 2).

In order to be registered on the special register held by CONSOB the platform managers must fulfil the following requirements:

- A. be a joint stock company, a limited liability company or a cooperative;
- B. have the registered and administrative office or, for companies based in any EU Member State, have a branch in Italy;
- C. have as company's purpose the management of on-line platform for raising capital for innovative start-ups innovative SMES, for collective investment bodies and for companies which invest primarily in innovative start-ups and in innovative SMEs;
- D. have the controlling shareholders and the directors and auditors fulfilling the integrity and professional requirements established by CONSOB.

Such platforms may not in any case hold sums or financial instruments pertaining to third parties. In this respect, Article 100-ter, Paragraph 2-bis, of the TUF expressly provides that for the subscription or purchase and subsequent sale of quotas representing the innovative start-up and innovative SME capital, constituted in the form of a limited liability company:

- A. the subscription or purchase may be carried out through a bank of financial intermediary, which have to carry out the subscription or purchase of the stocks in their own name or on behalf of the subscribers that subscribe to the bid via the platform;
- B. within 30 days from the close of the bid, authorized intermediaries shall notify the Companies Register of their ownership of stocks on behalf of third parties, incurring the relevant cost thereof; in this regard, the subscription conditions published on the platform must expressly provide that: should the subscription to the bid be successful and should the investor decide to make use of the alternative regime referred to the section above, this shall imply the concurrent and mandatory grant of a mandate to the appointed intermediaries so that they may;
- C. register the stocks/units in their own name or on behalf of the subscribers, providing adequate proof of the latter's identity and the shares owned;
- D. issue a confirmation certificate on behalf of the subscriber, proving ownership of the stocks; said confirmation certificate is needed only to legitimise the corporate rights, refers to the subscriber by name, is not transferable to third parties even on a temporary basis, for any reason, and does not constitute a valid instrument to transfer ownership of the stocks;
- E. allow the subscribers that make application to sell the stocks pursuant to letter c) below;
- F. grant subscribers the right to apply, at any time, for the relevant stocks to be registered directly in their name;

G. the subsequent sale of stocks/units pursuant to point b), number 3) is carried out by simply annotating the transfer in the registers held by the intermediary; the subscription and transfer do not result in costs or fees for the buyer or seller; the subsequent certification issued by the intermediary for the purposes of exercising corporate rights replaces and covers the formalities referred to under article 2470, section two of the Italian Civil Code.

### 3.1.2 Lending Model

The lending Crowdfunding activity has been recently recognised by the Bank of Italy as mentioned in the previous paragraph 2.3.

As reported above, the only requirement is for those online platform willing to open and manage payment accounts, which must apply for the Payment Service Provider or Electronic Money Issuer license or ask to passport the license granted by another European supervisory authority.

The terms to be granted with said licensed are set forth by the Italian Consolidated Law on Banking (Legislative Decree 385/1993 - *Testo unico delle leggi in materia bancaria e creditizia*) and the relevant Regulation issued by the Bank of Italy on 17 May 2016 – *Disposizioni di vigilanza per gli istituti di pagamento e gli istituti di moneta elettronica*.

Please note that under the Italian Consolidated Banking Act, the Bank of Italy has the power to reject the license request not only for the lacking of formal requirements but also if it, as a result of an assessment of the business, may deem that the company applying for the license has not enough technical and/or financial capabilities.

Peer to Business platforms may be required to enrol in the register of the credit mediators (in Italian “*Mediatori Creditizi*”) if lenders admitted to lend through the platform are banks or financial intermediaries authorised to lend money to enterprises or individuals.

Moreover, the platforms shall have to comply also with the Regulations issued by the Bank of Italy on transparency of the contractual relationship between financial intermediaries and clients – Regulation dated 29 July 2009 as amended on 15 July 2015 – *Trasparenza delle operazioni e dei servizi finanziari, correttezza delle relazioni tra intermediari e clienti* (some exceptions are applicable in case the relationship is with a professional client).

### 3.1.3 Donations or Rewards Model

Donation and reward model are not regulated in Italy.

## 3.2 Prospectus requirements

According to the TUF public offers of shares or of stocks of innovative start-ups and innovative SMEs made through an authorized online platform which does not exceed the overall amount of EUR 5,000,000 are not subject to the duty to publish a prospectus.

Article 100-ter of the TUB in particular states that “*public offers conducted exclusively via one or more online platforms dedicated to the raising of capital may have the sole purpose of the underwriting of financial instruments issued by the innovative start-ups, by the innovative SMEs, by the collective investment bodies or other companies which invest primarily in innovative start-ups and in innovative SMEs must have the total amount lower than the one determined by Consob*” (EUR 5,000,000).

Moreover, Article 100-ter of the TUB and CONSOB Regulation 18592/2013 provides also that:

- A. public offers conducted via an online platform must also be underwritten for a percentage of at least 5% by professional investors;
- B. if the majority shareholders of the innovative start-up or innovative SME transfer their own equity to third parties the underwriters shall have the right to withdraw from the company or co-sell their shares or quotas.

Moreover, according to Consob Regulation 18592/2013 the Crowdfunding platforms have only to provide to the public a short investment memorandum reporting information on the offering company (name, registered office, structure, name and role of the directors and auditors, description of the shareholdings), on the characteristics of the offer (type of shares or stocks offered, timing, relevant rights, etc.) as well as on the risks related to the offer.

### **3.3 Regulation of Crowdfunding under the AIFMD regime**

Italian AIFMD discipline does not apply to Crowdfunding due to the fact that Crowdfunding platforms do not raise capital from investors for their own business and on a specific investment policy.

AIMFD is applicable to collective investment undertakings (investment funds) and investment companies (holdings) which invest primarily in innovative start-ups and in innovative SMEs raising capitals through equity Crowdfunding platforms, since in Italy AIMFD has been enforced without exemption with reference to the amount of investments collected by an investment funds or an holding company.

Therefore also small investment funds or holding company shall have to comply with AIFMD.

### **3.4 Possible additional Regulations**

Another regulation that is applicable to Crowdfunding are those referring to Anti Money Laundering (Legislative Decree 321/2007), Data Privacy (Legislative Decree 196/2003), and for consumer credit also the relevant provisions of the Consumer Code (Legislative Decree 206/2005).

Please note that on February 2017, the Government has adopted the draft of the Legislative Decree implementing the IV Directive on Anti Money Laundering (Directive EU n. 849/2015), which is now submitted to the Parliament for the final approval.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable Law

#### 4.1.1 Applicable Law for equity business

Equity business may be subject to the application of the following laws and regulations

- A. Law no. 221 of 17 December 2012;
- B. CONSOB Regulation of 26 June 2013 n. 18592 as further amended by the CONSOB decision n. 19520 dated 25 February 2016;
- C. Decree Law n. 76 dated 28 June 2013, also known as “*Decreto Lavoro*” (duly implemented by the Law n. 99 dated 9 August 2013) and more recently by the Decree Law n. 3 dated 24 January 2015 (known as “Investment Compact” and duly implemented by the Law n. 33 dated 24 March 2015).

#### 4.1.2 Applicable law for lending business

Social lending business may be subject to the application of the following laws and regulations:

- A. Italian Consolidated Law on Banking, Legislative Decree n. 385 of 1 September 1993 – *Testo unico delle leggi in materia bancaria e creditizia* (hereinafter the “**TUB**”); and
- B. Regulation issued by the Bank of Italy on 17 May 2016, *Disposizioni di vigilanza per gli istituti di pagamento e gli istituti di moneta elettronica* (hereinafter the “**Bank of Italy Regulation**”) applicable to both Payment Service Provider and Electronic Money Issuers;
- C. Legislative Decree n. 231 of 21 November 2007, regulating the money laundering proceedings. As mentioned above, the draft of the Legislative Decree implementing the IV Directive on Anti Money Laundering (Directive EU n. 849/2015) has been submitted to the Parliament for the final approval.

### 4.2 Inbound

#### 4.2.1 Foreign equity Crowdfunding platform addresses investors in Italy

In accordance to the applicable Italian laws, foreign equity Crowdfunding platforms cannot directly operate in the Italian market without the prior obtainment of the relevant authorization by CONSOB, unless the platform is granted with a MIFID EU license which will allow the performance of the activity in Italy through the establishment of a local branch, or directly without any establishment of a local branch, or through an agent established in Italy.

The above mentioned authorization can be granted only if the relevant provisions of TUF and of the CONSOB regulation are respected.

The above mentioned rules are also applicable with regard to foreign projects published in foreign Crowdfunding platforms, due to the fact that such platforms are, as reported above, not allowed to address their activity towards Italian investors.

In any case companies that are willing to offer (even through a Crowdfunding platform) have to comply with the prospectus requirements (and/or with the relevant exemptions) as set forth above under paragraph 3.4.

#### **4.2.2 Foreign equity Crowdfunding platform addresses Italian companies/project to intermediate**

Please refer to what set forth above under 4.2.1.

#### **4.2.3 Foreign lending Crowdfunding platform addresses investors in Italy**

According to the TUB a Payment Institution (“PSP”) or an Electronic Money Issuer (“EMI”) authorized in a EU Member State is allowed to provide payment services in Italy:

- A. through the establishment of a local branch, in accordance with the right of freedom of establishment; or
- B. directly without any establishment of a local branch, in accordance with the right of freedom of provide services; or
- C. through an agent established in Italy.

In compliance with TUB, PSP and EMI are also entitled to provide payment services without any need of any further authorization.

Also foreign companies are allowed to publish a request for financing through a lending Crowdfunding platform, in this respect they (as well as the Crowdfunding platform operating in Italy) have to comply with the mandatory provisions of the Italian law regarding lending Crowdfunding (please refer to paragraph 2.3).

#### **4.2.4 Foreign lending Crowdfunding platform addresses Italian companies/project to intermediate**

Please refer to what set forth above under 4.2.3.

### **4.3 Outbound**

#### **4.3.1 Italian equity crowdfunding platform addresses foreign investors**

In accordance to Italian laws, Italian equity Crowdfunding platforms that have obtained the relevant authorization by CONSOB cannot directly perform their activity in other countries. Such activities, in fact, are not subjected to the principle of mutual recognition.

Italian companies are in theory allowed to publish a project in an EU equity Crowdfunding platform, in accordance with the relevant EU country applicable laws and regulations.

#### **4.3.2 Italian equity Crowdfunding platform addresses foreign companies/project to intermediate**

Please refer to what set forth above under 4.3.1.

#### **4.3.3 Italian lending crowdfunding platform addresses foreign investors.**

Pursuant to the applicable laws, a PSP or an EMI which is duly authorized in Italy, is also allowed to provide payment services in any other EU Member State through *(i)* establishment of a local branch, in accordance with the right of freedom of establishment, or *(ii)* directly without any establishment of a local branch, in accordance with the right of freedom of provide services, or *(ii)* through an agent established in such other Member State.

Italian companies are in theory allowed to publish a project in an EU lending Crowdfunding platform, in accordance with the relevant EU country applicable laws and regulations.

Despite nothing is said in the relevant regulation considering the fact that the social lending activity is in Italy allowed only in compliance within the limits set forth by the Bank of Italy (see above paragraph 2.3), even in case of a lending requested through a foreign platform in another EU country such limitation may apply to Italian companies.

#### **4.3.4 Italian lending Crowdfunding platform addresses foreign companies/project to inter-mediate**

Please refer to what set forth above under paragraph 4.3.3.

### **4.4 Impact of EU regulation**

In light of the above, a PSP or an EMI duly authorized in a EU Member State is allowed to provide payment services in Italy through:

#### **4.4.1 Establishment of a branch**

In compliance with the right of freedom of establishment in the EU the TUB states that any authorized EU PSP (or authorized EU EMI) wishing to provide payment services for the first time in Italy is allowed to do so through the establishment of a branch in Italy (Article 114-*decies* of the TUB for EU Payments Institutions - Article 114-*quinquies* of the TUB for EU EMI).

In this case, according to the Bank of Italy Regulation (Chapter VIII, Section I) the possibility to provide payment services in Italy by an EU Payment Institution (or by an EU EMI) through the establishment of a branch is subject to:

- A. the notification by the EU Payment Institution (or by the EU Electronic Money Institution) to the competent Authority of its home Member State in compliance with the relevant legislation of this Member State, of its intention to operate in Italy through a local branch (the competent Authority of the home Member State of the EU Payment Institution, or of the EU Electronic Money Institution, has to

- inform the Bank of Italy of the name and address of the relevant EU Payment Institution – or the relevant EU Electronic Money Institution – the names of those responsible for the management of the branch, its organizational structure and of the kind of payments services it intends to provide in Italy);
- B. the absence of any communication by the Bank of Italy to the competent Authority of the Member State of the EU Payment Institution (or of the EU Electronic Money Institution) with regard to the existence of reasonable grounds to suspect that with the intended establishment of the branch money laundering activities or terrorists financing is taking place or has taken place or that such establishment could increase the risk to commit such activities;
  - C. the communication by the EU Payment Institution (or the EU Electronic Money Institution) to the Bank of Italy of the date of the beginning of the activity of the local branch.

The activity of the local branch can start only after the receipt by the Bank of Italy of the relevant communication from the competent Authority of the Member State of the EU Payment Institution (or of the EU Electronic Money Institution) and in absence of any suspect of money laundering or terrorist financing activities.

#### **4.4.2 Freedom to provide services**

In accordance with the right of freedom to provide services in the EU, an EU Payment Institution (or an EU Electronic Money Institution) shall also provide payment services in Italy directly without establishing a branch (Article 114-*decies* of the TUB for Payments Institutions - Article 114-*quinquies* of the TUB for EMI).

In such a case the Bank of Italy Regulation (Chapter VIII, Section I) states that an EU Payment Institution (or an EU Electronic Money Institution) can provide payment services in Italy directly without any establishment of a branch after the date in which the Bank of Italy has received the relevant notification by the competent Authority of the Member State of the EU Payment Institution (or the EU Electronic Money Institution).

Therefore, also in this case, the EU Payment Institution (or the EU Electronic Money Institution) has to notify the relevant intention to provide services in Italy to the competent Authority of its home Member State in compliance to the relevant applicable legislation.

#### **4.4.3 Activity through agent in providing payment services established in Italy**

According to the TUB, a EU Payment Institution (or the EU Electronic Money Institution) can also provide payment services in Italy through an agent in providing payment services established in Italy (Article 114-*decies* of the TUB for Payments Institutions – Article 114-*quinquies* of the TUB for EMI - Article 128-*quater* of the TUB for EMI).

In compliance with the provisions of the Directive 2007/64/CE on payment services an agent in payment services is any natural or legal person which acts on behalf of an EU Payment Institution (or an EU Electronic Money Institution) in providing payment services.

In this scenario if an EU Payment Institution (or an EU Electronic Money Institution) intends to provide payment services in Italy through an agent the Bank of Italy Regulation (Chapter VIII, Section I):

- A. the EU Payment Institution (or the EU Electronic Money Institution) has to notify to the competent Authority of its home Member State in compliance with the applicable legislation, the relevant intention to operate in Italy through an agent in providing payment services established in Italy;
- B. the Bank of Italy, after having received the relevant communication by the competent home Authority of the EU Payment Institution (or of the EU Electronic Money Institution), have to communicate to such Authority if there are reasonable grounds to suspect that with the intended engagement of said agent money laundering activities or terrorists financing is taking place or has taken place or if such engagement could increase the risk to commit such activities.
- C. the EU Payment Institution (or the EU Electronic Money Institution) has to communicate to the Bank of Italy the date of the beginning of the activity of the relevant agent.

The beginning of the activity of the agent is subject to the receipt by the Bank of Italy of the relevant communication from the competent home Authority of the EU Payment Institution (or of the EU Electronic Money Institution) and the absence of any suspect with regard to the conduction of money laundering activities or financing of terrorism.

Moreover, Article 128-*quater*, Paragraph 7, of the TUB states that an agent in providing payment services established in Italy which acts only on behalf of an EU Payment Institution (or an EU Electronic Money Institution) in providing payment services in Italy is not obliged to obtain any specific authorization to perform this activity and, as a consequence, it has not to be registered in any public register in Italy.

However, in order to avoid any lack of control with regard to possible conduction of money laundering activities or terrorist financing by the agent in the performing of its activity on behalf of the EU Payment Institution (or an EU Electronic Money Institution) article 128-*quater* of the TUB states that the relevant agent:

- A. has in any case to be subject to the provisions of the Legislative Decree 231/2007 on prevention of money laundering;
- B. shall be requested to communicate (by way of certified registered e-mail) to the competent Italian Authority designated to control all the agents in providing financial activities (including agents in providing payment services) the *Organismo degli Agenti e dei Mediatori* (OAM): (i) the date of the beginning of its activity in Italy; (ii) all its information and data and any relevant change; (iii) the termination of the activity.

In compliance with the right of establishment and freedom to provide services an agent established in an EU Member State (eventually already authorized in said Member State to

act as agent in financial activities of agent in providing payment services) can provide its activities also in Italy without any need of further registration by way of establishing a branch.

#### **4.4.4 Supervision over the EU Payment Institution or the EU Electronic Money Institution**

In accordance with the principle of the home country control the Authority that is competent to exercise the prudential supervision over the EU Payment Institution (or the EU Electronic Money Institution) providing services in Italy is the Authority of the home Member State of such EU Payment Institution (or of the EU Electronic Money Institution).

In this respect, the competent Authority of the home Member State of the of the EU Payment Institution (or of the EU Electronic Money Institution) shall cooperate with the Bank of Italy, to whom can also delegate (in case of establishment of a branch or activity through an agent established in Italy) to carry out on-site inspections of the institution concerned.

According to the TUB and the Bank of Italy Regulation (Chapter VIII, Section I) the Bank of Italy can proceed to carry out all the supervisory activities that are not carried out by the competent home Member State Authority (such as transparency and correctness with clients rights and duties of the parties of the payment service, protection against money laundering and terrorist financing) with regard to the local branch and agent of the EU Payment Institution (or of the EU Electronic Money Institution).

#### **4.4.5 PSD/PSD II**

The Payment Services Directive was implemented by the Legislative Decree n. 11 dated 27 January 2010. The Payment Services Directive II (entered into force in 2016) must be implemented until January 2018. Payment services in Europe are generally harmonized, but regarding the details there is still room for interpretation of the national legislators and (especially) financial regulation authorities which does not lead to a fully harmonized single market in Europe.

Regarding Crowdfunding especially the money remittance services come into consideration:

Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services within the meaning of the above mentioned Legislative Decree n. 11/2010 implementing the PSD Directive. Such transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform which then passes the funds to the company / project.

Due to the above, any operator of a Crowdfunding platform may cooperate, as financial agent or outsourcer, with a bank or a licenced payment institution (PSP/EMI) for the handling of payments rather than acting as an intermediary itself. However, the structure of this cooperation must meet detailed requirements by the Bank of Italy or, in case of foreign PSP/EMI by their Supervisory Authority (Home Country Control Principle).

Therefore these two directives have a great impact for Crowdfunding regarding the transaction of the investments.

On September 2016 the Italian Parliament has adopted the so called “EU delegation law” delegating the Italian government, among other, to implement into the Italian market the PSDII Directive. The government has not yet approved the relevant legislative decree that - in theory - has to be approved within September 2017.

#### **4.5 Summary**

In consideration of the above, foreign equity Crowdfunding platforms cannot directly operate in the Italian market without the prior obtainment of the relevant authorization by CONSOB, unless the platform is granted with a MIFID EU license which will allow the performance of the activity in Italy through the establishment of a local branch, or directly without any establishment of a local branch, or through an agent established in Italy; accordingly Italian equity Crowdfunding platforms that have obtained the relevant authorization by CONSOB cannot directly perform their activity in other countries.

As far as the social lending activity is concerned, a PSP or an EMI duly authorized in a EU Member State is allowed to provide payment services in Italy through the establishment of a local branch, or directly without any establishment of a local branch, or through an agent established in Italy. Under the same conditions a PSP or an EMI duly authorized in Italy is also allowed to provide payment services in any other EU Member State.

### **5 Lessons learned from Italy's regulation for a possible harmonized European Crowdfunding regulation**

#### **5.1 Role model ("dos")**

The creation of a category of new regulated entities (professional equity Crowdfunding portal managers) has allowed the explosion of the relevant Italian market; the CONSOB regime proved to be affordable for new comers and it is not a relevant barrier to enter the market.

The possibility for the issuers to create different categories of financial instruments to be offered to the investors is also very useful instrument in order to define the structure of each single share capital offer.

#### **5.2 Aspects that should be avoided ("don'ts")**

Even though Law n. 33/2015 has amended the provisions dealing with equity Crowdfunding transactions by allowing also Innovative SMEs and investment funds to raise funds by means of online Crowdfunding platforms, the possibility of raising money online is however restricted only to innovative entities.

The rules applicable to the sale of units representing the share capital of limited liability Italian companies may impact the possibility to create a secondary market for this kind of

financial instruments due to the strict requirement applicable to execute the relevant transfer of units between shareholders.

## 6 Conclusion

The Crowdfunding Lending Model, either in the peer to peer or in the peer to business form, is not yet subject to a specific “light” regulation (and platforms must carefully review which authorisation must be sought pursuant to the Italian Consolidated Banking Law and/or the Consolidated Financial Law to operate in Italy) which could support a significant growth of the relevant markets.

The equity based Crowdfunding model is subject to its own specific regulatory regime, which is fully applicable and in force as of June 2013; the entering into force of this regulation has allowed significant development of the relevant market.

The reward Crowdfunding market is increasing (either looking at the number of platforms and projects) while different Crowdfunding models (profit sharing and real estate) are currently under assessment and development.

## 7 Summary – Crowdfunding regulation

| Country   | Italy   |
|---|---|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Law 33/2015: allowing also Innovative SMEs and investment funds to raise funds by means of online Crowdfunding platforms.</li> <li>• CONSOB decision n. 19520 dated 25 February 2016: verification of the suitability of the investment (MIFID assessment), increase of the number of those authorized to subscribe as professional investors and loss of license if the platform does not start to operate within 6 months from the granting of the license.</li> <li>• Bank of Italy (resolution 584/2016): recognition of social lending activity (P2P and P2B).</li> </ul> |
| <b>Current / planned Crowdfunding regulation</b>                            |   |
| <b>General regulation</b>   | <ul style="list-style-type: none"> <li>• Equity Crowdfunding is limited only to: (a) innovative start-ups; (b) innovative SMEs; (c) collective investment undertakings and investment companies which invest primarily in innovative start-ups and in innovative SMEs (Law 221/2012 and Law 33/2015).</li> <li>• Crowdfunding activity has to be performed only by authorized entities (such as banks and investment companies) and by platform managers expressly authorized by CONSOB.</li> </ul>   |
| <b>Prospectus requirement</b>   | <p>Exception from prospectus requirements for public offers of shares or of stocks of innovative start-ups and innovative SMEs made through an authorized equity Crowdfunding platform which does not exceed the overall amount of EUR 5,000,000.</p>   |
| <b>AIFMD-regulation</b>   | <p>Italian AIFMD discipline does not apply to Crowdfunding.</p>   |
| <b>Further possible requirements</b>  | <ul style="list-style-type: none"> <li>• Italian Money Laundering law;</li> <li>• Italian Data Privacy law;</li> <li>• Consumer Code.</li> </ul>  |
| <b>Regulatory barriers</b>  |   |
| <b>Inbound</b>  | <p><b>Foreign equity Crowdfunding platform addresses investors in Italy</b></p> <ul style="list-style-type: none"> <li>• In accordance to the applicable Italian laws, foreign equity Crowdfunding platforms cannot directly operate in the Italian market without the prior obtainment of the relevant authorization by CONSOB, unless the platform is granted with a MIFID EU license which will allow the performance of the activity in Italy through the establishment of a local branch, or directly without any establishment of a local branch, or through an agent established in Italy.</li> </ul>            |

|                        |  |
|------------------------|--|
|                        | <ul style="list-style-type: none"> <li>• (Such authorization can be granted only if the relevant provisions of TUF and of the CONSOB regulation are respected.)</li> <li>• The above mentioned rules are also applicable with regard to foreign projects published in foreign Crowdfunding platforms, due to the fact that such platforms are, as reported above, not allowed to address their activity towards Italian investors.</li> <li>• In any case companies that are willing to offer (even through a Crowdfunding platform) have to comply with the relevant prospectus requirements (and/or with the relevant exemptions).</li> <li>• The same considerations can be made in relation to foreign equity Crowdfunding platform addresses Italian companies/project to intermediate.</li> </ul> <p><b>Foreign lending Crowdfunding platform addresses investors in Italy</b></p> <ul style="list-style-type: none"> <li>• According to the TUB a Payment Institution (“PSP”) or an Electronic Money Issuer (“EMI”) authorized in a EU Member State is allowed to provide payment services in Italy:             <ul style="list-style-type: none"> <li>a) through the establishment of a local branch, in accordance with the right of freedom of establishment; or</li> <li>b) directly without any establishment of a local branch, in accordance with the right of freedom of provide services; or</li> <li>c) through an agent established in Italy.</li> </ul> </li> <li>• In compliance with TUB, PSP and EMI are also entitled to provide payment services without any need of any further authorization.</li> <li>• Also foreign companies are allowed to publish a request for financing through a lending Crowdfunding platform, in this respect they (as well as the Crowdfunding platform operating in Italy) have to comply with the mandatory provisions of the Italian law regarding lending Crowdfunding and with regard to lending granted by consumers.</li> <li>• The same considerations can be made in relation to foreign lending Crowdfunding platform addresses Italian companies/project to intermediate</li> </ul> |
| <p><b>Outbound</b></p> | <p><b>Italian equity crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>• In accordance to Italian laws, Italian equity Crowdfunding platforms that have obtained the relevant authorization by CONSOB cannot directly perform their activity in other countries. Such activities, in fact, are not subjected to the principle of mutual recognition.</li> <li>• Italian companies are in theory allowed to publish a project in an EU equity Crowdfunding platform, in accordance with the relevant EU country applicable laws and regulations.</li> <li>• The same considerations can be made in relation to Italian equity Crowdfunding platform addresses foreign companies/project to intermediate.</li> </ul>  |

|   |  |
|---|--|
|   | <p><b>Italian lending crowdfunding platform addresses foreign investors.</b></p> <ul style="list-style-type: none"> <li>• Pursuant to the applicable laws, a PSP or an EMI which is duly authorized in Italy, is also allowed to provide payment services in any other EU Member State through (i) establishment of a local branch, in accordance with the right of freedom of establishment, or (ii) directly without any establishment of a local branch, in accordance with the right of freedom of provide services, or (ii) through an agent established in such other Member State.</li> <li>• Italian companies are in theory allowed to publish a project in an EU lending Crowdfunding platform, in accordance with the relevant EU country applicable laws and regulations.</li> <li>• Despite nothing is said in the relevant regulation considering the fact that the social lending activity is in Italy allowed only in compliance within the limits set forth by the Bank of Italy, even in case of a lending requested through a foreign platform in another EU country such limitation may apply to Italian companies.</li> <li>• The same considerations can be made in relation to Italian lending Crowdfunding platform addresses foreign companies/project to inter-mediate.</li> </ul> |
| <p><b>Impact of EU regulation</b></p>     |  |
| <p><b>Prospectus regulations</b></p>      | <p>According to the Italian Consolidated Law on Finance (TUF) public offers of shares or of stocks of innovative start-ups and innovative SMEs made through an authorized online equity platform which does not exceed the overall amount of EUR 5,000,000 are not subject to the duty to publish a prospectus.</p>  |
| <p><b>Freedom to provide services</b></p> | <ul style="list-style-type: none"> <li>• According to the Consolidated law on Banking (TUB) a Payment Institution (“PSP”) or an Electronic Money Issuer (“EMI”) authorized in a EU Member State is allowed to provide payment services in Italy: (a) through the establishment of a local branch, in accordance with the right of freedom of establishment; or (b) directly without any establishment of a local branch, in accordance with the right of freedom of provide services; or (c) through an agent established in Italy.</li> <li>• In compliance with TUB, PSP and EMI are also entitled to provide payment services without any need of any further authorization.</li> </ul>   |
| <p><b>PSD/PSD II</b></p>                  | <ul style="list-style-type: none"> <li>• Any transfer of funds through the operator of a Crowdfunding platform generally constitutes money remittance services within the meaning of the Legislative Decree n. 11/2010, the Italian implementation of PSD / PSD II in Italian law;</li> <li>• Great impact for Crowdfunding regarding the transaction of the investments.</li> </ul>   |

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# Latvia

## 1 Recent developments in the market of Crowdfunding in Latvia

Latvia was identified as the top seventh country globally in alternative finance volume per capita in the 2016 study by KPMG and University of Cambridge.<sup>1</sup> Yet Crowdfunding is still a fairly new alternative financing vehicle in Latvia with few examples from practice.

### 1.1 The Equity Model

Currently there are no known Crowdfunding platforms based on Equity Model in Latvia.

### 1.2 The Lending Model

To date, the most considerable sector within the Latvian Crowdfunding market is composed by peer-to-peer lending platforms (although not in a classical sense). There are four known such platforms: *Mintos*, *Twino*, *Viventor* and *Viainvest*. All of these are claim right assignment platforms, meaning that investors can acquire claim rights from loan originators deriving from already concluded credit agreements. The loan originators can be the platforms themselves, as well as third party non-bank lenders, including consumer lenders. *Mintos*, the first platform of its kind in Latvia, began operating in January 2015. The state authorities, namely, the Consumer Rights Protection Centre of Latvia (*Patērētāju tiesību aizsardzības centrs* - 'CRPC') took a conservative stance towards the peer-to-peer loan concept, requesting the platform to cease issuing loans to consumers and publicly declaring that due to lack of regulation the investors who invest in loans offered on the platform would not be protected by any of the financial schemes of protection existing in Latvia. The Financial and Capital Market Commission (*Finanšu un kapitāla tirgus komisija* - 'FCMC') - the financial services regulator of Latvia - also endorsed this position. Since then FCMC has developed a more liberal approach towards peer-to-peer lending platforms, on a condition that they were not falling under any of the regulated types of activity and were informing their customers that these platforms were not supervised by the financial services authority and that the customers did not enjoy protection under any of the schemes available to customers of regulated financial market participants. However, most recent development is that FCMC has been considering whether these platforms should obtain investment firm licenses under the Financial Instrument Market Law (implementing MIFID I).

In the end of 2016 the first Lending Model Crowdfunding project, which is not a peer-to-peer platform, was kicked-off in Latvia – *Bulkestate*. It invests in real estate (see Section 1.4. below).

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<sup>1</sup> Published in October 2016, available at: <https://home.kpmg.com/content/dam/kpmg/uk/pdf/2016/10/global-alternative-finance-report-web.pdf>, accessed on 13.04.2017.

### 1.3 The Donations or Rewards Model

Recently two new reward model Crowdfunding platforms commenced their operation in Latvia, of which one is solely devoted to financing creative or scientific projects, whilst the other has got broader spectrum and expressly provides for a consideration to be offered by the authors of the project to donators, without specifying the type of such consideration. Also, Crowdfunding for separate one-time projects has become increasingly popular.

### 1.4 Real Estate Crowdfunding and Renewables Crowdfunding

On December 2016 the first Real Estate Crowdfunding platform in Latvia – *Bulkestate* – began operating. *Bulkestate* has been created for those willing to invest into real-estate either by providing loans to real-estate companies (collective investment – lending based Crowdfunding) or through collective purchase of real estate. *Bulkestate* claims to have already successfully funded two real estate objects – apartment buildings. However, most recent development is that FCMC has been considering whether such platforms should obtain licenses under the AIFMD regime.

Currently in Latvia there are no known Crowdfunding platforms investing in renewable energy.

### 1.5 International approach in Latvia

Some Crowdfunding platforms from other countries have invested in real estate in Latvia, for instance the Estonian *EstateGuru* and *Crowdestate*. Investing via these platforms is available to investors from Latvia, as well.

## 2 Recent developments regarding Crowdfunding regulation in Latvia

Crowdfunding-specific regulation has not yet been introduced in Latvia, although the government publicly confirmed the plan of establishing such regulation a couple of years ago. Since 2015 Latvian Ministry of Finance has been engaged in drafting a law on Crowdfunding and peer-to-peer lending. It is envisaged that the law will set forth certain criteria as regards the statutory capital, members of the management board of the platforms, information provided to investors, etc. In addition, the law will put the said platforms under the supervision of FCMC which will issue licenses accordingly. Possibly the law might be adopted till the end of the year 2017.

To sum up, a reform of the Crowdfunding regulation is being awaited, which might open new horizons for the development of the Crowdfunding market.

## 3 Current regulation of Crowdfunding in Latvia

Currently Crowdfunding as such is not a specifically regulated activity, yet, it might fall under one of the regulations applicable to financial and capital market participants in general.

### 3.1 Licence under the Financial Instrument Market Law (in Latvian – *Finanšu instrumentu tirgus likums*)

#### 3.1.1 Equity Model

Pursuant to the Financial Instrument Market Law (“FIML”), anyone intending to provide investment services in Latvia commercially or on a scale which requires a commercially organised business undertaking requires a licence from the FCMC. Also a licence issued in another EU member state passported to Latvia satisfies this requirement, as long as this licence covers the type of investment services the person provides in Latvia is covered by the licence.

Investment firms must have a certain initial capital, and also, depending of the relevant activity – have risk-management plans, ensure the disclosure of information and fulfil other requirements.

Investment services are, inter alia, the brokering of business involving the purchase and sale of financial instruments or their documentation (investment brokerage), the purchase and sale of financial instruments in the name of and for the account of others (contract brokerage) and the placement of financial instruments without commitment to underwrite those instruments (placement of financial instruments).

Under the FIML a “financial instrument” means an agreement, which concurrently creates financial assets for one person, but financial liabilities or capital securities for another. Transferable securities (in Latvian – *pārvedami vērtspapīri*) are covered by this definition of a financial instrument.

Transferable securities are, inter alia, (a) shares in joint stock companies and other securities equivalent to shares in companies (shares in private limited liability companies would not count as transferrable) including convertible securities; (b) bonds or other forms of securitised debt; or (c) any other securities giving the right to acquire or sell any such transferable securities or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures.

In summary, where an online Crowdfunding platform facilitates the offering of financial instruments, most likely, the operator of the platform will be deemed to provide investment services within the meaning of the FIML and therefore will require a licence by the FCMC. Where the securities in issue do not qualify as financial instruments to which FIML applies, this may well fall outside the scope of investment services regulation (although guidance from the FCMC would be advised since there are few, if any, precedents of such activity resembling investment services but dealing in non-financial instruments).

### 3.1.2 Lending Model

Depending on the structure in detail loans are considered as “debt” (in contrast to equity) and would not qualify as investment services under the FIML.

Nonetheless, according to most recent developments FCMC has been considering treating the services offered by existing marketplace lending platforms operating in Latvia described in Section 1.2 as investment services falling under FIML. The investment services provided by the platform operators in the opinion of FCMC could be, for example, execution of orders on behalf of clients, dealing on own account, as well as operation of multilateral trading facilities (depending on the exact model chosen). In that case the requirements described in Section 3.1.1. above may also apply (including the necessity to obtain an investment firm license under FIML).

To our knowledge, currently no Crowdfunding platform operating on the Latvian market holds an investment services license.

### 3.1.3 Donations or Rewards Model

Depending on the structure in detail there are good reasons to state that donations or rewards model Crowdfunding does not qualify as investment service and thus should fall outside the scope of Latvian investment services regulation.

## 3.2 Prospectus requirements

### 3.2.1 General rule

Where transferable securities are offered to public and the offer is expressed to more than 150 individuals in each EU Member State, it might be subject to a prospectus requirement, namely a requirement to publish a prospectus approved by the FCMC under the FIML. Again, if the securities in question do not qualify as transferable (negotiable) securities, then the prospectus requirement might not be triggered.

Depending on the structure, loans do not generally qualify as financial instruments under the FIML and therefore no prospectus is required. The same should apply to investments where individuals provide money to a company or project for benevolent reasons or for a non-monetary reward (Donations or Rewards Model).

### 3.2.2 Exceptions from prospectus requirement

The general prospectus requirement does not apply where (a) the offering of transferable securities does not exceed EUR 100,000 within a time period of 12 months, (b) only qualified investors are addressed, or less than 150 non-qualified investors per member state are addressed, (c) the offering is made in respect of transferable securities with the nominal value at least EUR 100,000, or (d) in offering each investor must acquire transferable securities with the nominal value at least EUR 100,000 and acquiring of one transferable security so that it belongs to several persons is prohibited.

A prospectus must include the information required by the Prospectus Regulation ((EC) No 809/2004), such as information on the securities offered, information of the offeror, and other information that would allow the investor to evaluate the offeror as well as the investment in general.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

According to the “Law on Alternative Investment Funds and its’ Managers” (in Latvian - *Alternatīvo ieguldījumu fondu un to pārvaldnieku likums*) (“AIFM Law”) the extensive AIFMD regulation of funds and fund managers applies when there is an alternative investment fund (“AIF”) managed by an alternative investment fund manager (“AIFM”). The FCMC has not provided any guidelines on whether a Crowdfunding platform would qualify as an AIFM.

On most occasions a company seeking financing by means of Crowdfunding should not qualify as an AIF. At the same time, a project company established to finance a single project (for example, a movie, a computer game, a wind farm or a solar park) that does not operate the facility or production itself might constitute an AIF within the meaning of the Latvian AIFMD regulation. The aforementioned applies if the project company seeks funding in return for a share in the profits or revenue generated by the project (within the Equity Model) provided that the funding is envisaged for its own project and does not distribute the funding to other companies/entities to finance their projects.

As a general rule the operator of a Crowdfunding platform does not raise capital from investors for its own business. Therefore, the operator of a Crowdfunding platform should not qualify as an AIFM. However, it might depend on the scope of services provided by a Crowdfunding platform. A Crowdfunding platform might qualify as an AIFM if it performs investment management or other functions that under the law can be performed only by licenced or registered AIFMs. For instance, under the AIFM Law one of ancillary services of an AIFM is distribution of units or shares of an AIF. This could apply if the underlying investment (e.g. a project company) qualifies as an AIF and the relevant Crowdfunding platform in fact distributes the shares of that AIF. Each situation should be evaluated separately to establish whether a Crowdfunding platform qualifies as an AIFM.

As outlined above, FCMC has recently been considering treating platforms operating under the Real Estate Crowdfunding model as operating under the AIFMD regime.

### 3.4 Licence under the Payment Services regulation

A transfer of funds through the operator of a Crowdfunding platform might constitute money remittance services within the meaning of the Payment Services and E-Money Law (in Latvian - *Maksājumu pakalpojumu un elektroniskās naudas likums*). Such transfer of funds could occur if the investors pay their investment amounts to the operator of a Crowdfunding platform which then passes the funds to the entrepreneur. The mentioned activity requires either a licence from, or registration with, the FCMC.

In order to avoid such licensing or registration, as the case may be, requirements - the operator of a Crowdfunding platform might use an external provider or partner for processing payments and keeping money rather than acting as an intermediary himself: a payment institution, credit institution or electronic money institution. This is the approach used by the platforms operating in Latvia and to date the FCMC has taken the view that such a setup does not require the platform to obtain a payment services or e-money license itself.

As an alternative, a platform operator might rely on the exemption for commercial agents under the Payment Services and E-Money Law, but this approach is untested in practice.

Thus, in each situation where any of the above exemptions is considered, before starting the respective project, advice from legal counsel shall be sought on the structure of each platform.

### 3.5 Licence under the Credit Institutions Law

Under the Credit Institutions Law (in Latvian – *Kredītiestāžu likums*) only credit institutions are permitted to advertise (in Latvian – *izsludināt*, which in English means to advertise, to announce, to proclaim) the acceptance of deposits and other repayable funds, and to receive them. Besides, most likely an entity managing a Crowdfunding platform, which is not a credit institution, cannot hold sums of money due to third parties because such sums might be qualified as deposits, unless the money is kept in an account opened with a credit institution and the said account is not opened on the name of the platform operator.

### 3.6 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include, but is not necessarily limited to, the following laws and regulations.

#### 3.6.1 Consumer Rights Protection Law (in Latvian – *Patērētāju tiesību aizsardzības likums*)

If a Lending Model Crowdfunding platform wishes to directly issue loans to Latvian consumers, then it would be required to obtain a consumer credit license with the CRPC. Also, if a third-party loan originator is granting loans to Latvian consumers, such originator must hold a consumer credit license.

If the Crowdfunding platform is issuing loans to Latvian consumers as a consumer lender itself and has obtained a consumer credit license, then it has to obtain the evidence that the receiver of the loan has sufficient funds to repay the loan.. However, according to the CRPC making loans granted to Latvian consumers available for investment through peer-to-peer lending platforms (by assigning them to investors) is a violation of the law. Therefore, several licensed Latvian consumer credit providers have been requested to cease this activity. Some of them have complied with the request, while the others have disputed the position of the CRPC with the court with the cases currently pending before the court. This only affects peer-to-peer lending platforms assigning claims that have originated from consumer credit providers licensed in Latvia

If the activity of the lending-based Crowdfunding platform falls under the regulation applicable to credit intermediaries, it should obtain a credit intermediary license with the CRPC.

Crowdfunding platforms are also subject to other consumer rights protection rules, such as rules on fair contract terms, on distance contracting etc.

### **3.6.2 Law on the Prevention of Laundering the Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing (in Latvian - *Noziedzīgi iegūtu līdzekļu legalizācijas un terorisma finansēšanas novēršanas likums*);**

If the Crowdfunding platform qualifies as an investment or other type of financial service provider, or a consumer creditor provider pursuant to rules described before, it is also subject to anti-money laundering rules. However, the law does not provide a clear answer whether a Crowdfunding platform which does not fall under any of licensing regimes can be regarded an obliged entity under Latvian anti-money laundering legislation.

### **3.6.3 The Cabinet of Ministers regulations and/or FCMC regulations in relation to any of the licensed activities (where applicable).**

If the Crowdfunding platform qualifies as an investment or other type of financial service provider, or a consumer creditor provider pursuant to rules described before, it is also subject to the regulations by the Cabinet of Ministers and/or FCMC.

### **3.6.4 Further possible regulation**

Finally, as any commercial entities, Crowdfunding platforms are subject to laws related to non-misleading and fair advertising, fair commercial practices, data privacy and protection, namely, but not exclusively:

- Law on Advertising (in Latvian – *Reklāmas likums*);
- Unfair Commercial Practices Prohibition Law (in Latvian – *Negodīgas komercprakses aizlieguma likums*);
- Natural Persons' Data Protection Law (in Latvian – *Fizisko personu datu aizsardzības likums*);
- Commercial Law (in Latvian – *Komerclikums*);
- Civil Law (in Latvian – *Civillikums*);
- Law on Corporate Income Tax (in Latvian – *Likums "Par uzņēmumu ienākuma nodokli"*).

## **4 Regulatory barriers for Crowdfunding crossing borders**

### **4.1 Applicable law**

The following Latvian financial regulation laws might apply:

- A. Depending on the registration (seat) - if the Crowdfunding platform wishes to establish itself in Latvia -
- licence requirements under FIML / Payment Services and E-Money Law / AIFM Law / Consumer Rights Protection Law/ Credit Institution Law (where the Crowdfunding platform falls within the scope of the respective licence);
  - notification requirements under FIML / Payments institutions law / AIFM Law / Credit Institution Law (where the Crowdfunding platform falling within the scope of the respective licence intends to provide its services also in other EU member states);
  - the Cabinet of Ministers regulations and/or FCMC regulations;
  - AML rules - Law on the Prevention of Laundering the Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing;
- B. Depending on the marketing – if the Crowdfunding platform approaches investors in Latvia:
- Requirements to notify FCMC on the provision of financial services without creating an establishment in Latvia under FIML / Payments institutions law / AIFM Law (where the Crowdfunding platform falls within the scope of the respective law);
  - Prospectus requirements under FIML;
  - Consumer crediting rules under the Consumer Rights Protection Law;
  - Rules on consumer protection, advertising and other rules.

## 4.2 Inbound

### 4.2.1 Crowdfunding platform from another EU country addresses investors in Latvia

If a Crowdfunding platform from another EU country addresses investors in Latvia, the following Latvian regulatory requirements may apply.

#### 4.2.1.1 Crowdfunding platforms

To the Crowdfunding platforms the requirement to obtain the relevant licence or to notify the FCMC on an existing licence in another EU member state, as well as all the other requirements identified above in Section 4.1. might apply, depending on whether the Crowdfunding platform falls within the scope of the respective law. It should be stressed that the application of the obligation to notify on an existing licence is uncertain, as the necessity for a licence in Latvia for Crowdfunding is highly fact-specific.

We can also highlight the following barriers which may create significant legal obstacles for Crowdfunding in Latvia:

- Latvian law does not recognize the concept of “security trustee” allowing an agent to hold and enforce security on behalf of multiple lenders;

- The assignment of claims through peer-to-peer lending platforms is not fully clear from the taxation perspective.

#### **4.2.1.2 Foreign companies or projects**

To foreign companies or projects prospectus regulation and AIFMD regulation might apply, depending on the circumstances, as described above in Sections 3.2.2. and 3.3. respectively.

#### **4.2.2 Crowdfunding platform from another EU country addresses companies or projects in Latvia**

No specific regulatory barriers are associated with this situation.

### **4.3 Outbound**

#### **4.3.1 Crowdfunding platform from Latvia addresses investors in another EU country**

If a Crowdfunding platform from Latvia addresses investors in another EU country, the following Latvian regulatory requirements may apply.

##### **4.3.1.1 Crowdfunding platforms**

To the Crowdfunding platforms the requirement to obtain the relevant licence from the FCMC, as well as other requirements identified above in Section 4.1.(a) and (b) might apply (apart, of course, from the requirement to notify on the provision of services in Latvia). The requirements apply to the same extent as if the platforms were to address investors in Latvia, apart from the rules on consumer protection, which are determined by the laws of the home state of the consumers. Thus, consumer crediting rules of Latvia would not apply.

##### **4.3.1.2 Foreign and domestic companies and projects**

To foreign as well as domestic companies or projects prospectus regulation and AIFMD regulation might apply, as described above in Sections 3.2.2. and 3.3. respectively.

#### **4.3.2 Crowdfunding platform from Latvia addresses companies or projects in another EU country**

No specific regulatory barriers are associated with this situation.

### **4.4 Impact of EU regulation**

Latvian FIML generally mirrors the prospectus rules provided in the Prospectus Regulation ((EC) No 809/2004).

AIFMD Directive has been implemented in Latvia since August 2013. So far, no known Crowdfunding platforms have been subject to the Latvian rules implementing the directive.

MIFID II Directive is planned to be implemented in Latvia by the extended deadline, via amendments in the FIML, which currently implements the MIFID I. Thus, there has not yet been an impact to Crowdfunding platforms by the directive. planned to be transposed.

PSD II Directive is planned to be implemented in Latvia by the deadline, that is, January 2018. Thus, there has not yet been an impact to Crowdfunding platforms by the directive. PSD II is planned to be transposed via amendments in the Payment Services and E-Money Law, which currently implements the PSD I regime.

#### 4.5 Summary

Most significant regulatory obstacles in Latvia in practice currently are posed by the strict stance of the supervisory authorities, mostly the CRPC towards the peer-to-peer lending platforms and the lack of specific regulation governing Crowdfunding platforms. In the future, the most important regulatory restraints might be posed by the new regulation on Crowdfunding.

### 5 Lessons learned from Latvia

#### 5.1 Role model ("dos")

Since the Crowdfunding regulation is yet to be adopted, it is unclear whether it will provide a good example for European Union regulation.

#### 5.2 Aspects that should be avoided ("don'ts")

The hostile position of Latvian authorities at the onset of development of peer-to-peer lending platform market, is not an example to be followed. However, since then FCMC has developed a much more nuanced and liberal approach.

### 6 Conclusion

- Latvian assignment-based marketplace (peer-to-peer) lending platforms have established themselves on the peer-to-peer lending market in Europe. Apart from them, Crowdfunding is in the early stages of development in Latvia.
- There is currently no regulatory regime that is specifically adapted to Crowdfunding in Latvia.
- Nonetheless, regulation of Crowdfunding will be submitted to the Latvian Parliament in late autumn 2017.
- In principle, Latvian law allows for the implementation of Crowdfunding projects.
- Yet the application of the existing financial services regulation is uncertain and highly case-specific, which hinders the cross-border activities of Crowdfunding platforms.
- Also, up to date regulatory authorities have taken a restrictive stance regarding peer-to-peer lending.

- In each situation taking legal advice before any Crowdfunding project is started is highly recommended.

## 7 Summary – Crowdfunding Regulation

|   |  |
|---|--|
| <b>Country</b>  | <h1>Latvia</h1>  |
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | Draft legislative amendments aimed at regulating Crowdfunding might be submitted to the Latvian Parliament in 2017.  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• No regulatory regime specifically adapted to Crowdfunding. In principle, Latvian law allows for the implementation of Crowdfunding projects. In each situation it is recommended to involve local counsel.</li> <li>• If Crowdfunding platform facilitates offering of securities or other financial instruments or holds money belonging to third persons, operator of the platform most likely provides investment or financial services <ul style="list-style-type: none"> <li>→ FCMC authorisation required</li> </ul> </li> <li>• Where securities do not qualify as financial instruments, this may fall outside the scope of investment services regulation, although guidance from FCMC would be advised.</li> <li>• Depending on the structure in detail: there are sound arguments that contributions under Donations/Rewards Model do not constitute provision of investment or financial services</li> <li>• According to the position of FCMC, assignment-base peer-to-peer lending Crowdfunding falls under the provisions of investment services</li> <li>• Most likely an entity managing a Crowdfunding platform which is not a credit institution cannot hold sums of money belonging to third parties <ul style="list-style-type: none"> <li>→ sums might be qualified as deposits</li> <li>→ Credit Institutions Law only permits credit institutions to advertise receipt of deposits and other repayable funds, and to receive them.</li> </ul> </li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for a public offer regarding transferable securities (i.e., offer is expressed to more than 150 individuals in one EU Member State)</li> <li>• Exemptions of Prospectus requirements (a) offering of transferable securities does not exceed EUR 100,000 within a time period of 12 months, (b) only qualified investors are addressed, or less than 150 non-qualified investors per member state are addressed, (c) the offering is made in respect of transferable securities with the nominal</li> </ul>  |

|                                      |  |
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|                                      | <p>value at least EUR 100,000, or (d) each investor must acquire transferable securities with the nominal value at least EUR 100,000 and acquiring of one transferable security so that it belongs to several persons is prohibited.</p> <ul style="list-style-type: none"> <li>Depending on the structure in detail: there are no prospectus requirements for loans or contributions under Donations/Rewards Model</li> </ul>   |
| <b>AIFMD-regulation</b>              | <ul style="list-style-type: none"> <li>Typical start-up company in general does not constitute an AIF</li> <li>A project company might constitute AIF <ul style="list-style-type: none"> <li>→ extensive AIFMD regulation for AIF and its manager</li> <li>→ manager (AIFM) requires FCMC authorisation</li> </ul> </li> <li>Depending on the structure in detail: funding by means of or contributions under Donations/Rewards Model should not entail an AIF</li> <li>Depending on the scope of the services provided by the Crowdfunding platform, Crowdfunding platforms might qualify as AIFM.</li> </ul>   |
| <b>Payment service regulation</b>    | <ul style="list-style-type: none"> <li>Transfer of funds through operator may constitute money remittance service <ul style="list-style-type: none"> <li>→ FCMC licensing or registration with the FCMC required.</li> </ul> </li> <li>"Commercial Agents" exemption probably not applicable to operators of Crowdfunding platforms</li> <li>Other exemption might be that the operator of a Crowdfunding platform uses an external provider or partner for processing payments rather than acting as an intermediary himself</li> </ul>   |
| <b>Consumer credit regulation</b>    | <p>If consumer borrowers are permitted on a platform (Lending Model) there are implications for licence for consumer crediting, form and content of the lending agreements.</p>  |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>Civil Law (in Latvian – <i>Civillikums</i>)</li> <li>Commercial Law (in Latvian – <i>Komerclikums</i>)</li> <li>Law on the Prevention of Laundering the Proceeds from Criminal Activity (Money Laundering) and of Terrorist Financing (in Latvian – <i>Noziedzīgi iegūtu līdzekļu legalizācijas un terorisma finansēšanas novēršanas likums</i>)</li> <li>Natural Persons' Data Protection Law (in Latvian – <i>Fizisko personu datu aizsardzības likums</i>)</li> <li>The Cabinet of Ministers regulations and FCMC regulations in relation to investment services and payment institutions</li> <li>Consumer Rights Protection Law (in Latvian – <i>Patērētāju tiesību aizsardzības likums</i>)</li> <li>Unfair Commercial Practices Prohibition Law (in Latvian – <i>Negodīgas komercprakses aizlieguma likums</i>)</li> </ul> |

|                            |   |
|----------------------------|---|
|                            | <ul style="list-style-type: none"> <li>• Law on Advertising (in Latvian – <i>Reklāmas likums</i>)</li> <li>• Law on Corporate Income Tax (in Latvian – <i>Likums “Par uzņēmumu ienākuma nodokli”</i>)</li> </ul>  |
| <b>Regulatory barriers</b> |   |
| <b>Inbound</b>             | <p><b>Foreign Crowdfunding platform addresses Latvian investors</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platforms <ul style="list-style-type: none"> <li>– may be required to obtain a licence under FIML / Payment Services and E-Money Law / AIFM Law / Consumer Rights Protection Law/ Credit Institution Law; or</li> <li>– may be required to notify the FCMC on an existing licence in another EU member state;</li> <li>– the obligations to obtain a specific licence or to notify on an existing licence are highly uncertain and fact-specific</li> <li>– may be subject to other requirements, such as AML/CTF, consumer crediting rules and other regulations applicable to entities holding a particular licence;</li> <li>– Latvian law does not recognize the concept of “security trustee” allowing an agent to hold and enforce security on behalf of multiple lenders;</li> <li>– the assignment of claims through peer-to-peer lending platforms is not clear from the taxation perspective.</li> </ul> </li> <li>• Foreign companies or projects - Prospectus requirement and AIFMD regulation might apply, depending on the circumstances.</li> </ul> <p><b>Foreign Crowdfunding platform addresses Latvian investors, companies or projects in Latvia</b></p> <p>No specific regulatory barriers.</p> |
| <b>Outbound</b>            | <p><b>Latvian Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platforms <ul style="list-style-type: none"> <li>– may be required to obtain a licence under FIML / Payment Services and E-Money Law / AIFM Law / Consumer Rights Protection Law/ Credit Institution Law</li> <li>– the obligation to obtain a specific licence is highly uncertain and fact-specific</li> <li>– may be subject to other requirements, such as AML/CTF and other regulations applicable to entities holding a particular licence</li> <li>– the assignment of claims through peer-to-peer lending platforms is not clear from the taxation perspective.</li> </ul> </li> </ul>  |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>Foreign and domestic companies and projects - prospectus requirement and AIFMD regulation might apply.</li> </ul> <p><b>Latvian Crowdfunding platform addresses foreign companies or projects</b></p> <p>No specific regulatory barriers.</p> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | <p>Latvian FIML generally mirrors the prospectus rules provided in the Prospectus Regulation ((EC) No 809/2004).</p> <p>Thus, if Crowdfunding platform is considered as an investment service provider, it is subject to prospectus rules provided in the Regulation.</p>            |
| <b>AIFM-Directive</b>          | <p>So far, no known Crowdfunding platforms have been subject to the Latvian rules implementing the AIFM Directive.</p>   |
| <b>MiFID / MiFID II</b>        | <p>Financial Instrument Markets Law implements the MiFID I.</p> <p>MiFID II Directive is planned to be implemented in Latvia by the extended deadline. Thus, there has not yet been an impact to Crowdfunding platforms by the directive.</p>  |
| <b>PSD / PSD II</b>            | <p>PSD II Directive is planned to be implemented in Latvia by the deadline, that is, January 2018. Thus, there has not yet been an impact to Crowdfunding platforms by the directive.</p>  |

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# Lithuania

## 1 Recent developments in the market of Crowdfunding in Lithuania

During the last years there were the following significant developments in Lithuania regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Since adoption of the Law on Crowdfunding of the Republic of Lithuania (*Lietuvos Respublikos sutelktinio finansavimo įstatymas*; the “Law on Crowdfunding”) in November 2016, the Crowdfunding, including equity based Crowdfunding, became legal in Lithuania. After the Law on Crowdfunding came into effect, only few operators of Crowdfunding platforms were included into the Public List of Crowdfunding Platform Operators (the “List”) and obtained the right to engage in Crowdfunding activities. None of these operators of Crowdfunding operators declared their intentions to engage in equity based Crowdfunding due to several reasons:

- A. Equity model can be used only by public limited liability companies, which share capital must be at least EUR 50,000.
- B. Legal uncertainty if it is possible to increase the share capital without physical participation of the Crowdfunding investors (requirement to provide the signed share subscription agreements to the notary public).

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

The trend of lending based Crowdfunding in Lithuania becomes more popular due to a new regulation on Crowdfunding and peer-to-peer consumer lending. New regulation led to a development of lending based Crowdfunding platforms and peer-to-peer consumer lending platforms that now have the biggest piece in the rather small Crowdfunding market in Lithuania.

The lending based Crowdfunding in Lithuania developed as follows:

- A. Investors (individuals) lend funds to the individual in return for repayment of the loan and interest on their investment (the “P2P Consumer Lending”). This form of lending based Crowdfunding is regulated by the Law on Consumer Credit of the Republic of Lithuania (*Lietuvos Respublikos vartojimo kredito įstatymas*; the “Law on Consumer Credit”).
- B. Investors (either individuals or legal entities) lend funds to the company / project in return for repayment of the loan and interest on their investment (the “P2P Business Lending”). This form of lending based Crowdfunding is regulated by the Law on Crowdfunding.

- C. The project owner (legal entity) offers debt securities (i.e. bonds) to the investors. This form of lending based Crowdfunding is also regulated by the Law on Crowdfunding.

In Lithuania there are currently three operating lending based Crowdfunding platforms and according to the market rumours many more are willing to apply to the Lithuanian financial supervisory authority the Bank of Lithuania in order to be included into the List and start their operations. This shows a great interest in lending based Crowdfunding market in Lithuania, which is expected to grow each month. One Crowdfunding platform – *Myriad Capital* – should soon start its operations and invite limited liability companies to raise funds by publicly offering debt securities (i.e. bonds) to the investors.

In the past few months (i.e. March – May 2017) investors together have invested each month approximately EUR 800,000 through the lending based Crowdfunding platforms in Lithuania. Furthermore, P2P Consumer Lending became more popular in Lithuania. In 2015 lenders have provided approximately 2 thousand consumer credits that amounts to EUR 2.3m. There is no official statistics of P2P Consumer Lending in 2016, thus the numbers shall be higher due to a fast development of P2P Consumer Lending in Lithuania.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

There are no Crowdfunding platforms operating in Lithuania based on donations or rewards model.

A Crowdfunding platform based on donations or rewards would be governed by the Civil Code of the Republic of Lithuania (*Lietuvos Respublikos civilinis kodeksas*; the “Code”). Under the Code, relationships between the parties where individuals provide money to a company or project for benevolent reasons can be qualified as a contract of gift and those provided for a non-monetary reward can be qualified as a sale and purchase agreement. Tax implications for the recipient of funds should be assessed when implementing the donations or rewards model since the received funds would likely be considered as taxable income.

However, for example, lending based Crowdfunding platform are not prohibited to offer a project where individuals may provide money for benevolent reasons.

### **1.4 Real Estate Crowdfunding / Renewables Crowdfunding**

There are no specific real estate Crowdfunding platforms operating in Lithuania. Yet, there are no limitations for Crowdfunding platforms to offer real estate Crowdfunding. The real estate Crowdfunding in Lithuania would fall under the scope of the Law on Crowdfunding.

Currently the trend of real estate Crowdfunding is highly increasing in the market taking into consideration the amount of projects on real estate in lending based Crowdfunding platforms. Therefore, we expect that new participants in the Crowdfunding market

specialising in real estate Crowdfunding will start their operations in the near future due to a rather favourable regulation.

Crowdfunding platform Rontgen announced that it has filed application to the Bank of Lithuania to be included into the List, with the aim to start real estate Crowdfunding activities. Furthermore, an Estonia Crowdfunding platform Estate Guru specialising in real estate Crowdfunding is an active participant in Lithuanian market where Lithuanian real estate projects are crowdfunded.

There was no initiative regarding renewables Crowdfunding in Lithuania. In addition, there are no Crowdfunding platforms or projects related to renewables Crowdfunding in other platforms.

### **1.5 International approach**

There is no publicly available information that foreign country based Crowdfunding platforms are planning to expand into Lithuania.

## **2 Recent developments regarding Crowdfunding regulation in Lithuania**

### **2.1 Law on Crowdfunding**

The Law on Crowdfunding came into force on 1<sup>st</sup> December 2016. The law eliminated regulatory obstacles in Lithuania on establishing and running debt based and equity based Crowdfunding platforms. The Law on Crowdfunding has also established a regulation of marketplace lending platforms engaged in assignment of claim rights deriving from already concluded agreements, which could be used, for example, in invoice trading models.

The regulatory regime has been adopted in order to help organising easier ways for companies to attract funding through loans or in other monetary form; and issuance of financial instruments. For example, Lithuanian private limited liability companies are finally allowed to issue bonds and offer them publicly, including distributing them through Crowdfunding platforms. Before the Law on Crowdfunding came into force, according to the opinion of the Bank of Lithuania, the Crowdfunding platform operators engaged in equity or lending based Crowdfunding needed to obtain a credit institution licence.

#### **2.1.1 Key features of the Law on Crowdfunding:**

- A. Legal entities are allowed to raise capital through Crowdfunding platforms using one of four different instruments: (i) simple loan agreement; (ii) issue of debt securities (i.e. bonds); (iii) issue of equity securities (i.e. shares); or (iv) assignment of claim rights deriving from already concluded agreements. However, private limited liability companies are not allowed to publicly offer their shares.
- B. Legal entities are allowed to act as operators of Crowdfunding platforms. Before starting their activities, operators must be included in the Lists managed by the Bank of Lithuania.

- C. Investors are able to freely invest in Crowdfunding projects without limitations. Investors have to do an appropriateness test. If the results of the test are negative, the Crowdfunding platform operator must provide a warning / disclaimer and then the investor can start investing on its own risk.
- D. The secondary market on the Crowdfunding platform for securities distributed through the Crowdfunding is qualified as a multilateral trading facility and falls under regulation of the Law on Markets in Financial Instrument (Lith. Lietuvos Respublikos finansinių priemonių ir rinkų įstatymas; the “Law on MiFI”), which in turn implements the Markets in Financial Instruments Directive (the “MiFID”). This requirement for the secondary market applies only for the secondary market in financial instruments other than claim rights deriving from loan agreements.
- E. Crowdfunding platform operator falls under exemption of Article 3 of MiFID and has the right to provide the following investment services: (i) execution of orders; and (ii) provision of investment recommendations.
- F. If the offering is up to EUR 5m, the project owner must prepare an information document which must be approved by the Crowdfunding platform operator. There is no need to prepare a prospectus – “light prospectus regime”. An information document is a simple form document that contains general information about the project owner and risks related to the offering. Offerings above EUR 5m require preparation of the prospectus, which must be approved by the Bank of Lithuania.
- G. The capital requirement for the Crowdfunding platform operator amounts to EUR 40,000. However, the own capital cannot be lower than the bigger of the following amounts: EUR 40,000 or the need of own capital, which must be at least 0.2% of the amount of outstanding funds financed through the Crowdfunding platform and not repaid to investors.

## 2.2 Law on Consumer Credit

The P2P Consumer Lending in Lithuania falls under regulation of consumer credit. Regulation of the P2P Consumer Lending entered into force as of 1 February 2016.

The amended Law on Consumer Credit introduces regulation on P2P Consumer Lending. This type of lending is currently not separately regulated in Lithuania. Existing Lithuanian P2P Consumer Lending platforms are associated with consumer activities and must be included in the Public List of Peer-to-Peer Consumer Lending Operators, managed by the Bank of Lithuania.

In general P2P Consumer Lending activities are regulated in the same way as consumer lending. For example, the operator of a P2P Consumer Lending platform is required to comply with the same requirements set for consumer credit providers, such as advertising limitations, pre-contractual information requirements, creditworthiness assessment rules, etc.

Moreover, the amended Law on Consumer Credit contains some specific requirements for operators of the P2P Consumer Lending platforms:

- A. The authorised capital of a P2P Consumer Lending platform's operator should be at least EUR 40,000.
- B. An operator must prepare and approve a business continuity plan setting measures and procedures to ensure that P2P Consumer Lending platform activities are carried out continuously and without interruption, as well as ensuring the smooth functioning of consumer credit contract administration and continuous implementation of contractual obligations in case of unforeseen circumstances.
- C. An operator must publish certain information about itself and the lending process on its website as well as disclose certain information to the lender prior to concluding a loan agreement.

However, the amended Law also contains some controversial provisions:

- A. Legal persons cannot be lenders on the P2P Consumer Lending platforms.
- B. Each lender may lend to a particular borrower up to EUR 500 for any 12-month period.
- C. An operator of a P2P Consumer Lending platform may calculate its commission fee only from repayments already paid by the borrower to the lender.

### 2.3 Remote identity verification

On 26 October 2016 the Lithuanian Government amended its resolution establishing client identity verification methods by adding additional methods for remote identification. The amended resolution came into effect on 1 December 2016. This regulatory development was crucial for Crowdfunding development. Without a modern regulation on non-face-to-face identification, Lithuanian Crowdfunding platforms would be local and with low possibilities to be fully online solutions.

Under the amended resolution, remote identification is possible in the following ways:

- A. When information about a person's identity is certified by a qualified electronic signature which complies with the requirements of Regulation (EU) No 910/2014.
- B. When information about a person's identity is confirmed by electronic identification means issued in the European Union and functioning under electronic identification schemes with high or substantial assurance level under Regulation (EU) No 910/2014.
- C. Using electronic means, allowing direct view transmission, in one of the following ways: (i) Identity document or residence permit in Lithuania captured using video-streaming and identity confirmation using at least an advanced electronic signature, meeting the requirements of Regulation (EU) No 910/2014; or (ii) Client's facial image and original identity document or residence permit in Lithuania captured using video-streaming.

Detailed arrangements for the use of electronic means for video-streaming are confirmed by the Lithuanian Financial Crime Investigation Unit. There is a requirement for video-streaming to be direct and live, which means that videos or photos not taken during the live video-streaming are not accepted.

### **3 Current Regulation of Crowdfunding in Lithuania**

#### **3.1 Banking / Financial Service licence requirements**

##### **3.1.1 Equity / Lending model**

As mentioned above, only legal entities are allowed to act as operators of Crowdfunding platforms. Before starting their activities, operators must be included in the List. For more information, please refer to Section 2.1 above.

Operators included in the List are considered to be financial advisory firms under the Law on MiFI. In other words, a financial advisory firm is a firm that enjoys exemption from Article 3 of the MiFID. According to the Law on MiFI, a financial advisory firm may provide:

- A. Execution-only services (i.e. reception and transmission of orders).
- B. Offer investment recommendations.

According to the Law on Crowdfunding, an operator that wishes to provide investment services other than execution-only services and provision of investment recommendations must be licensed under the Law on MiFI as a financial brokerage firm.

The Crowdfunding platform does not need to separately apply for the financial advisory firm's licence, if the investment services specified in the Law on MiFI (i.e. execution-only services and offering of investment recommendations) are related to Crowdfunding agreements.

##### **3.1.2 P2P Consumer Lending**

The operator of a P2P Consumer Lending platform is required to be listed on the Public List of P2P Consumer Lending Platforms' Operators administered by the Bank of Lithuania only. For more information, please refer to Section 2.2 above.

##### **3.1.3 Donations or Rewards Model**

As mentioned above, the Crowdfunding platform based on donations or rewards is governed by the Code. Under the Code, relationships between the parties where individuals provide money to a company or project for benevolent reasons can be qualified as a contract of gift and those provided for a non-monetary reward can be qualified as a sale and purchase agreement. Therefore, there is no specific regulation regarding licence requirements for donations or rewards model based Crowdfunding platforms. The Law on Crowdfunding explicitly excludes such platforms from the regulation.

## 3.2 Prospectus requirements

### 3.2.1 Equity / Lending Model

#### 3.2.1.1 Securities

If securities (shares and / or bonds) are publicly offered to investors, the company issuing the securities has to publish a prospectus. The prospectus can be published only with the approval of the Bank of Lithuania. The requirements for the preparation, submission and approval of the prospectus as well as the exemptions from the requirement to publish the prospectus are established in the Law on Securities of the Republic of Lithuania (*Vertybinių popierių įstatymas*; the “Law on securities”).

The obligation to publish a prospectus does not apply in the presence of at least one of the following conditions:

- A. An offer of securities addressed solely to professional investors.
- B. An offer of securities addressed to fewer than 150 natural or legal persons in each Member State of EEA, other than professional investors.
- C. An offer of securities addressed to investors who acquire securities for a total amount of at least EUR 100,000 for each separate offer.
- D. An offer of securities with the nominal value amounting to at least EUR 100,000 per unit.
- E. An offer of securities with a total amount less than EUR 100,000 calculated over a period of 12 months.

Moreover, the requirement to publish a prospectus is also not applicable if the securities are offered through a Crowdfunding platform and the project owner is willing to raise below EUR 5m in a 12 month period. In such case Lithuanian laws applies the light prospectus regime where project owner must prepare an information documents, which must be approved by the Crowdfunding platform operator.

In case of offerings through Crowdfunding platform above EUR 5m, the prospectus regime is applicable in accordance with the Law on Securities. Where the securities are publicly offered via the Crowdfunding platform, the operator of the platform is not responsible for publishing the prospectus. However, the operator shall make the prospectus public on the platform and easily accessible to each investor.

#### 3.2.1.2 P2P Business Lending

In accordance with the above mentioned and the Law on Securities, if a project owner is willing to raise above EUR 5m through a Crowdfunding platform in a 12 month period, it is allowed to do so only by issuing securities (i.e. shares or bonds). In such case the prospectus regime is applicable and the prospectus must be prepared and approved by the Bank of Lithuania.

If the project owner raises below EUR 5m, it could use simple loan instrument or debt securities (i.e. bonds). In such case the project owner must prepare only an information document. Regulation of information document is fully applicable in lending model and only if the project amount exceeds EUR 100 thousand information document shall be prepared.

### 3.2.1.3 P2P Consumer Lending

As mentioned above, the Law on Consumer Credit is applicable for P2P Consumer Lending activities. The regulation on prospectus is not applicable for P2P Consumer Lending since an individual is seeking to borrow funds through the P2P Consumer Lending platform.

Borrowing limits are set by compliance with the credit-worthiness assessment requirements. When entering into a credit agreement the creditworthiness assessment shall be done not only of a borrower, but also of his/her spouse. It is required to obtain the spouse's approval to perform such checks and it makes online business difficult.

### 3.2.2 Donations and Rewards Model

The regulation on prospectus is not applicable for donations and rewards model since the Crowdfunding platform based on donations or rewards is governed by the Code. The Code determines the form of a contract of gift based on a gift amount:

- A. If the amount of a gift exceeds EUR 1,500 the contract of a gift shall be concluded in a written form.
- B. If the amount of a gift exceeds EUR 14,500 the contract of a gift shall be notarized.

## 3.3 Regulation of Crowdfunding under the AIFMD regime

AIFMD regime which was implemented in Lithuania by means of the Law on Managers of Collective Investment Undertakings for Professional Investors of the Republic of Lithuania (Lietuvos Respublikos profesionaliesiems investuotojams skirtų kolektyvinio investavimo subjektų valdymo įmonių įstatymas; the "Law on Managers of Funds").

According to the Law on Managers of Funds, the AIFMD regulation of funds and fund managers applies when there is an alternative investment fund (the "AIF") managed by an alternative investment fund manager (the "AIFM"). The Law on Managers of Funds provides that AIFs include a collective investment undertaking which:

- A. Raises capital (through equity-based securities) from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors.
- B. Is not an operating company conducting business outside the financial sector.
- C. Does not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS).

### 3.3.1 Equity Model

Lithuanian AIFMD regulation should not apply to companies issuing equity securities through the Crowdfunding platform that qualify as operating companies outside the financial sector. Taking this into account, projects that are seeking funding by means of a Crowdfunding platform could be qualified as operating companies outside the financial sector, if:

- A. Their business strategy is simply the commercial success of their business.
- B. They do not intend to follow any defined investment policy, but want to finance their on-going day-to-day business.
- C. They operate the facility, production or project themselves within their day-to-day business or make use of the service of an intra-group company or an external service provider (as long as the day-to-day discretion remains at the company).

The above list of criteria is non-exhaustive and in practice might be amended and/or supplemented accordingly by the Bank of Lithuania.

### 3.3.2 Lending Model

Investments by means of debt securities, i.e. bonds, and loans can generally be structured as non-AIF investments, since the investors do not share liability for any losses – and, therefore, do not invest in a collective investment undertaking. Consequently, such projects should be excluded from any possible regulation under the AIFMD.

### 3.3.3 Donations and Rewards Model

Donations and / or rewards based Crowdfunding projects may offer in return some non-financial rewards as an alternative to any kind of revenue. In such event it can be argued that the funds are not invested for the benefit of those investors and the funding therefore contains no collective investment undertaking and no AIF. Thus, such Crowdfunding project should be excluded from any possible regulation under the AIFMD.

In a nutshell, a Crowdfunding platform arranges investments into projects or companies. Since, an operator of a Crowdfunding platform usually does not raise capital from investors for its own business, it should not qualify as an AIF. Therefore, the operator of a Crowdfunding platform should not be qualified as an AIF or an AIFM and the AIFMD shall not be applicable.

## 3.4 Regulation under the Payment Services Directive

The Payment Services Directive was implemented in Lithuania by the Law on Payments of the Republic of Lithuania (*Lietuvos Respublikos mokėjimų įstatymas*; the “Law on Payments”). The provision of payment services is subject to the licencing requirements in Lithuania. In accordance with the Law on Payments, the transfer of funds, for example, between the Crowdfunding platforms, may be considered as a payment service and the Crowdfunding platform therefore will be a subject of licencing requirements (i.e. payment service provider).

Moreover, if the funds of users of a Crowdfunding platform are held in the account of the operator of a Crowdfunding platform for indefinite period, the operator is required to have a licence of at least an electronic money institution. Electronic money institution's licence allows the provision of payment services referred to in Law on Payments. Such licence is issued based on the Law on Electronic Money and Electronic Money Institutions of the Republic of Lithuania (*Lietuvos Respublikos elektroninių pinigų ir elektroninių pinigų įstaigų įstatymas*).

Since the licencing procedure may take approximately three months to complete and includes a significant amount of paperwork, EU-licensed payment service providers may choose to provide payment services on a cross-border basis without establishing a branch (i.e. to passport their licence) by notifying about the intention to provide payment services in Lithuania through its home Member State supervisory authority to the Bank of Lithuania.

Furthermore, the Crowdfunding platforms are allowed to conclude outsourcing agreements and outsource funds' handling function to other licenced institution – credit institution, payment and/or electronic money institution. In such way Crowdfunding platform would avoid licencing requirement for provision of certain payment services.

### 3.5 Possible additional regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- A. Law on Prevention of Money Laundering and Terrorist Financing of the Republic of Lithuania (Lith. Lietuvos Respublikos Pinigų plovimo ir teroristų finansavimo prevencijos įstatymas);
- B. Law on Legal Protection of Personal Data Protection of the Republic of Lithuania (Lith. Lietuvos Respublikos Asmens duomenų teisinės apsaugos įstatymas);
- C. Law on Electronic Money and Electronic Money Institutions of the Republic of Lithuania (Lith. Lietuvos Respublikos elektroninių pinigų ir elektroninių pinigų įstaigų įstatymas).

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable Law

According to unofficial interpretation of the Lithuanian regulator, financial regulation applies in case Lithuanian investors are approached by foreign financial institutions. Although there is no official position or guideline on provision of cross-border financial services, the marketing focussed approach is applicable in Lithuania. This means that only providers of financial services that have their registered office or ordinary residence in Lithuania fall under Lithuanian regulatory law but also in case the financial institution targets the Lithuanian market in order to offer financial services to companies / persons in Lithuania. Few indicators to assume that financial services are pointed to the Lithuanian market:

- A. Addressing of potential Lithuanian investors by direct contact (through mail, fax, e-mail, etc.).
- B. A series of factors show that products are targeted to potential Lithuanian investors: domain name, website language, contact details, disclaimers, etc.

## 4.2 Inbound

### 4.2.1 Crowdfunding platform addresses Lithuanian investors

According to Part 2 of Article 6 of the Law on Crowdfunding, person engaged or willing to engage in the activities of an operator of a Crowdfunding platform in the Republic of Lithuania must have a residence in the Republic of Lithuania, except the case when a person registered in other EU Member State have the right in accordance with the laws of the Republic of Lithuania governing provision of investment services to intermediate in conclusion of financial transactions without a registered office or through an established branch in the Republic of Lithuania. Therefore, foreign Crowdfunding platform willing to address Lithuanian investors must either establish a subsidiary in Lithuania and include it in the List, or it must have the right in accordance with the laws of the Republic of Lithuania governing provision of investment services to intermediate in conclusion of financial transactions without a registered office or through an established branch in the Republic of Lithuania. In other words, if the foreign Crowdfunding platform has the MiFID licence, it can engage in Crowdfunding activities in the Republic of Lithuania after it passports its licence into the Republic of Lithuania.

Foreign companies / projects willing to attract funds in the Republic of Lithuania through the Crowdfunding platform must comply with requirements deriving from the Law on Crowdfunding. The main requirement for the companies / projects would be to prepare an information document or a prospectus, depending on the offering size. For more information please refer to Section 2.1 above.

### 4.2.2 Crowdfunding platform wants to present Lithuanian companies / projects on its platform

Regulatory barriers would depend on the applicable law for the offering. In case the Lithuanian company issues securities through the Crowdfunding platform, the prospectus regime is applicable. Regarding exemptions from the prospectus regulation applicability, please refer to Section 3.2.1.1 above.

If the Lithuanian company needs to prepare a prospectus, it must be registered with the Bank of Lithuania. The requirement to register the prospectus with the Bank of Lithuania would not be applicable according to Part 3 of Article 4 of the Law on Securities if the issues of non-equity securities' (or for any issues of non-equity securities, provided that the issuer of non-equity securities is not the issuer of the underlying securities and is not related to the issuer of the underlying securities) denomination per unit amounts to at least EUR 1,000. In such case the issuer can select the home Member State for the offering other than the Republic of Lithuania.

## 4.3 Outbound

### 4.3.1 Lithuanian Crowdfunding platform addresses investors in another EU country

If Lithuanian Crowdfunding platform addresses investors in another EU country, the Crowdfunding platform should comply with the law of another EU country. Neither the Law on Crowdfunding nor the Law on Consumer Credit regulates such activity. However, if the investors from another EU country initiate the contact, the reverse solicitation principle should be applied.

If natural or legal persons approach the Lithuanian Crowdfunding platform and register in order to invest into Crowdfunding projects, such approach should be regarded as reverse solicitation and the provision of services on the basis of such approach should not trigger other EU country regulation. Since neither the Lithuanian law nor the EU law determines clear rules on reverse solicitation, for the purpose of determining whether the services are provided within or outside the territory of Lithuania the Commission Interpretative Communication – Freedom to provide services and the interest of the general good in the Second Banking Directive (SEC(97) 1193 final) should be taken into account.

Nevertheless, in case the services were provided due to the client initiating the contact, the question as to whether services fall within the category of reverse solicitation is subject to the nature of the services, the actions of the Crowdfunding platform and the client. The provision of services by way of reverse solicitation must be carried out exclusively on the basis of the client's unsolicited approach and no promotion may be performed by the Crowdfunding platform.

### 4.3.2 Lithuanian Crowdfunding platform addresses companies / projects in another EU country

If Lithuanian Crowdfunding platform addresses companies / projects in another EU country, the Crowdfunding platform should comply with the law of another EU country. Neither the Law on Crowdfunding nor the Law on Consumer Credit regulates such activity. However, if the company / project from another EU country initiate the contact, the reverse solicitation principle should be applied. For more information about the reverse solicitation principle, please refer to Section 4.3.1 above.

## 4.4 Impact of EU regulation

As for the EU regulation, please refer to the above Sections. However, it must be noted that MiFID II and PSD II have not been transposed into Lithuanian laws yet. Once the latter EU laws will be transposed, we might expect changes in the regulation on Crowdfunding.

## 4.5 Summary

With the growing number of countries implementing specific Crowdfunding regulation it is becoming more burdensome for European market participants to develop a pan-European

Crowdfunding business and for foreign Crowdfunding platforms to enter into the European market. Only those Crowdfunding platforms that are in the List or have the MiFID licence and have passported it to Lithuania can engage in Crowdfunding activities within the territory of the Republic of Lithuania. Moreover, not clear interpretation of the reverse solicitation principle brings legal uncertainty what is allowed and what is not for a Crowdfunding platform when targeting investors and/or companies / projects from another EU country. These developments are contrary to the aim of establishing a European single market and promoting Crowdfunding as a method of financing on a European level.

## **5 Lessons learned from Lithuania regulation for possible harmonised European Crowdfunding regulation**

### **5.1 Role models (“dos”)**

For possible harmonised European Crowdfunding regulation, the following aspects can serve as a role model:

- A. Exception from prospectus requirement for offerings up to EUR 5 million
- B. Information document requirement for offerings up to EUR 5 million
- C. Unlimited investment amounts
- D. Application of the appropriateness test
- E. Crowdfunding platform operator has the right to provide execution of order services and investment recommendations
- F. The right for the Crowdfunding platform operator to act as the mortgage security agent

### **5.2 Aspects that should be avoided (“don’ts”)**

The following aspects should not be inherited:

- A. Prohibition to distribute convertible securities through the Crowdfunding platform
- B. Lack of regulation on conclusion of Crowdfunding contracts through the Crowdfunding platform (notary public questions legality of the contracts concluded through the Crowdfunding platform by conclusive actions).

## **6 Conclusion**

Lack of single EU regulation on Crowdfunding, different interpretation of EU laws applicable to Crowdfunding activities and local Crowdfunding regimes hinder all Crowdfunding platforms to extend their activities to cross-border businesses. The increasing fragmentation of the national Crowdfunding regulations amplifies obstacles for cross-border Crowdfunding.

Creation of a single EU regulation on Crowdfunding would create a level playing field around the EU. Such single EU regulation on Crowdfunding should take into account:

- A. Regulation of all types of financial instruments used in Crowdfunding.

- B. Clarification whether MiFID licence and its passport would allow provision of Crowdfunding on cross-border basis.
- C. Clarification how other EU laws affect Crowdfunding.

## 7 Summary – Crowdfunding regulation

| Country   | Lithuania   |
|---|---|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• The Law on Crowdfunding of the Republic of Lithuania (<i>Lietuvos Respublikos sutelktinio finansavimo įstatymas</i>) came into force on 1 December 2016. It has eliminated regulatory obstacles in Lithuania on establishing and running debt based and equity based Crowdfunding platforms.</li> <li>• P2P Consumer Lending in Lithuania falls under regulation of consumer credit. Regulation of P2P Consumer Lending platforms entered into force as of 1 February 2016.</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>                            |   |
| <b>General regulation</b>   | <ul style="list-style-type: none"> <li>• To engage in lending based and / or equity based Crowdfunding, the Crowdfunding platform operator must be included in the Public List of Crowdfunding Operators, managed by the Bank of Lithuania.</li> <li>• To engage in P2P Consumer lending, the P2P Consumer Lending platform operator must be included into the Public List of P2P Lending Platforms, managed by the Bank of Lithuania.</li> <li>• Reward based and donation based Crowdfunding is unregulated activity which falls under the scope of the Civil Code of the Republic of Lithuania (Lith. Lietuvos Respublikos civilinis kodeksas).</li> </ul>   |
| <b>Prospectus requirements</b>  | <p>Prospectus requirement for the public offering of securities. The obligation to publish a prospectus does not apply in the presence of at least one of the following conditions:</p> <ul style="list-style-type: none"> <li>• An offer of securities addressed solely to professional investors;</li> <li>• An offer of securities addressed to fewer than 150 natural or legal persons in each Member State of EEA, other than professional investors;</li> <li>• An offer of securities addressed to investors who acquire securities for a total amount of at least EUR 100,000 for each separate offer;</li> <li>• An offer of securities with the nominal value amounting to at least EUR 100,000 per unit;</li> <li>• An offer of securities with a total amount of less than EUR 100,000 in all Member States calculated over a period of 12 months.</li> </ul> <p>Moreover, offerings of securities through a Crowdfunding platform below EUR 5 million in a 12 month period does not fall under prospectus requirement. In such case Lithuanian laws applies the light prospectus regime where project owner must prepare an information documents, which must be approved by the Crowdfunding platform operator.</p> |
| <b>AIFMD-regulation</b>   | <p>As collective investment undertakings are defined in a very comprehensive way, RES projects can easily serve the purpose of such definition and could therefore fall within the AIFMD regulation which is implemented in</p>   |

|                                      |  |
|--------------------------------------|--|
|                                      | Lithuania through the Law on Managers of Collective Investment Undertakings for Professional Investors of the Republic of Lithuania (Lith. <i>Lietuvos Respublikos profesionaliesiems investuotojams skirtų kolektyvinio investavimo subjektų valdymo įmonių įstatymas</i> ). However, there is no practice in Lithuania, nor are there any regulatory explanations as to how AIFMD could be applied with respect to RES projects.   |
| <b>Payment service regulation</b>    | Transfer of funds via the operator may be considered as payment services, thus, may be subject to licensing requirements in Lithuania in accordance with the local legislation on payment services, which implements the Payment Service Directive.  |
| <b>Consumer credit regulation</b>    | Amended Law on Consumer Credit of the Republic of Lithuania (Lietuvos Respublikos vartojimo kredito įstatymas; the “Law on Consumer Credit”) is applicable in the case of P2P Consumer Lending   |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Law on Prevention of Money Laundering and Terrorist Financing of the Republic of Lithuania (<i>Lietuvos Respublikos pinigų plovimo ir teroristų finansavimo prevencijos įstatymas</i>).</li> <li>• Law on Legal Protection of Personal Data of the Republic of Lithuania (<i>Lietuvos Respublikos asmens duomenų teisinės apsaugos įstatymas</i>).</li> <li>• Law on E-money and E-money Institutions of the Republic of Lithuania (<i>Lietuvos Respublikos elektroninių pinigų ir elektroninių pinigų įstaigų įstatymas</i>).</li> <li>• Law on Consumer Credit of the Republic of Lithuania (<i>Lietuvos Respublikos vartojimo kredito įstatymas</i>).</li> </ul>   |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <ul style="list-style-type: none"> <li>• According to the Law on Crowdfunding, person engaged or willing to engage in the activities of an operator of a Crowdfunding platform in the Republic of Lithuania must have a residence in the Republic of Lithuania, except the case when a person registered in other EU Member State have the right in accordance with the laws of the Republic of Lithuania governing provision of investment services to intermediate in conclusion of financial transactions without a registered office or through an established branch in the Republic of Lithuania.</li> <li>• In case the Lithuanian company issues securities through the foreign Crowdfunding platform, the prospectus regime is applicable.</li> </ul> |
| <b>Outbound</b>                      | <ul style="list-style-type: none"> <li>• If Lithuanian Crowdfunding platform addresses investors in another EU country, the Crowdfunding platform should comply with the law of another EU country. Neither the Law on Crowdfunding nor the Law on Consumer Credit regulates such activity. However, if the investors from another EU country initiate the contact, the reverse solicitation principle should be applied.</li> <li>• If Lithuanian Crowdfunding platform addresses companies / projects in another EU country, the Crowdfunding platform should comply with the law of another EU country. If the company / project from another EU</li> </ul>   |

|                                |   |
|--------------------------------|---|
|                                | country initiate the contact, the reverse solicitation principle should be applied.   |
| <b>Impact of EU regulation</b> |   |
| <b>Prospectus regulations</b>  | Please see above  |
| <b>AIFM-Directive</b>          | Please see above  |
| <b>MiFID / MiFID II</b>        | According to the Law on Crowdfunding, the operator of the platform is considered to be financial advisory firm which falls under Article 3 of MiFID exemption and has the right to provide the following investment services without additional licence: execution of orders and provision of investment recommendations. |
| <b>PSD / PSD II</b>            | For fund's handling activities the Crowdfunding platform must obtain payment or electronic money institutions licence or outsource this function to another financial institution able to provide respective financial services.  |

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# Luxembourg

## 1 Recent developments in the market of Crowdfunding in Luxembourg

To our knowledge, there are currently only two Crowdfunding platforms that are active in Luxembourg, both are foreign-based. The one is built on the Equity Model and the other one on the Rewards Model. There have been several local attempts to launch Crowdfunding platforms on the Luxembourg market but these platforms have ceased their initiative shortly after. Compared to other countries where Crowdfunding is an increasingly popular method of raising capital, Luxembourg is rather in the testing phase.

### 1.1 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

One of the world's largest US-based Crowdfunding platform built on the Rewards Model has expanded its activity into Luxembourg in 2015 and it is the only Rewards-based platform that is currently active in Luxembourg. It finances creative projects and investors were given non-monetary rewards, for example in the form of special thanks on the album cover of a CD, the production of which was financed via the platform.

### 1.2 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

The other active foreign-based Crowdfunding platform available in Luxembourg is built after the Equity Model. It is used to finance projects in start-ups and innovative businesses in general in the seed phase, including real estate projects. Indeed, it is the first platform that has introduced a real estate project to be funded through equity Crowdfunding in Luxembourg. In return, the investors receive ownership of a small piece of the businesses and become "shareholders" of the business(es) they have invested in.

### 1.3 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

There is currently no Crowdfunding platform under the Lending Model that operates in Luxembourg.

### 1.4 Real Estate Crowdfunding /Renewable Crowdfunding

Currently there is no Crowdfunding platform solely presenting real estate projects. As mentioned under point 1.2, there is currently one active Equity-based Crowdfunding that also offers real estate projects.

Regarding the Renewable Crowdfunding, there is, to this date, no Crowdfunding platform specialised on funding renewable energy sources projects that has been established in or imported into Luxembourg.

As a general remark compared to other countries, Luxembourg's Crowdfunding activity is very limited. This is for the most part due to the size of the local market and the regulatory and operational costs linked to an activity that could in some cases fall under the supervision of the Luxembourg financial supervisory authority, the *Commission de Surveillance du Secteur Financier* ("CSSF").

The General Secretary of the CSSF Danièle Berna-Ost commented to us, that contrary to what is mentioned in the press, for the moment no Crowdfunding platform has obtained or needed to obtain an authorization from the CSSF. She explained that the CSSF has been approached on some few occasions and that after consideration of their business models, they have been solely considered as contact intermediaries bringing businesses looking for funds into contact with investors, which brought the CSSF to the conclusion that their activity is not subject to the prior authorisation of the CSSF.

### 1.5 International approach

In the last two years, a US Crowdfunding platform and platforms from other European countries have entered or plan to enter into the Luxembourg market. Their sustainability on the market depends on their overall market size as a key element for the financial success of a Crowdfunding platform. As a result of the cost-benefit considerations i.e. the size of the market vs. the cost of entering the market, local initiatives that have occurred have struggled to establish themselves whereas established and organized foreign-based Crowdfunding platforms could easily expand their activity to Luxembourg. Moreover, platforms might benefit from their business model, when it is based on the Donations and Rewards Model like in the case of the US-based Crowdfunding platform and may be exempted from the Luxembourg license requirements.

## 2 Recent developments regarding Crowdfunding regulation in Luxembourg

As of this moment, Luxembourg does not have any regulation that is specifically targeting at Crowdfunding. Given that relatively few Crowdfunding structures have been submitted to the CSSF so far and given that the considerations of the financial sector regarding Crowdfunding are somewhat embryonic at this stage, the positioning of the Luxembourg authorities is generally quite uncertain when dealing with a Crowdfunding structure. Luxembourg awaits the response at the European Union-level to develop a specific regulation for this investment tool. Therefore, the analysis of the Crowdfunding platforms based on the different models is to be done under the perspective of the existing legislation and regulations.

## 3 Current Regulation of Crowdfunding in Luxembourg

There is no such specific regulation regarding Crowdfunding platforms in Luxembourg yet, however following other laws and regulations may apply.

## **3.1 Banking / Financial licence requirements**

### **3.1.1 Equity Model and Lending Model**

#### **3.1.1.1 Licence under the law on the financial sector dated 5 April 1993, as amended**

Pursuant to the Luxembourg law on the financial sector, any natural person established in Luxembourg for professional reasons or any legal person governed by Luxembourg law whose regular occupation or business is to exercise an activity of the financial sector, (i.e. banks and other professionals of the financial sector) requires a licence from the CSSF. Depending on the services offered by the Crowdfunding platform, be it under the Equity or the Lending Model, it is possible that the law on the financial sector could be applicable, which would mean that the Crowdfunding platform could be required to obtain a licence in order to execute its activities. This would be the case if the Crowdfunding platform was to offer investment or banking services in Luxembourg. The Crowdfunding platform could, in particular, be considered an investment adviser, a broker in financial instruments, a commission agent, an investment firm operating a Multilateral Trading Facility in Luxembourg or a financial intermediation firm if it comes to investing under the Equity Model. Also, it could be qualified as a credit institution or possibly a professional carrying out lending activities if it was to grant loans under the Lending Model. In that respect, investors, if they invest through a Crowdfunding platform operating under the Lending Model (depending on the manner they are financed), might also be considered to provide banking or lending services for which a licence could in theory be required.

#### **3.1.1.2 Licence under the law on financial markets dated 13 July 2007, as amended**

Depending on the services offered by the Crowdfunding platform, the platform might be considered to constitute a Multilateral Trading Facility and the law on financial markets would become applicable. The platform would have to obtain a licence from the minister, having in his competences the CSSF, before beginning its activities.

### **3.1.2 Donations or Rewards Model**

A platform operating under the Donations and Reward Model should probably not fall within the scope of the law on financial markets and therefore no licence would be required.

## **3.2 Prospectus requirements**

Depending on the legal form of the companies looking for funds and on whether the securities issued by the companies would be viewed as transferrable or not, these companies addressing investors in Luxembourg could be required to publish a prospectus (or a simplified prospectus, as the case may be), which would have to get approved by the CSSF. The obligation to publish a prospectus would however not apply to the following type of offers of securities to the public:

(i) In case of securities offered by companies and which are to be EU-passported in accordance with Directive 2003/71/EC:

- an offer of securities addressed to qualified investors; and/or
- an offer of securities addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors; and/or
- an offer of securities addressed to investors who acquire securities for at least EUR 100.000 per investor, for each separate offer; and/or
- an offer of securities whose denomination per unit amounts to at least EUR 100.000; and/or
- an offer of securities with a total consideration of less than EUR 100.000, which limit shall be calculated over a period of 12 months.

(ii) In case of securities offered by companies in Luxembourg and which are not to be EU-passported:

- an offer of securities addressed to qualified investors; and/or
- an offer of securities addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors; and/or
- an offer of securities addressed to investors who acquire securities for at least EUR 100.000 per investor and for each separate offer; and/or
- an offer of securities whose denomination per unit amounts to at least EUR 100.000; and/or
- an offer of securities with a total consideration of less than EUR 1.500.000, which limit shall be calculated over a period of 12 months.

Offers of securities with a total consideration of more than EUR 1.500.000 and less than EUR 5.000.000 which limit shall be calculated over a period of 12 months, will require a simplified prospectus.

In case of securities offered by open-ended undertakings for collective investment (UCIs) or in case of securities offered which are to be admitted to trading on a stock exchange, other or additional rules and exemptions may also apply.

### **3.3 Regulation of Crowdfunding under the AIFMD regime in Luxembourg**

#### **3.3.1 Status of AIFMD implementation**

The AIFMD has been implemented on 12 July 2013 by the law on alternative investment fund managers.

##### **3.3.1.1 Definition of an alternative investment fund ("AIF")**

In his Article 1 paragraph 39, "AIFs" are defined as collective investment undertakings, including investment compartments thereof, which raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of

those investors, and do not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS)

If the managed Crowdfunding platform is not an “AIF”, the AIFM Law would not apply.

### **(1) Equity Model**

The European Securities and Markets Authority (ESMA) clarifies in his guidelines on key concepts of the AIFMD that a collective investment undertaking pools together capital raised from its investors for the purpose of investment with a view to generating a pooled return for those investors; “Pooled return” is defined by the ESMA as “the return generated by the pooled risk arising from acquiring, holding or selling investment assets – including the activities to optimise or increase the value of these assets – irrespective of whether different returns to investors, such as a tailored dividend policy, are generated” (see Annex III of the Final Report of the ESMA guidelines on key concepts of the AIFMD, p. 29 and 31).

Generally, Crowdfunding platforms do not pool the capital raised from the investors for the purpose of the investment and do not aim at generating a pooled return for those investors. Every investor acts independently and the platform theoretically does not intervene to pool the funds. However, depending on the business model of the Crowdfunding platform, it is possible that the Crowdfunding platform could be considered to fall within the definition of an AIF and, thus could fall within the scope of the law on AIFM, whereby licence requirements could apply.

### **(2) Lending model**

In accordance with the interpretation provided by ESMA, it is rather unlikely that a Crowdfunding platform operating under the Lending Model (and being financed through loans) would be considered an AIF.

### **(3) Donations or Rewards Model**

In our opinion a Crowdfunding platform operating under the Donations and Rewards Model would not be considered as an AIF and should therefore not fall within the scope of the law on alternative investment fund managers.

## **3.4 Regulation under the Payment Services Directive (and implementing local regulation)**

The Directive has been transposed in the law of 10 November 2009 on payment services, on the activity of electronic money institution and settlement finality in payment and securities settlement systems (the “PSD”).

The Crowdfunding undertaking may fall within the scope of the PSD. The envisaged services may constitute either (i) money remittance (in the event that no account is being created in the name of the payer or the payee) or (ii) payment transaction, which implies the existence of a payment account, at least, in the recipient’s side.

In the event that the Crowdfunding does fall within the scope of the PSD, potential exemption methods may to be addressed on a case-by-case basis.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Amended law on undertakings for collective investment dated 17 December 2010;
- Amended law relating to the investment company in risk capital (“SICAR”) dated 15 June 2004;
- Anti-money laundering law dated 12 November 2004, as amended;
- Law regulating the access to the occupations of craftsman, tradesman, industrialist and certain liberal professions dated 2 September 2011;

## 4 Regulatory barriers for Crowdfunding crossing borders

As already mentioned, there are currently only two active Crowdfunding platforms in Luxembourg, both are foreign-based. Local platforms that have emerged on the Luxembourg market could not sustain due to the small size of the market and to the regulation of the financial sector in Luxembourg and have therefore disappeared rapidly.

### 4.1 Applicable law

The Luxembourg law on the financial sector applies to any natural person established in Luxembourg for professional reasons or any legal person governed by Luxembourg law whose regular occupation or business is to exercise an activity of the financial sector and will therefore be subject to the prior approval of the CSSF. The CSSF focuses on the existence of the central administration in Luxembourg and of the registered office of the institution or professional of the financial sector that applies for an authorisation. As regards the professional of the financial sector who is a natural person, he must provide the evidence that he effectively conducts business in Luxembourg and has his central administration in Luxembourg. A natural person may therefore reside in a foreign country and have the authorisation of the CSSF as a professional of the financial sector in Luxembourg as long as his financial activity is performed in Luxembourg and has that his central administration is in Luxembourg.

Besides the central administration, the CSSF focuses on the infrastructure of the applicants. Both credit institutions and professionals of the financial sector must also provide evidence of robust internal governance arrangements including a clear organisational structure with well defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks they are or might be exposed to, and adequate internal control mechanisms, including sound administrative and accounting procedures, as well as control and security arrangements for information processing systems.

A second aspect related to the companies / projects that offer their transferable securities to the public in exchange for the funds invested has to be taken into consideration. Should there be an offer of securities made to the public within the territory of Luxembourg and even if it is not a regulated activity of the financial sector, the law on prospectuses for securities dated 10 July 2005 may apply.

## 4.2 Inbound

In this situation, a foreign Crowdfunding platform addresses Luxembourg investors (see below in subsection 4.2.1) or wants to present Luxembourg companies / projects on its platform (see below in subsection 4.2.2). The law on the financial sector does not differ between the different financial activities i.e. addressing the Luxembourg investors or promoting Luxembourg companies / projects on its platform. As a general rule, it will only be subject to the CSSF's supervisory if the financial activity is effectively exercised in Luxembourg and has its central administration in Luxembourg. If this is not the case, the applicable law will depend on whether the platform benefits from an European Union (EU) licence in another Member State or not.

### 4.2.1 Crowdfunding platform from another EU country addresses investors in Luxembourg

Luxembourg regulatory law can apply to:

- the Crowdfunding platform (licence requirements mainly); and/or
- the company /project seeking funding (prospectus requirements mainly)

#### 4.2.1.1 Licence requirements

In Luxembourg, the Markets in Financial Instruments Directive of 2004 (MiFID) was implemented through amendments made in the law on the financial sector dated 1993. As a general rule, a foreign platform holding a licence for its activity granted by the relevant authority in the origin Member State does not need an authorisation of the host Member State (Luxembourg) to exercise its business activity in Luxembourg to the extent it can take advantage of the EU Passport. In this case, the procedure is light and the simple notification to the CSSF (through the authority in the origin Member State) will be sufficient. The Crowdfunding platform may, in principle, exercise its activity in Luxembourg and benefit from the EU passport for the activities provided in Section A of Annex II (and for the annex activities listed in section C of Annex II) in the law on the financial sector as long as the activity exercised is covered by the licence from the origin Member State.

However, if it is a non-EU Crowdfunding platform that wishes to exercise its activity in Luxembourg or if a Crowdfunding platform would not be able to take advantage of the EU-Passport, it must, as a principle, apply for a licence from the CSSF.

#### **4.2.1.2 Other regulation**

Depending if the Crowdfunding platform would be qualified as an AIF, it would fall within the scope of the AIFM law and would therefore have to comply with the conditions of the AIFMD and relevant national law having implemented the AIFMD.

#### **4.2.1.3 Prospectus requirements**

As mentioned above, generally any offer of (transferable) securities to the public within the territory of Luxembourg requires a prior publication of a prospectus. Therefore, a (Luxembourg or foreign) company offering its securities to Luxembourg investors will in principle have to provide a prospectus, except the offer of securities falls under the exemptions mentioned in subsection 3.2. in the Law on prospectuses for securities.

### **4.2.2 Crowdfunding platform from another EU country addresses companies / projects in Luxembourg**

#### **4.2.2.1 Licence requirements**

If the Crowdfunding platform has a licence from another Member State to exercise its investment activity, and in general, provided the activity is defined in the law on the financial sector in Annex II, section A (and for auxiliary activities in section C), it will not need an authorisation of the CSSF to exercise his activity but will benefit from the EU passporting.

#### **4.2.2.2 Prospectus requirements**

If the company / project in Luxembourg offers its securities also to Luxembourg investors, it will have to provide a prospectus. If it does not offer its securities in Luxembourg but only to investors in others EU or non-EU States, there are no prospectus requirements to be fulfilled in Luxembourg.

## **4.3 Outbound**

In this situation, a Crowdfunding platform that is established in Luxembourg would enter a European Market and would address foreign investors (4.3.1) or companies / projects (4.3.2).

### **4.3.1 Crowdfunding platform from Luxembourg addresses investors in another EU country**

#### **4.3.1.1 Licence requirements**

As mentioned before, there is no local Crowdfunding platform on the Luxembourg market yet.

However, theoretically a Crowdfunding platform established in Luxembourg that would already exercise its activity in Luxembourg and would have needed to obtain a licence from the CSSF to do so, that wishes to carry on business within the territory of another Member State, could benefit from the EU passporting if the activity is EU-passportable. Pursuant to the law on the financial sector the platform would only need to notify to the CSSF the activities which it wished to exercise in the other EU country.

Within one month of this notification, the CSSF forwards the information to the competent authority in the host Member State.

#### **4.3.1.2 Other regulation**

In the case the Crowdfunding platform would be qualified as a Luxembourg AIF, it could fall within the scope of the AIFM law and would therefore have to comply with the conditions of the AIFMD and relevant national provisions.

#### **4.3.1.3 Prospectus requirements**

If the Crowdfunding platform established in Luxembourg addresses only investors in other Member States and does not offer any securities to the Luxembourg public, there are in principle no prospectus requirements to be fulfilled in Luxembourg.

### **4.3.2 Crowdfunding platform from Luxembourg addresses companies / projects in another EU country**

#### **4.3.2.1 Licence requirements**

In the case a Luxembourg Crowdfunding platform approaches Luxembourg investors and presents foreign companies on its platform, it could need a licence for its activity of the financial sector.

In the case a Luxembourg Crowdfunding platform needs to expand its activity within the territory of another Member State in order to be able to address these foreign companies (either by way of establishment of a branch in the host Member State or simply by providing services in this Member State), it would benefit from the EU passporting and would pursuant to the law on the financial sector need to notify to the CSSF the activities which it wished to exercise in the other EU country.

Unless the CSSF has a reason to doubt the adequacy of the administrative structure or the financial situation of the applicant, taking into account the activities envisaged the CSSF would, within three months communicate that information to the competent authority of the host Member State and inform the applicant accordingly.

On receipt of a notice from the competent authority of the host Member State, or failing such notice from the latter at the latest after two months from the date of transmission of the communication by the CSSF, the branch may be established and start business in the host Member State.

#### **4.3.2.2 Prospectus requirements**

If the Luxembourg Crowdfunding platform approaches Luxembourg investors and offers securities from companies / projects of other EU country on its platform, it could need to publish a prospectus on the securities of these companies (to the extent no exemption could apply). If the Luxembourg Crowdfunding platform only offers these securities to foreign markets, there are no prospectus requirements to be fulfilled in Luxembourg.

## 4.4 Impact of EU Regulation

### 4.4.1 Prospectus rules

The Luxembourg law on prospectuses for securities dated 10 July 2005 transposed the European Directive 2003/71/EC and provides for a prospectus regime related to the public offering of securities. Companies / projects that would offer equity or bonds to Luxembourg investors through a Crowdfunding platform (based on the Equity or the Lending model, if the latter operates through bond issuance) could be affected by this prospectus regime.

### 4.4.2 AIFM Directive

The Luxembourg law on alternative investment fund managers dated 12 July 2013 transposed the European Directive 2011/61/EU and provides for a regime for the authorisation, ongoing operation and the requirements of transparency of AIFMs established in Luxembourg which manage and/or market AIFs in the European Union.

This AIFM Directive would in principle mainly affect Equity-based Crowdfunding platforms. If the CSSF would consider that the platform meets the criteria of an AIF, the AIFMD would be applicable.

### 4.4.3 MiFID / MiFID II

In Luxembourg, the Directive 2004/39/EC on markets in financial instruments was implemented in national law via the law dated 13 July 2007. In addition to transposing the directive, the law also introduced five new categories of professionals of the financial sector (“PFS” as defined in the law of 5 April 1993, as amended). These new categories are financial intermediation companies, investment firms operating a Multilateral Trading Facility in Luxembourg, operators of a regulated market authorised in Luxembourg, Primary IT System operators, Secondary IT systems and communication networks operators. The Directive 2004/39/EC and the Regulation on Markets in Financial Instruments, commonly referred to as MIFID II, revising MiFID rules that will be applied at the latest January 2018, addresses the development of new trading platforms and activities.

The MIFID, ensuring a high degree of harmonised protection for investors in transferable securities could affect mainly Crowdfunding platforms based on the Equity or the Lending Model.

### 4.4.4 PSD / PSD II

The Directive 2007/64/EC on payment services was implemented by the payment services law dated 10 November 2009. The Payment Service Directive II that entered into force in 2016 must be implemented until January 2018. The Luxembourg law would apply to the Crowdfunding platforms if there are transfers of funds from the investor to the company / project funded. Generally, Crowdfunding platforms use intermediaries, operators that render these services. Any transfer of funds through an intermediary would in general be qualified

as money remittance or a payment transaction within the meaning of the law dated 10 November 2009 and could therefore be impacted by such Directives.

#### 4.5 Summary

From a Luxembourg perspective, the following barriers hinder the cross-border activities of Crowdfunding platforms:

- cost-benefit considerations i.e. the size of the Luxembourg market vs. the cost of entering the market (regulatory, mainly licensing costs and operational costs);
- prospectus regulatory considerations: as soon as transferable securities are offered to the public in Luxembourg, there is an obligation to publish a prospectus (and to effect the payment related thereto);
- foreign companies / projects may be subject to different prospectus requirements in their home country and in Luxembourg;

### 5 Lessons learned from Luxembourg regulation for a possible harmonised European Crowdfunding regulation

Since the Crowdfunding market in Luxembourg is rather at its very beginning and there are no local platforms that could serve as examples, there are, for the time being, no specific lessons that could be learned from the Luxembourg practice and adopted by other countries yet. So far, the Crowdfunding has not been recognized as a new category of investment that would need to be covered by a specific Luxembourg regulation and until now, Crowdfunding platforms could be impacted by licence requirements. The Luxembourg legislator rather awaits the impulses coming from the European Union to develop a specific regulation. However, the signals towards Crowdfunding are positive with the entry of two foreign-based platform that have offered companies / projects based in Luxembourg the possibility to benefit from the advantages of this new kind of investment.

### 6 Conclusion

Although welcome according to the CSSF, Crowdfunding has yet to establish itself in Luxembourg due especially to possible licence requirements. Neither the legislator nor the financial authority has given any indications as to how Crowdfunding will be organised on the field or what laws and regulations will be applicable. It has to be noted that the CSSF ensures the respect of applicable laws which might potentially apply to the Crowdfunding platforms. Nevertheless, it has to be kept in mind that the CSSF, generally speaking, is very flexible and will probably deal in a pro-active way with prospective Crowdfunding platforms on a case-by-case basis.

It may also not be ruled out that, should Crowdfunding become a popular and wide-spread tool, the Luxembourg legislator would be keen to put in place an attractive legislation in this respect, especially with a growing start-up community in Luxembourg.

## 7 Summary – Crowdfunding regulation

| Country   | <b>Luxembourg</b>  |
|---|--|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Currently two crowd-funding platforms are active in Luxembourg, one is based on the Equity model (also offering real estate projects) and the other based on the Donations or Rewards model.</li> <li>• There is no platform specialised in renewable energy or real estate solely.</li> <li>• Compared to other countries Luxembourg's Crowdfunding market is in the testing phase.</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>                            |  |
| <b>General regulation</b>   | <ul style="list-style-type: none"> <li>• Licence requirement under the law on the financial sector dated April 1993, as amended in particular if the platform is considered being an investment adviser, a broker in financial instruments, a commission agent, an investment firm operating a Multilateral Trading Facility in Luxembourg or a financial intermediation firm if it comes to investing (Equity Model) or considered as a credit institution or possibly a professional carrying out lending activities (Lending Model)</li> <li>• Licence under the law on financial markets dated 12 July 2007 in particular if the platform is being considered as a Multilateral Trading Facility.</li> </ul>   |
| <b>Prospectus requirements</b>  | <p>Prospectus requirement for offers of securities to the public and admission of trading of securities on a regulated market</p> <p>Exceptions:</p> <ol style="list-style-type: none"> <li>a) an offer of securities addressed solely to qualified investors; and/or</li> <li>b) an offer of securities addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors; and/or</li> <li>c) an offer of securities addressed to investors who acquire securities for at least the total amount laid down in Article 3(2)(c) of Directive 2003/71/EC and in the delegated acts adopted in accordance with Article 24a of this Directive, per investor, for each separate offer; and/or</li> <li>d) an offer of securities whose denomination per unit amounts to at least the amount laid down in Article 3(2)(d) of Directive 2003/71/EC and in the delegated acts adopted in accordance with Article 24a of this Directive; and/or</li> <li>e) an offer of securities with a total consideration in all Member States of less than the amount laid down in Article 3(2)(e) of Directive 2003/71/EC and in the delegated acts adopted in</li> </ol> |

|                                      |  |
|--------------------------------------|--|
|                                      | accordance with Article 24a of this Directive. Such limit shall be calculated over a period of 12 months.  |
| <b>AIFMD-regulation</b>              | If the Crowdfunding platform would be considered as an AIF, the AIFMD could apply and licencing requirements thereof would have to be complied with. Depending on the form of the Model and the investments, exceptions or derogations might apply   |
| <b>Payment service regulation</b>    | <ul style="list-style-type: none"> <li>• The Crowdfunding platform may fall within the scope of the PSD. The envisaged services may constitute either (i) money remittance (in the event that no account is being created in the name of the payer or the payee) or (ii) payment transaction, which implies an existence of a payment account, at least, in the recipient's side.</li> <li>• In the event that the crowd-funding does fall within the scope of the PSD, potential exemption methods would have to be addressed on a case-by-case basis.</li> </ul>   |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Amended law on undertakings for collective investment dated 17 December 2010;</li> <li>• Amended law relating to the investment company in risk capital ("SICAR") dated 15 June 2004;</li> <li>• Anti-money laundering law dated 12 November 2004, as amended;</li> <li>• Law regulating the access to the occupations of craftsman, tradesman, industrialist and certain liberal professions dated 2 September 2011.</li> </ul>  |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p>The law on the financial sector does not differ between the different financial activities i.e. addressing the Luxembourg investors or promoting Luxembourg companies / projects on its platform (main criteria: activity and central administration in Luxembourg).</p> <p><b>Foreign Crowdfunding platforms address Luxembourg Investors</b></p> <ul style="list-style-type: none"> <li>• <i>Licence requirements:</i> As a general rule, foreign platforms holding a licence for activity granted by the relevant authority in the origin Member State do not need authorisation in Luxembourg (if can take advantage of the EU Passport)</li> <li>• <i>A non-EU Crowdfunding:</i> platform wishing to exercise its activity in Luxembourg or if a crowd-funding platform not able to take advantage of the EU-Passport must apply for a licence from the CSSF.</li> <li>• <i>Prospectus requirements:</i> A Luxembourg or foreign company offering its securities to Luxembourg investors as a general rule have to provide a prospectus, except the offer of securities falls under the exemptions mentioned</li> </ul> <p><b>Foreign Crowdfunding platform addresses companies / projects in Luxembourg</b></p> |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>• <i>Licence requirements:</i> If Crowdfunding platforms have a licence from another Member State to exercise their investment activity, no authorisation of the CSSF is needed (EU passporting).</li> <li>• <i>Prospectus requirements:</i> If the company / project offers its securities to Luxembourg investors, it will have to provide a prospectus. If it offers its securities only to investors in others EU or non-EU States, no prospectus requirements in Luxembourg.</li> </ul>  |
| <b>Outbound</b>                | <p><b>Luxembourg Crowdfunding platforms address foreign investors</b></p> <ul style="list-style-type: none"> <li>• <i>Licence requirements:</i> Luxembourg Crowdfunding platforms that wish to carry on business within the territory of an-other Member State could benefit from the EU passporting</li> <li>• <i>Prospectus requirements:</i> If Luxembourg Crowdfunding platforms address only foreign investors, there are in principle no prospectus requirements to be fulfilled in Luxembourg</li> </ul> <p><b>Luxembourg Crowdfunding platforms address foreign companies / projects</b></p> <ul style="list-style-type: none"> <li>• <i>Licence requirements:</i> if Luxembourg Crowdfunding platforms approach Luxembourg investors and present foreign companies on their platform, could need a licence for their activity of the financial sector, but could benefit from EU Passporting</li> <li>• <i>On receipt of a notice</i> from the competent authority of the host Member State, or failing such notice from the latter at the latest after two months from the date of transmission of the communication by the CSSF, the branch may be established and start business in the host Member State.</li> <li>• <i>Prospectus requirements:</i> if Luxembourg Crowdfunding platforms approach Luxembourg investors and offer securities from companies / projects of other EU country on their platform (to the extent no exemption could apply).</li> <li>• If Luxembourg Crowdfunding platforms only offer securities to foreign markets, there are no prospectus requirements to be fulfilled in Luxembourg.</li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | Companies / projects that would offer equity or bonds to Luxembourg investors through a Crowdfunding platform (based on the Equity or the Lending model, if the latter operates through bond issuance) could be affected by this prospectus regime   |
| <b>AIFM-Directive</b>          | Crowdfunding platforms that would meet the criteria of an AIF would be impacted by this Directive (mainly Equity based platforms)  |
| <b>MiFID / MiFID II</b>        | MIFID and MiFID II (addressing the development of new trading platforms and activities) could affect mainly Crowdfunding platforms based on the Equity or the Lending Model  |

|                     |   |
|---------------------|---|
| <b>PSD / PSD II</b> | Any transfer of funds (from investors to companies / projects) through an intermediary would in general be qualified as money remittance or a payment transaction within the meaning of the law dated 10 November 2009 and could therefore be impacted by such Directives |
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# Malta

## 1 Recent developments in the market of Crowdfunding in Malta

The importance and feasibility of Crowdfunding platforms is increasing in stature and importance for current and future the entrepreneurs. Malta has recently acceded to the rising trend by creating its first Crowdfunding platform, *ZAAR*, a reward-based Crowdfunding platform which has recently been awarded with the first prize in its section at the National Enterprise Support Awards 2016 also as well as being one of the local projects that have represented Malta at the European Enterprise Promotion Awards 2016, held in Slovakia.<sup>1</sup> Nonetheless start-ups based in Malta with global aspirations often rely on international platforms. An increase in interest has emerged amongst the art and culture community as well in social entrepreneurship projects. Crowdfunding in Malta is still at the early stages of development. Despite this, there are endless opportunities for local entrepreneurs and the local business community. Research has shown that through international Crowdfunding platforms, monies have been raised for projects in the field of gaming consoles, apps and software as well as for artistic projects. Testimony to this is a new game design studio in Malta, that launched its first game, “Politicks”, raised financing through the Crowdfunding platform *Indiegogo*.

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

The Malta Competition and Consumer Affairs Authority estimates that Malta’s SMEs represent the larger part of the Maltese Economy accounting for the 99.8% of the enterprises. Though Maltese SMEs have limited access to traditional sources of funds, equity Crowdfunding (also known as investment-based Crowdfunding) has a great potential to help and sustain the SME sector.

As a result, the equity model has attracted the interest of the Malta Financial Services Authority (the “MFSA” or “Authority”) that has recently issued a consultation paper to establish its position regarding equity based Crowdfunding.

Equity Crowdfunding platforms perform the investment activities of “reception and transmission of orders in relation with one or more instruments” and “execution of orders on behalf of other persons”<sup>2</sup>. The equity Crowdfunding platforms intermediate and execute orders in relation to “transferable securities”<sup>3</sup>.

In particular, equity Crowdfunding platforms intermediate the acquisition by investors of “shares in companies and other securities equivalent to shares in companies, partnerships or other entities, and depositary receipts in respect of shares”. Having regard of the fact that the

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<sup>1</sup> <http://www.grantthornton.com.mt/press/news/zaar-malta-Crowdfunding-platform>.

<sup>2</sup> First Schedule of the Investment Service Act, 1994.

<sup>3</sup> Second Schedule of the Investment Services Act, 1994.

equity Crowdfunding platforms are deemed to provide an “Investment Service” in relation to an “Instrument”, such platforms will fall within the realm of the Investment Services Act, 1994<sup>4</sup> (“ISA”) requiring the authorisation of such businesses as investment service providers by the MFSA. For comparison purposes, the equity Crowdfunding business is analogous with a securities brokerage business which intermediates private equity transactions, with the key common factors being the Fintech element (the reliance on technology, dominantly the internet), and the tendency to focus on smaller, retail investors. The general framework of equity Crowdfunding also raises some concerns to the MFSA especially due to the likelihood that unsophisticated / inexperienced investors will be the bulk of the investors subscribing to projects seeking funding. A lack of understanding could be detrimental to the market as it may give the sector a poor reputation.

There is yet an insufficient pool of Crowdfunding platforms to arrive at reasonable assumptions on which factors that could be helpful to determine the success or the failure of an investment-based Crowdfunding platform. In this moment in time there are no equity based Crowdfunding platforms in Malta, albeit progress in this area is expected to take place following the setting of ZAAR.

### **1.2 Lending model (individuals lend money to a company or project in return for a repayment of the loan and interest on their investment)**

The Crowdfunding Lending model is used to raise funds for a project in the form of a loan agreement, with a promise to repay with (or in certain cases without) interest. Certain platforms may also use institutional money or their own balance sheet to finance such loans.

Although peer-to-peer lending (“P2PL”) and loan-based Crowdfunding (which might be considered as a spin-off from the P2PL) could potentially present legal implications under the Financial Institutions Act, 1994, Chapter 376 of the Laws of Malta (“FIA”) and the ISA, there are no direct references in this respect. This is mainly because these laws were drafted before the existence of P2PL and Crowdfunding, and therefore such laws are yet to be brought in line with the new realities.

### **1.3 Donations and Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward).**

The donations model is a particular form of Crowdfunding whereby, people supporting a project do not receive any financial return, whilst with the rewards model there is a certain element of expected return in the form of either a reward, service or product. Unlike investment-based Crowdfunding this form implies lower regulatory risks, and for this reason it has not been addressed by the regulator.

In Malta, the local Crowdfunding platform *ZAAR* follows this model, where *ZAAR* is a modification of the word ‘*zaghhar*’ in Maltese meaning ‘small change’ whereby the underlying

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<sup>4</sup> Chapter 370 of the Laws of Malta.

concept is that prospective investors that believe in a project will contribute to donate to the idea that they believe in.<sup>5</sup> The aforementioned platform takes an all-or-nothing approach to the fundraising, whereby it is envisaged that all donations are to be refunded in case the project does not meet its pre-defined funding objectives.

#### 1.4 Real estate Crowdfunding / Renewables Crowdfunding

Renewable energy plays a crucial role in reducing emissions as well as other forms of pollution. Malta together with the other European Union Member States have agreed on legally binding national targets for increasing the share of renewable energy, so to achieve a twenty per cent (20%) share for the entire Union by 2020. Malta has committed to reach a renewable energy share target of ten per cent (10%).<sup>6</sup>

The European Directive 2009/28/EC also requires Member States to publish a National Renewable Energy Action Plan explaining how such target will be achieved. Malta's main aim is therefore to incentivize and facilitate the renewable energy industry. Large wind farms, micro wind turbines, larger solar farms and other commercial initiatives are all potentially capable of absorbing the above-mentioned target. So far, this sector has been largely dependent on EU funded subsidy schemes with the downside that whilst these funds are not unlimited the market tends to be dependent on the availability of such funding.

Hence, the existing targets which Malta has committed to achieve within the Horizon 2020, as well as the local guidelines being published by Governmental Authorities, highlights the need and the appetite for alternative sources of funding being complementary to the above-mentioned ones. Unfortunately, at this stage Malta does not have a platform or platforms which address real-estate crowd-funding. Also at present, Malta does not have any on-going Renewable Energy Sources Projects ("RES Projects") which are being funded via a Crowdfunding platform financing model. The current RES Projects in Malta are being financed through private methods, most of them being partially financed by governmental subsidies as well as the Horizon 2020 schemes. The majority of renewal energy within Malta is produced through photovoltaic solar panels, and on-going projects are primarily focused on this energy resource. The Malta Environment and Planning Authority ("MEPA") has issued a solar farm policy in November 2014, encouraging RES Projects in abandoned quarries and large industrial rooftops, highlighting the local need for such projects.<sup>7</sup>

#### 1.5 International approach

Start-ups based in Malta with global growth objectives are the ones typically involved in seeking funds through Crowdfunding platforms or Venture Capital Investments ("VC"). Such companies are usually present in another market as a result of their organisational structure.

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<sup>5</sup> <http://www.zaar.com.mt/>

<sup>6</sup> <http://www.timesofmalta.com/articles/view/20160212/local/malta-still-doing-poorly-on-renewable-energy>

<sup>7</sup> <https://www.mepa.org.mt/file.aspx?f=11943>

Local players who have successfully managed to get funds have mainly used international platforms. For instance, we can refer to the Crowdfunding campaign of “Mighty Box” that has successfully raised monies on the Crowdfunding platform *Kickstarter*.<sup>8</sup>

These examples indicate that the absence of local platforms is not necessarily a hindrance to pursue Crowdfunding campaigns. However, since Crowdfunding (at least within the EU) is not yet harmonized, the level of effort and cost which one would need to enter into and access the European market with just one platform will be extensive, since the platform would need to ensure that it is adhering to the requirements of not just its host Member State but of another twenty-seven (27) other Member States.

## 2 Recent developments regarding Crowdfunding regulation in Malta

The MFSA, the single regulator for financial services in Malta, has issued a discussion paper in November 2016 regarding investment-based Crowdfunding, whereby it is proposing to create a legislative framework addressing the area of Crowdfunding. The Authority is currently assessing whether Crowdfunding should be regulated by the Authority and if yes, what will be the effects of regulating Crowdfunding. The MFSA is consulting the industry in general and is requesting feedback on such consultation document before deciding whether to go forward with the proposal for a legal framework on investment-based Crowdfunding.

The MFSA discussion paper entered into the merits of some of the key risks which may arise under investment-based Crowdfunding, such as loss of capital, lack of liquidity, fraud and platform. It also looked at what is happening at EU level and it highlighted the European Securities Markets Authority (“ESMA”) concerns in its published advice<sup>9</sup> and opinion<sup>10</sup> of December, 2014, which provided some clarity to national competent authorities. The MFSA reported that ESMA identified the fact that Crowdfunding platforms fall outside the existing regulatory parameters which is thus hindering their growth within the EU. Nonetheless, the MFSA discussion paper noted a Commission Working Document<sup>11</sup> which ruled out any EU intervention in the near future given that Crowdfunding is predominantly local in nature.

The discussion paper noted that the MFSA is minded to regulate Crowdfunding by applying the general securities framework which regulates investment services licence holders with the addition of ad-hoc investment protection measures. The MFSA is minded to capture equity-based Crowdfunding platforms under a Category 1A Investment Services Licence which would therefore capture such entity as a platform operator which would fall within the scope of the Markets in Financial Instruments<sup>12</sup> Directive (MiFID). A Category 1A investment services provider will require fifty thousand euros (€50,000) as a minimum capital

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<sup>8</sup> <http://www.timesofmalta.com/articles/view/20150329/local/Crowdfunding-appeal-for-new-board-game-hit-target-in-just-12-hours.561762>

<sup>9</sup> ESMA/2014/1560

<sup>10</sup> ESMA/2014/1378

<sup>11</sup> Commission Staff Working Document on “Crowdfunding in the EU Capital Markets Union” – 3rd May, 2016

<sup>12</sup> Directive 2004/39/EC

requirement and can provide “*reception and transmission of orders, investment advice and also place investment instruments without a firm commitment.*”<sup>13</sup>

In its discussion paper the MFSA identified the transmission and reception of orders as the service most likely to be provided by investment-based Crowdfunding. The Authority also disclosed that it is “*currently considering whether to restrict the Category 1A licence when provided to investment-based Crowdfunding platforms in order to restrict the platforms’ activity to reception and transmission of orders and placing without a firm commitment only. In general, platforms do not market themselves as providing personalised recommendations on investments. Some platforms operating in the EU are required by their regulator to provide investment advice. The Authority is of the view that platforms should restrict their involvement in the investments to customer due diligence checks and the investors should be encouraged to make their own well informed investment choices.*”

The MFSA is also of the opinion that investment-based Crowdfunding should be available to both public and private companies and that platforms may be exempt from the Prospectus Directive<sup>14</sup> if such platforms satisfy one of the exemption or the limitation of scope within such Directive as more clearly explained in section 3.2 below.

The discussion paper also identified the type of financial instruments (securities) which investment-based Crowdfunding will use, these being shares and mini-bonds.<sup>15</sup> The Authority identified that it is also minded to interpret the term ‘transferable security’ as identified in MiFID and the Prospectus Directive in a broad manner and that in only limited instances it will deem securities to be non-transferable. The MFSA also noted that since there is no or limited secondary market for securities offered through online Crowdfunding it is its opinion that such platforms will avoid any form of regulation. The discussion paper also touches upon conduct of business requirements, anti-money laundering legislation as well as other investment protection measures such as the possibility of:

- A. capping the maximum amount which can be invested by each investor;
- B. capping the maximum project size;
- C. requirements for platforms to undertake a minimum level of due diligence on the projects / project owners and to take measures to reduce the risk of fraud; and
- D. specific disclosure requirements tailored to Crowdfunding.

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<sup>13</sup> www.mfsa.com.mt

<sup>14</sup> Directive 2003/71/EC

<sup>15</sup> A mini-bond is a type of debt security, typically issued by small businesses. Mini-bonds run for around three to five years, in general, and offer an interest rate of between 6% and 8% a year. They are becoming increasingly popular with investors, attracted by the interest rates on offer, however, they are illiquid and can be high risk, as the failure rate of small businesses is high.

### 3 Current Regulation of Crowdfunding in Malta

#### 3.1 Licence under the Investment Services Act or the Financial Institution Act

##### 3.1.1 Equity model

Currently, there is no regulatory framework which specifically regulates Crowdfunding. However, the Authority is considering setting up a local framework for the regulation of investment based Crowdfunding, whereby both corporate issuers and platform operators need to be limited liability companies formed and registered in Malta pursuant to the Companies Act. The approach being considered by the Authority is to apply the regulatory framework applicable to Investment Services Licence Holders, with the addition of some tailored measures to better implement investor protection measures.

Since in the view of the Authority the Crowdfunding platform will undertake licensable activities the main legislative documents worth mentioning are the ISA, the Companies Act (“CA”)<sup>16</sup> and the Financial Institutions Act (“FIA”)<sup>17</sup>.

The approach chosen by the Authority is to apply the general securities regulatory framework. The platform would need to obtain an investment services licence in terms of the Investment Services Act and have both its head office and registered office in Malta. It appears that the platform operator would fall within the scope of the Markets in Financial Instruments Directive (“MiFID”) with the benefit of a passport to carry on the services/activities for which it is authorized throughout the EU without any additional authorization being required.

In terms of the ISA, a licensable activity takes place when an investment service listed in the First Schedule of the act is offered in respect to an instrument listed in the Second Schedule.

As mentioned above, the Authority identified, among the four possible categories of investment service licence, the Category 1A as the licence which would be most suitable for Crowdfunding platforms. This is the least onerous since it requires a minimum capital of fifty thousand euros (EUR 50,000). The Authority has identified the activity most likely to be provided by the Crowdfunding platform as the “*reception and transmission of orders*” since the main activity undertaken by the platform is to receive orders from investors to subscribe for instruments and transmit them to the issuer or another third-party intermediary for the execution. The Authority also identified that some platforms might also wish to undertake the marketing for project owners, carrying out the service of placing without a firm commitment<sup>18</sup>.

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<sup>16</sup> Chapter 386 of the Laws of Malta

<sup>17</sup> Chapter 376 of the Laws of Malta

<sup>18</sup> A firm commitment is defined as an underwriting whereby a company is committed to buy and sell an entire issue of stock and assumes all the financial responsibility for any unsold share

The Authority is currently evaluating the hypothesis of restricting the Category 1A licence when given to investment-based Crowdfunding platforms to restrict its activities to reception and transmission of orders and placing without a firm commitment.

Many investment-based Crowdfunding platforms operating within the European Union avoid regulation, as they use non-transferrable securities. However, the MFSA is minded to interpret this term in a broader way and only in a few circumstances securities are considered not to be transferrable. Thus, since shares, bonds and other securities are listed under “transferable securities” under the Second Schedule of the ISA, this would mean that regulation will apply.

Investment-based Crowdfunding platforms may be subject to license conditions applicable to investment service license holders. Consequentially, a range of conduct of business requirements shall be enforced on investment Crowdfunding platforms. Therefore, should the MFSA deem it necessary to enforce regulation, the platform may be required to provide appropriate information to allow potential investors to be in a position to make and take an informed investment decision. Additionally, an appropriateness assessment of the financial instrument released by the issuer should be undertaken unless a number of conditions are satisfied. Amongst them, one such condition is that the investment service relates to non-complex financial instruments. Financial instruments listed as non-complex include shares admitted to trading on a regulated market, bonds and other securitised debt, excluding those containing derivatives. Bonds and other debt securities are relevant in the context of Crowdfunding, however those shares which are not normally quoted on a regulated market shall require an appropriateness assessment.

In this regard, derivatives and other instruments involving leverage are meant to be complex. Other instruments should be considered non-complex if:

- there are frequent opportunities to dispose or realise the instrument at publicly available market prices; and
- adequate and comprehensive information are available concerning its features allowing the retail investors to make an informed investment choice based on the information gathered.

Since the Crowdfunding market is characterised by the lack of a secondary market, therefore having limited possibilities to dispose of the investment, such instruments may be considered as complex. Accordingly, potential investors may also be subject to an appropriateness test to better assess their knowledge and experience in investing in such ‘instrument’. However, at this stage this is all speculation since the Authority still needs to take a stance on how and whether Crowdfunding platforms will be regulated. Although an indication was given that the MFSA is considering regulating the business of Crowdfunding, the purpose of its discussion paper was to ask the industry to provide its thoughts and thus, the industry may to a certain degree be able to influence the Authority’s line of action.

### 3.1.2 Donations or Reward Model

The donations or rewards model is not regulated in Malta and at this stage the MFSA has not indicated whether it will consider reviewing this model and possibly also include it under a regulatory framework. At this point in time Malta has a reward based Crowdfunding platform called ZAAP<sup>19</sup> however it is not regulated by any regulatory body in Malta and, one cannot exclude possible regulatory intervention in the future.

## 3.2 Prospectus requirements

### 3.2.1 Equity model

The MFSA is of the view that a Crowdfunding platform can be set up both as private or public companies.

In respect of public companies, Article 89 to the CA requires the issuance of a prospectus whenever there is an offer of transferable securities to the public in a European Member State. Therefore, in accordance with the Prospectus Directive the prospectus must be published unless one of the exemptions mentioned in the Prospectus Directive itself are triggered.

For instance, some offers of securities are exempt from the prospectus requirements such as:

- where the total consideration of the securities for the offer within the European Union and the EEA does not exceed five million euros (€5,000,000), which limit shall be calculated over a period of twelve (12) months; or
- of securities made only to qualified investors<sup>20</sup>; or
- to less than one hundred-fifty (150) persons per Member State.<sup>21</sup>

As far as a private company is concerned, Article 209 to the CA identifies a private company as one which:

- has the right to transfer the shares is restricted;
- has the number of its members is limited to fifty (50);
- prohibits the public to subscribe for any shares or debentures of the company.

As a result of the above, the MFSA has not yet indicated whether a full prospectus will be required in accordance with the Prospectus Directive or whether there will be any derogations or lesser requirements or exemptions for any particular industry. In fact in its discussion paper the MFSA asked the industry two key questions. The first question being “*which exemptions from the prospectus requirement are most relevant to crowd funded offers?*” and the

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<sup>19</sup> Its website states in its website that “Project owners owe their donors a high standard of effort, honest communication, and a dedication to bringing the project to life” thus showing that some form of onus is being placed on the project owners.

<sup>20</sup> A qualified investor is a person or entity that can deal with securities not registered with financial authorities by satisfying one of the requirements regarding income, net worth, governance status or professional experience.

<sup>21</sup> Article 2(3)(b) of the Companies Act

second question being “do you agree with the interpretation that crowd-funded offers are likely to fall outside the scope of the Prospectus Directive?”

### 3.2.2 Donations or Reward Model

As already stated above, the donations or reward model is not regulated in Malta. Having said that one cannot state with absolute certainty whether a prospectus will be required unless clarify if provided and an exemption to this model is given. Malta’s reward model Crowdfunding platform in its website does include a brief of the different type of projects including the objective of the project – however this is a far cry from a fully-fledged prospectus.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

The transposition of the Alternative Investments Funds Manager Directive<sup>22</sup> (“AIFMD”) in Malta has been implemented through the amendment of the ISA and its subsidiary legislation. Platforms which are seen to collectivise investments and fall within the regulatory definition of a collective investment scheme (“CIS”) might also fall within the scope of the AIFMD regime.

The act defines a CIS as:

*“as means any scheme or arrangement which has as its object or as one of its objects the collective investment of capital acquired by means of an offer of units for subscription, sale or exchange and which has the following characteristics:*

- A. the scheme or arrangement operates according to the principle of risk spreading; and either*
- B. (b) the contributions of the participants and the profits or income out of which payments are to be made to them are pooled; or*
- C. (c) at the request of the holders, units are or are to be re-purchased or redeemed out of the assets of the scheme or arrangement, continuously or in blocks at short intervals; or*
- D. (d) units are, or have been, or will be issued continuously or in blocks at short intervals:*

*Provided that an alternative investment fund that is not promoted to retail investors and that does not have the characteristic listed in paragraph (a) hereof shall only be deemed to be a collective investment scheme if the scheme, in specific circumstances as established by regulations under this Act, is exempt from such requirement and satisfies any conditions that may be prescribed.”*

According to ESMA, the AIFMD should not apply to investment-based Crowdfunding platforms operating in line with their current business models. Typically, a platform which offers opportunities for investments in particular projects do so through the use of specific vehicles dedicated to that particular project which allows investors to choose the project they wish to invest in. In the event that a platform was to offer investors access to a collective

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<sup>22</sup> Directive 2011/61/EU

investment undertaking which is not considered as an Undertaking for Collective Investment in Transferable Securities (“UCITS”) then it would be likely that the investment vehicle would be classified as an Alternative Investment Fund.

However, the AIFMD contains a number of exemptions that might be applicable to investment-based Crowdfunding platforms such as companies operating outside the financial sector (i.e. companies not following any investment policy) remit or holding companies or securitisation special purpose vehicles.

### **3.3.1 Equity model**

The Investment Services Rules which capture Alternative Investment Funds do provide for companies which would like to establish themselves in the form of a fund and which objective would be a particular project, such as real estate, vintage cars, forestry funds, renewable forms of energy. Consequently, the collective investment scheme objective would be to fund a particular project. Therefore, such projects could easily be captured by Malta’s adaptation of the AIFMD - meaning that a Crowdfunding platform following the equity model is potentially akin to a CIS especially if some form of return either in the form of dividends or capital appreciation is generated by a project on a platform which utilises the equity model.

### **3.3.2 Lending model**

In terms of Maltese legislation, a CIS may be established as a loan fund. The MFSA has taken as a basis the provisions of the AIFMD and also drew upon the Authority’s Banking Rules to address the specific areas of risk in a manner that ensures consistency with the Banking Act, while retaining the inherent characteristics of collective investment schemes established under the Investment Services Act.

The Authority addressed a number of risks associated with lending - such as risks to the stability of the funds. To mitigate the transmission or acquisition of unwarranted credit risk, loan funds are also required to follow strict credit assessment standards and fund managers must satisfy special competence and remuneration requirements. In order to reduce liquidity risks, loan funds must be closed-ended or at least make use of appropriate redemption gates. Other liquidity requirements also apply and leverage is not allowed.

Should the elements of a CIS as outlined above, be fulfilled, and the thresholds outlined by the AIFMD reached, the MFSA could be open to consider loan based crowd-funding as an arrangement falling within the scope of AIFMD. At this stage, this is mere speculation and one will need to better understand and engage with the Authority to understand its intended course of action.

### **3.3.3 Donations or Rewards Model**

This model does not seem to be captured by the AIFMD, since such model does not offer any form of financial return.

### 3.3.4 AIFMD concluding remarks

It can be argued that a Crowdfunding platform do not technically fall under the remit of the AIFMD since a Crowdfunding platform is not raising financing for its own use and that it is not managing the funds which have been raised. Therefore, the Crowdfunding platform would not be captured as an AIF or an Alternative Investment Fund Manager. Nonetheless the establishment of certain types of fund platforms in Malta are regulated to a lesser extent. In terms of Legal Notice 119 of 2012 – The Companies Act (Recognised Incorporated Cell Companies) Regulations, the Maltese legislator created a set of requirements for the establishment of a RICC company and its incorporated cells. A RICC may only provide services of an administrative nature for which it is issued with a Recognition Certificate in terms of Article 9A of the ISA. Unlike other structures, the RICC structure provides promoters with a flexible ICC structure that may be used as a vehicle to achieve various objectives including the setting up of a fund platform. A RICC must be established as a limited liability company and may not carry out any licensable activity. The RICC requires a memorandum of association restricted to the provision of administrative services to its incorporated cells. By analogy the Crowdfunding platform may be similar to a RICC and the underlying projects are the equivalent of an Incorporated Cell under the RICC, which Incorporated Cell is a CIS with separate legal personality.

### 3.4 Regulation under the Payment Services Directive

In the past, few years Malta has become a European hub for payment service providers given the favourable legal environment provided to these entities as well as the possibility of passporting such services throughout Europe.

One of the main issues that can arise from the development of the Crowdfunding platform is whether a lender who regularly lends to borrowers in Malta through a platform could be considered to be undertaking a licensable activity in terms of relevant laws and regulations.

In this context, it is relevant to note that although the platform acts as an intermediary between the lender and the borrower it is not part of the contractual arrangement between the parties.

The Crowdfunding Lending model is used to raise funds for a project in the form of a loan agreement, with a promise to repay with (or in certain cases without) interest. Certain platforms may also use institutional money or their own balance sheet to finance such loans.

Although peer-to-peer lending (“P2PL”) and loan-based Crowdfunding (which might be considered as a spin-off of the P2PL) could potentially present legal implications under the FIA and the ISA there are no direct references in this respect. This is mainly due to the fact that these laws were drafted before the existence of P2PL and Crowdfunding, and therefore such laws are yet to be brought in line with the new realities.

Unlike investment-based Crowdfunding to date there is no formal position taken by the MFSA on this subject. However, since Crowdfunding will increase in prominence and gain

market share as time goes by, it is possible to predict that the MFSA will look at whether such Crowdfunding platforms will also be caught under the Authority's regulatory framework.

In the event that it does, we are of the understanding that such type of Crowdfunding may be captured by the FIA. The Second Schedule of the FIA provides the list of activities to be undertaken by a licensed Financial Institution in Malta, among which there is lending, money remittance and electronic money.

However, a Crowdfunding platform has "borderline" features since it does not perfectly fit in any of the above listed activities.

The Crowdfunding lending platform does not typically lend money directly, since it is acting as an intermediary between the lender and borrower, thus holding itself out from being a party within the lending agreement. Therefore, the platform serves to provide a framework to:

- increase the visibility of the projects;
- enabling interaction with the two parties;
- provide the support documentation to allow parties to reach the investment agreement as well as facilitating the contractual terms and conditions;
- coordinate and monitor the effective fulfilment of the contractual obligations.

A Crowdfunding lending operation with a collective investment element may fall within the remit of the ISA. Based on the regulatory rules it is possible for CIS to be established as loan funds.

"Investment through loans" generally means that the:

- loans are directly originated by the Scheme; and
- Scheme would then acquire a portfolio of loans or direct interest in loans which would give rise to a direct legal relationship between the Scheme and the projects, as respectively lender and borrower.

One still needs to determine whether the Authority will consider such activity to be a licensable activity or not. In the meantime, operators of Crowdfunding platforms may take into consideration the possibility of co-operating with either banks or similar financial institutions providing payment services to avoid being caught on the wrong end of the regulatory stick, should the MFSA consider that the platform is undertaking a licensable activity.

### 3.5 Possible additional Regulations

- Prevention of Money Laundering Act (“PMLA”);<sup>23</sup>
- Prevention of Money Laundering and Funding of Terrorism Regulations (“PMLFTR”);<sup>24</sup>
- Distance Selling (Retail Financial Services) Regulations;<sup>25</sup>

The MFSA is also proposing the introduction of several other investment protection measures apart from the authorisation and conduct of business requirements applicable to investment service providers as explained in the last paragraph to section 2 above.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable Law

The European Commission is monitoring on an ongoing basis the development of investment-based and lending - based Crowdfunding. Nowadays the development of Crowdfunding activity occurs within the countries’ borders and is not so common to find platforms able to operate on a cross-border basis. The implementation of European directives across Member States differs from one Member State to another and thus creates various bespoke regimes providing different guidelines and principles. The lack of harmonisation concerning consumer or investor protection can be seen as the main barrier for a cross-border Crowdfunding development. As a consequence, this may lead to the platform’s refusal to provide their services to non-residents and new markets might be targeted only through the establishment of Crowdfunding platforms in the various member states, which could become cumbersome and not cost-effective.

Other potential barriers to the international development of Crowdfunding platforms include:

- definitions of Crowdfunding and the scope of activities for investment-based models;
- different conditions for authorisation (for example capital requirements);
- business requirements (i.e. professional qualifications, information and risk warnings, due diligence, conflict of interests, investment limits, etc.).<sup>26</sup>

This will inevitably affect the cross-border strategies of the Crowdfunding organisation as they might need to develop different platforms or sustain important web development work. Moreover, they might seek approvals, licenses, or authorizations from different regulatory authorities, undermining the cost-effectiveness of such cross-border activity.

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<sup>23</sup> Chapter 373 of the Laws of Malta.

<sup>24</sup> Subsidiary Legislation 373.01 to Chapter 373 of the Laws of Malta.

<sup>25</sup> Subsidiary Legislation 330.07 to Chapter 330 of the Laws of Malta.

<sup>26</sup> [https://ec.europa.eu/info/sites/info/files/170227-report-capital-barriers\\_en.pdf](https://ec.europa.eu/info/sites/info/files/170227-report-capital-barriers_en.pdf)

The lack of harmonisation between countries, also qualified as “fragmentation”, may be a decisive barrier for the international implementation of the Crowdfunding practice. Although, the industry can grow within the country’s borders, it cannot easily cross borders, thus affecting the size and scalability of their campaigns as well as of the platforms themselves.

The problems regarding the regulatory framework differ for each type of Crowdfunding, with loan-based and investment-based being the most constrained. The European Commission, states that thirty-eight per cent (38%) of platforms offering financial returns are active in cross border transactions whereas nearly fifty per cent (50%) of them want to extend their operations in other countries. The same considerations and observations related to the regulatory barriers could be easily transposed to the field of taxation.

It is a common feature that many bespoke regimes require a certain level of local substance when it comes to licensable activities. For instance, the MFSA requires a licenced entity to have at least three (3) directors, one of which would need to be based in Malta and fulfil the role of a non-executive director. Even though such requirements might not pose specific problems for large banks and insurance companies, their suitability is doubtful and they can negatively impact smaller financial service providers. Whilst the residence requirements are justified for the purposes of easier oversight and supervision, ensuring effective management and prevention of fraud, the European Commission invites Member States to remove residence requirements on managers of companies in the financial sector where they are not justified, suitable or proportionate.

Moreover, the latest Capital Markets Union (“CMU”) Communication<sup>27</sup>, stressed out the negative impact that the differences and inefficiencies in national insolvency regimes have on cross-border investment and lending.

Although the differences in national insolvency regimes are not comparable to those applicable to Crowdfunding platforms, the sense of the basic situation may be also fructified for Crowdfunding platforms, especially in their cross-border activities. The negative effects of the different national insolvency regimes could lead to a decrease of trust and confidence from the potential investors that might be afraid of a non-consistent legislative framework.

Whilst the above has given a flavour of how Europe is looking at the matter, Malta still needs to formalise its position and therefore one cannot say what the requirements for Crowdfunding platforms are and which laws will apply.

## 4.2 Inbound

The question is if the Crowdfunding platform addresses Maltese investors or wants to promote Maltese companies/projects on its platform

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<sup>27</sup> Please refer to the Commission Communication of 14 September 2016: Capital Markets Union — accelerating reform ([http://ec.europa.eu/finance/capital-markets-union/docs/20160913-cmu-accelerating-reform\\_en.pdf](http://ec.europa.eu/finance/capital-markets-union/docs/20160913-cmu-accelerating-reform_en.pdf)).

#### 4.2.1 Foreign Crowdfunding platform addresses Maltese investors / companies

Currently there is no legislation or regulation which captures Crowdfunding activity. The MFSA, through its discussion paper, has kick-started the debate on the potential regulatory requirements which could apply, such as licensing requirements, conduct of business requirements, compliance and risk management implications. Furthermore, current Maltese legislation may apply for companies seeking funding for projects which would therefore require adherence to the preparation of a prospectus as well as fiduciary obligations.

As mentioned above the MFSA still need to position itself on Crowdfunding and therefore one cannot say whether foreign Crowdfunding platforms address the needs of Maltese investors.

##### 4.2.1.1 Crowdfunding platform

There appears the need to have more clarity from the European institutions in respect of Crowdfunding platforms. Should a platform hold a MiFID (or MiFID II) licence as being envisaged by the MFSA for local Crowdfunding platforms, Crowdfunding platforms could reach a larger market and pool of investors thanks to the ability to take advantage of passporting and market the platform in the various EU territories. Therefore, in theory an EU based Crowdfunding platform which holds a MiFID licence can passport into Malta.

On the other hand, if the Crowdfunding platform does not hold a MiFID licence, one would need to understand whether such platform would be subject to any regulatory requirements at a local level over and above existing laws such as anti-money laundering legislation.

##### 4.2.1.2 Company/project

Most EU legislation on financial services, including MIFID and the Prospectus Directive only apply where the financial instruments are transferable securities. However, as far as investment-based Crowdfunding is concerned, as previously mentioned the MFSA interprets the term transferable securities in a broad way, so it is likely that since most of the financial instrument are deemed to be transferable securities a prospectus shall be provided.

Furthermore, in the view of investor protection, a key information document related to the project seeking funds could be considered useful. In particular, this key document shall contain:

- Audited annual account summary (if any);
- Statement of the strengths (technology, patents) and weaknesses/threats (competition/obsolescence);
- Short biography of the founders, the board members and the senior management;
- Current capital structure and dilution due to fundraising;
- Commercial information about the product/service.

## 4.3 Outbound

### 4.3.1 Crowdfunding platform

In this situation, what is being described is the possibility of having a Maltese Crowdfunding platform entering a foreign market, thus addressing foreign investors.

Based on the assumption that the platform might undertake licensable activities passporting rights shall be addressed to the licenced platform. Therefore, we can differentiate between freedom to provide services on a remote basis or setting up a branch.

In the first case the notification to the overseas the Authority shall be accompanied by:

- information relating to the services intends to provide together with a programme of operations also indicating whether it intends to operate through tied agents;
- an indication of the Member States that will be targeted.

Moreover, in case the platform would hypothetically opt for the setting up of a branch it would therefore need to provide a notice accompanied by:

- An indication of the Member States within the territory of which the platform plan to establish a branch;
- A programme of operations identifying the operations it seeks to carry out through the branch also indicating whether there is an envisaged use of tied agents;
- The address of the proposed branch;
- The proposed organisation structure of the branch.

### 4.3.2 Maltese Crowdfunding platform addressing foreign (EU) investors

The debate on Crowdfunding platforms in Malta is still in its infancy from a regulatory and legal perspective. The MFSA discussion paper has started to address and encourage debate in this area and as mentioned above the MFSA is looking to regulate and require that a MiFID licence would be required for equity based Crowdfunding platforms.

## 4.4 Impact of EU Regulation

### 4.4.1 Prospectus regulation

In Malta, only prospectuses under the Prospectus Directive are harmonised as well as the definition of transferable securities under MiFID. As a result of this one can say that a negligible amount of any potential Maltese Crowdfunding market is overseen by harmonised EU legislation and implemented into Maltese law due to the current stance by the EU institutions of allowing Crowdfunding to be the competence of national regulators.

### 4.4.2 AIFMD

Malta has fully transposed the AIFMD and the possible impact of this directive is described in the above sections. One would also need to assess the MFSA's views on whether

the AIFMD would or could have an impact of equity based and lending based Crowdfunding. To date there is no formal position by the Authority.

#### 4.4.3 MiFID

Since the MFSA position within its discussion paper is to implement and apply a MiFID licence to Crowdfunding, Maltese based Crowdfunding platforms may be impacted by MiFID and eventually MiFID II. The purpose of a MiFID licence will be not only to regulate the Crowdfunding platform but also to be able to benefit from the passport.

#### 4.4.4 PSD / PSD II

The requirement of the Payment Services Directive<sup>28</sup> has been transposed into Maltese legislation under the Financial Institutions Act as amended from time to time. The FIA captures not only payments but also money remittance, an activity which could potentially be captured by the FIA in respect of Crowdfunding platforms since they receive the monies of subscribers to a project and then pass on such monies to the project owners. As mentioned earlier, it may be prudent for Crowdfunding platforms to enter into a co-operation agreement with either a credit institution or licenced payment institution rather than acting as intermediary between the project owner and the investor.

### 4.5 Summary

The way that Crowdfunding is developing from a legislative and regulatory perspective, leading to different interpretations and across a number of different EU member states (as well as non-EU member states), it is very likely that the establishment of a pan-European or global Crowdfunding platform will be very cumbersome, costly and potentially ineffective. Rather than having the EU leading the way and developing a harmonised product within the single market, the exact opposite is taking place. Whilst from a Maltese perspective, the debate is still open, other regulators are implementing their own legislative frameworks. The cross-border facility offered by a passport currently does not apply and either foreign or Maltese Crowdfunding platforms may face barriers of trade, since a licence in one jurisdiction may not be sufficient for other jurisdictions.

## 5 Lesson learned from Malta's for a possible harmonised European Crowdfunding regulation

### 5.1 Role model (“dos”)

The MFSA's discussion paper on Investment-based Crowdfunding is a positive signal that the Authority is of the view to recognize Crowdfunding as an economic instrument that might imply licensable activities. Thus, the MFSA is giving Crowdfunding more visibility as a reliable alternative source of financing for newly created SMEs.

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<sup>28</sup> 2007/64/EC

For a possible harmonised European Crowdfunding market the following aspects can serve as a role model:

- a lighter touch regime for Crowdfunding platforms in relation to existing financing models and/or products;
- appropriateness assessment for non-professional investors;
- transparency and reliability of the information provided to the investors
- Continuity plan in the view of investors protection – including capping of investments for non-sophisticated investors

## 5.2 Aspects that should be avoided (“dont’s”)

The wait and see approach by the EU in respect of Crowdfunding, should not be used as a means of seeing different legislative frameworks across the EU and then piecing them together to form an EU directive. The reason being that each regulator would be looking at different aspects of their own legislative framework and the hurdle to bring about a common front on such a matter may take time, energy and effort which could be utilised and invested in a better manner. Having said that any future harmonised Crowdfunding legislation should not allow for over-regulation, excessive bureaucracy and lack of transparency.

## 6 Conclusion

Nowadays, we are witnessing an extensive growth of Crowdfunding both in terms of popularity and in the term of effective use. It is currently considered as an important source of alternative finance for projects that would have otherwise experienced difficulties using traditional sources. Small businesses play a central role in the European economy as well as in the Maltese one, where small and medium enterprises account for more than ninety per cent (90%) of the overall economy. The Entrepreneurship Action Plan for 2020 invites Member States to “*assess the need of amending current financial legislation with the aim of facilitating new, alternative forms of financing for start-ups and SMEs in general, in particular as regards platforms for Crowdfunding*”. Its increasing importance is demonstrated also by the interest shown by the Maltese regulator, willing to create a defined legislative framework following the inputs given by the industry players.

As every novelty, Crowdfunding raises particular concerns under several points of view in particular on the investor protection side:

Some of the key risks pertaining to Crowdfunding are outlined below:

- A. Loss of capital: platforms will mostly be used by start-up and SME’s that might not have an established track record, therefore the failure rate is exponentially increased. These risks will be even higher for non-expert/professional investors;
- B. Lack of liquidity: there is no secondary market that allows one to trade the securities acquired through Crowdfunding, therefore investors may face the risk of

not having the possibility of selling their securities or, alternatively, they might be sold at a significant discount;

- C. Fraud: since fundraising is carried out via online platforms, there will be not personal contact between lenders and borrowers, as there is no intermediary acting in between. There might be also limited information of the projects being funded. Hence, the risk of fraud is significantly increased;
  
- D. Platform closure or failure: in the event of a temporary or permanent shut down of a Crowdfunding platform that handles clients' monies, investors may face losses unless safeguards are put in place.

Despite the increasing growth which Crowdfunding as a mode of financing is experiencing, it still remains mostly a domestic trend. The real challenge will come up when, or if, Crowdfunding will mature into a well-defined international phenomenon. At that point, European regulators will then have to reconcile and harmonize different national rules, without adding new layers of regulation that may threaten and stymie growth. Having a second regulatory regime to comply with would create a cost burden for platforms wishing to expand their business outside their national borders. The European Commission recently stated that it would prefer to see the Crowdfunding blossom before proposing to create a unique legislative framework preferring national regulators to take the lead at the early stages, despite some divergences.

Hence, given the fast-growing rate Crowdfunding is experiencing and its extraordinary value (yet not totally unleashed), the continuous and effective monitoring of the degree of harmonization of the national regimes shall be considered extremely important.

Notwithstanding the last provision, whilst the establishment a single regulatory licence is still relatively far away, it is envisaged that some sort of pan-European framework will be likely to be created.

## 7 Summary – Crowdfunding Regulation

| Country   | Malta  |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | MFSA's consultation paper on investment-based Crowdfunding   |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | If investment-based Crowdfunding contributors opt for the purchase of financial instruments, therefore the intermediary role played by the Crowdfunding platform may be considered to be an investment service. The investment service activity most likely to be provided is “the reception and transmission of orders without firm commitment” that would fall under the Category 1A of the investment services licence.   |
| <b>Prospectus requirement</b>                         | If a Crowdfunding platform facilitates offering of shares in collective investment schemes, it may be considered as providing an investment service under the Investment Services Act. As a consequence, an Offering Memorandum may be required to be provided to investors.   |
| <b>AIFMD-regulation</b>                               | If a Crowdfunding platform facilitates offering of securities, or shares in a collective investment scheme, it may be considered as providing an investment service under the Investment Services Act.<br><br>An MFSA authorisation may be required.   |
| <b>Payment service regulation</b>                     | If a Crowdfunding platform, acts as an intermediary between the parties involved in the transaction even from payment service point of view it may be considered as a payment service provider.<br><br>An MFSA authorisation may be required.  |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Prevention of Money Laundering Act (“PMLA”);</li> <li>• Prevention of Money Laundering and Funding of Terrorism Regulations (“PMLFTR”);</li> <li>• Distance Selling (Retail Financial Services) Regulations.</li> </ul>   |
| <b>Regulatory barriers</b>                            |  |
| <b>Inbound</b>  | There appears the need to have more clarity from the European institutions in respect of Crowdfunding platforms. Should a platform hold a MiFID (or MiFID II) licence as being envisaged by the MFSA for local Crowdfunding platforms, Crowdfunding platforms could reach a larger market and pool of investors thanks to the ability to take advantage of the passport and market the platform in the various EU territories. Therefore, in theory an EU based Crowdfunding platform which holds a MiFID licence can passport into Malta. |
| <b>Outbound</b>                                       | Based on the assumption that the platform might undertake licensable activities passporting rights shall be addressed to the licenced platform.  |

|                                |   |
|--------------------------------|---|
|                                | <p>Therefore, we can differentiate between freedom to provide services on a remote basis or setting up a branch.</p> <p>In the first case the notification to the overseas the Authority shall be accompanied by:</p> <ul style="list-style-type: none"> <li>• information relating to the services intends to provide together with a programme of operations also indicating whether it intends to operate through tied agents;</li> <li>• an indication of the Member States that will be targeted</li> </ul> <p>Moreover, in case the platform would hypothetically opt for the setting up of a branch it would therefore need provide a notice accompanied by:</p> <ul style="list-style-type: none"> <li>• An indication of the Member States within the territory of which the platform plan to establish a branch;</li> <li>• A programme of operations identifying the operations it seeks to carry out through the branch also indicating whether there is an envisaged use of tied agents;</li> <li>• The address of the proposed branch;</li> <li>• The proposed organisation structure of the branch.</li> </ul> |
| <b>Impact of EU regulation</b> |   |
| <b>Prospectus regulations</b>  | Due to the current lack of harmonisation a negligible amount of Crowdfunding market is likely to fall under the regulation of European law and subsequently transposed into the Maltese Law. Hence Crowdfunding would be more the competence of the national regulators.  |
| <b>AIFM-Directive</b>          | It is still to be understood whether Crowdfunding would be affected by the AIFMD at least from a Malta perspective since the MFSA is yet to provide the industry with its position.   |
| <b>MiFID / MiFID II</b>        | Since the view of the MFSA is to consider Crowdfunding as a potential licensable activity, it is likely that MIFID/ MIFID II will have an impact in this respect. These directives might apply for the licencing requirements as well as for pass-porting.  |
| <b>PSD / PSD II</b>            | <p>The requirements of the PSD have been transposed into the Maltese Financial Institutions Act (“FIA”). The FIA captures not only the payment service activities but also the activity of money remittance which could be seen as an activity that might be potentially undertaken by the Crowdfunding platform, therefore the PSD directive shall be taken into consideration.</p> <p>However, as previously stated it might be advisable for Crowdfunding platforms to set up partnerships with already existing credit/payment institutions rather than acting as a mere intermediary between the project owner and the investors.</p>  |

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# Netherlands

## 1 Recent developments in the market of Crowdfunding in Netherlands

The following significant developments could be noted in Netherlands with regards to Crowdfunding:

A total of 4800 projects with a value of EUR 170 million have been funded in 2016 via different forms of Crowdfunding in the Netherlands, which is an increase of 33% in comparison to the amount funded in 2015.<sup>1</sup>

As per 1 April 2016, the Netherlands Authority for the Financial Markets (*Autoriteit Financiële Markten*, the **AFM**) doubled the investment limits applying to loan based and equity based Crowdfunding platforms to EUR 40.000 (equity based) and EUR 80.000 (loan based), respectively. The investment limits apply to any retail investor investing through a Crowdfunding platform supervised by the AFM. Furthermore, loan based and equity based Crowdfunding platforms are required to conduct an investor test in order to assess whether the investment can be considered sound (*verantwoord*) for this particular retail investor. These investor tests need to be developed by the platforms themselves and must assist the investor to determine whether (s)he has sufficient knowledge, experience and a sound financial position to make the investment.

Investors are also required to take additional (limited) investment tests for each additional EUR 5.000 invested on the Crowdfunding platform. In relation thereto, the AFM has indicated that an investor should not invest more than 10% of its investable assets via Crowdfunding platforms.

The Crowdfunding platform is required to notify the investor of the outcome in an objective manner (and, if the outcome is negative), the platform must emphasize the risks involved by means of an explicit warning. The outcome of the test is not binding for the retail investor, nor is the Crowdfunding platform required to prevent the retail investor from investing in the relevant project or on its platform in general in case of a negative outcome.

In relation to the increase of the investment limits set out above, the AFM has started a research on the effectiveness of these limits. It has published a report in November 2016 on the first results of the national survey amongst investors on the effects of the new rules. The report is part of a bigger evaluation of the regulations that apply to Crowdfunding platforms with the aim to improve the effectiveness of the supervision of the Crowdfunding industry and the regulations that apply to the Crowdfunding industry.

The first results of the evaluation show that about 40% of the respondents consider the risks of participating in a Crowdfunding project lower than the risks associated with investing

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<sup>1</sup> All numbers in this paragraph are based on a report made available by Douw&Koren, Crowdfunding in Nederland 2016, de status van Crowdfunding in Nederland, dated 2 January 2017, available at (<http://www.douwenkoren.nl/kopie-van-download-rapport-cf-voor->).

in securities or investment funds (*beleggingsinstellingen*). Furthermore, 40% to 50% of the respondents invest more than 10% of its entire capital, which is more than what the AFM considers safe.

### **1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)**

Equity Crowdfunding via investments in (certificates of) shares (*certificaten van aandelen*) represents a low percentage of 3.3% of the total amount funded via Crowdfunding in the Netherlands. Certificates of shares are regularly issued to investors as an alternative to shares. The main advantages are twofold. Firstly, the company will have the option to hold shareholders' meetings without being required to invite the crowdfunders at these meetings as they are being represented by one or more representatives instead. Secondly, it is not necessary to involve a civil-law notary in order to issue and transfer certificates of shares, which would be a requirement if regular shares are used.

#### **Convertible subordinated loan**

An alternative investment form offered by a few Crowdfunding platforms is the convertible subordinated loan (also known as convertibles), which is a subordinated loan that can be converted into (certificates of) shares after certain conditions have been met. The conditions that apply before these convertibles can be converted may vary and are agreed upon issuance. The crowdfunders will be paid the agreed interest rate on the subordinated loans if the conditions for the conversion have not been met within the agreed time frame. These products are more regularly offered than regular (certificates of) shares. Around 6% of the projects funded via Crowdfunding in the Netherlands are convertible subordinated loans.

In a nutshell, the Dutch equity Crowdfunding market to date only represents a limited value compared to the overall Crowdfunding market in Netherlands.

### **1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

Since the beginning of Crowdfunding in the Netherlands, the lending model is, by far, the most popular option to fund projects. A percentage of 76% of all projects funded via Crowdfunding in the Netherlands made use of the lending model, varying from annuities to bullet loans. The biggest Dutch P2P lending platform alone has – according to the company's own information – mediated in an amount of more than 106 million euro since its incorporation.

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

In the Netherlands the donations or rewards models are used predominantly to finance social or creative projects or companies (e.g. NGOs). Here, no financial investment or return

is involved. Investors fund projects or companies and get no return at all or a non-monetary reward (e.g. tickets, products etc.). In some cases the rewards are of a symbolic value only.

#### 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

Irrespective of the aforementioned categories, there is a trend in Netherlands to facilitate Crowdfunding to finance real estate and renewable projects. The value of these categories is still fairly low in comparison to the total value of funded projects in the Netherlands. There are a few Crowdfunding platforms that specialise in these kinds of projects, but most projects are still financed via generic platforms that provide the option to finance these projects.

Renewable Crowdfunding is also rather popular in the Netherlands. In 2016, more than EUR 10 million has been financed via Crowdfunding in renewable energy. The majority related to the funding of solar power (more than EUR 6 million). In comparison to the EUR 61.000 funded in 2011, this clearly shows a large potential. To give an idea of the variety of options: even a hydro-electric power station was financed via Crowdfunding.<sup>2</sup>

Most of the renewable projects use more than one source of funding. Therefore, almost every renewable project is (still) partly financed via traditional bank loans. An increasing number of renewable projects use Crowdfunding as part of its finance structure – benefiting from the lower costs connected with funding over the crowd compared to the conditions of bank loans.

#### 1.5 International approach

More and more US Crowdfunding platforms and platforms from other European countries (try to) enter the Dutch market and plan to establish international Crowdfunding platforms in order to reach (at least part of) the European market with just one platform. Due to the (increasing) differences in the national Crowdfunding regulations such projects require a lot of efforts and legal advice in the different jurisdictions.

## 2 Recent developments regarding Crowdfunding regulation in the Netherlands

### 2.1 New Crowdfunding framework

Following an ongoing dialogue with the Crowdfunding sector, the AFM has introduced a new Crowdfunding framework per 1 April 2016. The new Crowdfunding framework:

- Doubles the investment limits applying to loan based and equity based crowdfunding platforms to EUR 40.000 (equity based) and EUR 80.000 (loan based), respectively. The investment limits apply to any retail investor investing through a Crowdfunding platform supervised by the AFM.

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<sup>2</sup> <http://www.douwenkoren.nl/single-post/2016/11/04/Crowdfunding-voor-duurzame-energie-groeit-opnieuw>

- Requires loan based and equity based Crowdfunding platforms to conduct an investor test in order to assess whether the investment is sound (*verantwoord*) for this particular retail investor. These investor tests need to be developed by the platforms themselves and must assist the investor to determine whether (s)he has sufficient knowledge, experience and a sound financial position to make the investment. See further chapter 1 above.

This Crowdfunding framework is not part of the Dutch financial supervision laws which are mainly laid down in the Dutch Financial Supervision Act (*Wet op het financieel toezicht*, the **Wft**) and decrees promulgated thereunder. The AFM imposes the Crowdfunding framework by attaching administrative regulations as part of a license as investment firm under Directive 2004/39/EC (**MiFID**) firm or a dispensation to mediate in redeemable funds (loan based). However, some MiFID license holders that mediate in bonds and notes (as opposed to non-transferable loans) issued by borrowers have not been made subject to the Crowdfunding framework by means of administrative regulations connected to their license.

## 2.2 New dispensation regime

Dutch Crowdfunding platforms that operate a non-transferable loan platform (the majority) require a dispensation granted by the AFM under Article 4:3, Paragraph 4 of the *Wft* to act as intermediary in respect of repayable funds. The Dutch minister of Finance has strengthened this dispensation regime by an amending decree of 18 February 2016, which has come into effect on 1 April 2016. The amending decree introduces general standards regarding:

- The business conduct of the Crowdfunding platform;
- Integrity tests for the board or management of the Crowdfunding platform;
- Transparent governance structures of the Crowdfunding platform;
- Mandatory handling of complaints in respect of all stakeholders of the Crowdfunding platform (including lenders and borrowers).

These general standards for dispensation holders are applied to Crowdfunding platforms by connecting the new requirements to a new definition: 'Public loan' (*publiekslening*).

## 2.3 Dispensation for the Dutch ban on commissions

The above mentioned decree of 2016 further introduces a dispensation for the Dutch ban on receiving commissions by a platform that operates under a MiFID license. The general ban on commissions prohibits MiFID Crowdfunding platforms to receive compensation from borrowers (or other third parties). However, the compensation received from borrowers for a successful project is generally the main source of revenue for Crowdfunding platforms as is demonstrated by Crowdfunding platforms that do not qualify as an investment firm under MiFID. The Dutch minister of Finance has recognized this lack of a level playing field between investment firms and dispensation holders that act as Crowdfunding platform and has created a dispensation on the ban on commission for investment firms that operated as Crowdfunding platform.

### 3 Current Regulation of Crowdfunding in the Netherlands

Although no formal definition of Crowdfunding exists in the Netherlands,<sup>3</sup> the current Dutch regulatory framework for Crowdfunding can generally be split into the following three categories: (i) the equity model (ii) the lending model and (iii) the donations or rewards model. We will discuss these models below.

#### 3.1 Licensing requirements

When a Crowdfunding platform mediates between investors and businesses that issue financial instruments, such a company will be regarded as providing MiFID investment services under Article 2:96 Wft and require a license from the AFM as investment firm.

"Financial instruments" within the meaning of the Wft include:

- shares or similar transferable equity instruments or rights (*effecten*);
- non-security collective investment participation rights (*rechten van deeleneming, niet zijnde een effect*); and
- transferable bonds or similar negotiable debt instruments (*obligaties*).

In respect of MiFID services, these platforms will be considered as providing the investment service:

- "Reception and transmission of orders in relation to one or more financial instruments" as defined in Annex I of the MiFID under Section A.

However, the AFM may consider that the service provided is more close to:

- "Placing of financial instruments without a firm commitment basis" as defined in the same Annex I under Section A.

This latter requalification by the AFM is to make sure that a platform that structures its activities such to circumvent reception and transmission of orders to avoid requiring a MiFID license is still captured. For this reason, the AFM has treated certain platforms as placing platforms, triggering MiFID.

##### 3.1.1 Equity / Lending model

When a Crowdfunding platform mediates between investors and businesses that issue shares or certificates of shares, such a platform will be regarded as providing MiFID investment services under Article 2:96 Wft and require a license from the AFM as investment firm.

To determine whether the platform is involved in issuing shares or certificates of shares, the definition of 'transferable securities' as defined in article 4 of the MiFID as implemented in article 1:1 of the Wft is followed. In this context of shares and certificates of shares, transferable securities are defined in Wft as:

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<sup>3</sup> Other than the in April 2016 introduced term 'public loan' (see paragraph 2.1.1).

- A. a share or similar transferable equity instrument or right, or
- B. any other negotiable instrument issued by a legal entity, company or institution which entitles the holder of it to a security as described under (i) upon such instrument being exercised or converted or which instrument can be settled in funds.

In the AFM policy rule on transferability<sup>4</sup> the AFM binds itself to a very broad interpretation of transferability to include any method that allows for a legal or economical transfer of a share, a certificate of a share or the rights connected to a share or instrument. This means in practice that irrespective of a limitation on transferability by contract or by a company's articles of association (*statuten*), a share or certificate of a share of a private or public Dutch limited company (*besloten vennootschap*) will be captured as transferable security.

The lending model includes Crowdfunding platforms that on the one hand provide services in respect of transferable bonds and notes issued by borrowers (MiFID regime) and on the other hand services in respect of non-transferable subordinated loans (convertible subordinated loans as discussed under paragraph 1) (dispensation regime).

### 3.1.2 Lending model under the MiFID regime

When a company acts as intermediary by bringing together investors and businesses that issue bonds or notes, such a platform will be regarded as an investment firm and require a license from the AFM for its Crowdfunding activities. Just as is the case under the equity model, these platform's will be considered as providing the investment service "Reception and transmission of orders in relation to one or more financial instruments" or "Placing of financial instruments without a firm commitment basis" as defined in Annex I of the MiFID under Section A (see paragraph **Fehler! Verweisquelle konnte nicht gefunden werden.**).

### 3.1.3 Bonds and notes

To determine if the platform is involved in issuing bonds or notes, the definition of 'transferable securities' as defined in article 4 of the MiFID as implemented in Dutch law is followed. In this context of bonds or notes, transferable securities are defined in Wft as:

- A. a negotiable bond or similar negotiable debt instrument, or
- B. any other negotiable instrument issued by a legal entity, company or institution which entitles the holder of it to a security as described under (i) upon such instrument being exercised or converted or which instrument can be settled in funds.

As stated above under the equity model, in the AFM binds itself under a policy rule to a very broad interpretation of transferability to include any method that allows for a legal or

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<sup>4</sup> <https://www.afm.nl/~/profmedia/files/wet-regelgeving/beleidsuitingen/beleidsregels/beleidsregel-verhandelbaarheid.ashx>

economical transfer of an instrument. However, other than with securities being shares or certificates of shares, the AFM in practice takes a slightly less stringent approach. For loan agreements that are not legally designed to be transferable, the AFM is likely to consider such loan agreements as not transferable (in which case the dispensation regime will apply, see paragraph 3.3). It also means that to qualify for a license as investment firm, a Crowdfunding platform must design the loan agreements it mediates in expressly as bonds or a notes.

#### **3.1.4 Increase in lending model investment firms**

In the past year, we have seen an increase in lending model Crowdfunding platforms getting authorized as investment firm. This may be due to the already discussed dispensation on taking commissions from borrows which dispensation in last year's report was still under constructio. Another likely reason is that it gives Crowdfunding platforms the ability to export their platform cross border on the basis of a passport available to MiFID license holders and not to dispensation regime platforms. A final reason is that the MiFID regime is more long standing and as such more ironed out than the patchwork Dutch Crowdfunding framework that is imposed largely on the basis of administrative regulations and decrees.

#### **3.1.5 License requirements equity model and lending model under the MiFID regime**

A Crowdfunding platform that acts as intermediary in the issuance of transferable securities such as shares or bonds will – in principle – be captured as investment firm under MiFID and as implemented in article 2:96 of the Wft.

Pursuant to Article 2:96 in the Wft, it is prohibited to provide investment services (*verlenen van beleggingsdiensten*) or to carry out investment activities (*verrichten van beleggingsactiviteiten*) without a MiFID license. Providing investment services is defined in Article 1:1 of the Wft and includes, among other things, the service of receiving and transmitting orders of clients in relation to one or more financial instruments in the pursuit of a profession or a business and the service of placement of financial instruments without a firm commitment when these are being offered by the issuer in accordance with the prospectus rules and regulations under the Wft.

- To meet the license requirements, a Crowdfunding platform must comply with various requirements as laid down in Article 2:99 of the Wft. These requirements include but are not limited to:
- An adequate policy ensuring a sound and prudent business conduct, including with respect to funds that may flow through it;
- That the daily policy makers (the board or management) meet the integrity and suitability tests of the AFM;
- That any supervisory board members or non-executive board members meet the integrity and suitability tests of the AFM;

- A declaration of no objection provided by the Dutch Central Bank (*De Nederlandsche Bank*, **DNB**) in respect of every entity or person with a qualified holding in the Crowdfunding platform.
- The minimum own funds requirement.

In our experience, obtaining a declaration of no objection from DNB and meeting the minimum own funds and solvability requirements can be challenging for platform. This also means that this sets the MiFID regime largely apart from the dispensation regime as discussed below under paragraph 3.3.2.

### 3.2 Prospectus requirements under the lending and equity model

A borrower that offers transferable securities (such as shares or bonds) to the public must take the prospectus rules into account. In practice, however, it is the Crowdfunding platform that typically provides that transferable securities documents or templates to be used by borrowers. This means that the Crowdfunding platform itself should be very aware of the prospectus regime.

Under Article 5:2 of the Wft an issuer (i.e. the borrower) that offers securities to crowdfunders in the Netherlands must publish an AFM approved prospectus. For the AFM to give approval, the prospectus must meet the requirements laid down in the Directive 2010/73/EC amending the Directive 2003/71/EC as implemented in the Wft, and Regulation no. 809/2004.

#### 3.2.1 Prospectus exemption

If a borrower engages a Crowdfunding platform to mediate in offering bonds, shares or other transferable securities to crowdfunders, the borrower in principle triggers the above mentioned prospectus obligation. However, for most borrowers that seek mediation by Crowdfunding platforms, an exemption to the prospectus obligation applies. At present, there is an exemption from the duty to publish an AFM approved prospectus for:

- Offering transferable securities to the public when the securities that are part of the offer in total stay below the monetary equivalent of EUR 2.5 million during a period of 12 months.

Moreover, this limit of EUR 2.5 million relates to a *category* of transferable securities. The borrowing issuer can, therefore, collect up to EUR 2.5 million in shares or certificates or shares *and* up to EUR 2.5 million in bonds or notes from the public in the Netherlands in the same year. However, any issuance of transferable securities by a borrower's group company must be taking into account, including issuances in other jurisdictions in the European Economic Area.

### 3.2.2 Information document

Irrespective an exemption to the prospectus obligation, the crowdfunders must be adequately informed. This means that there remains an information-document requirement, which document must include amongst other things:

- The characteristics of transferable securities; and
- The risks associated with the securities such that investors can make an informed decision.

### 3.2.3 Warning banner

Crowdfunding platforms that rely on an exemption to the prospectus obligation must display a warning banner on the part of their website that holds offers. The warning banner must also be printed on all offering documents including. The warning banner can be downloaded from the AFM website and holds the text: “Warning! You are investing outside AFM supervision. No prospectus obligation exists for this activity.”

## 3.3 Lending model – dispensation regime

If a platform is mediating by bringing together lenders and borrowers that attract a non-transferable loans, such platform requires a dispensation for mediating in attracting repayable funds from the AFM.

### 3.3.1 Non-transferable loans

Non-transferable loans are private subordinated loan contracts agreed between a crowdfunder and the borrower. As being private, the loan contracts are not considered transferable and thus do not qualify as a financial instrument (see paragraph 3.1.3).

#### 3.3.1.1 Convertible subordinated loan

An alternative investment form offered by a few Crowdfunding platforms is the convertible subordinated loan (also known as convertibles), which is a subordinated loan that can be converted into (certificates of) shares after certain conditions have been met. The conditions that apply before these convertibles can be converted may vary and are agreed upon issuance. Just as the above mention non-transferable loans, these convertibles can be drafted such that they are not considered to be transferable by the AFM. Also see paragraph 3.1.3 on the treatment of transferable loans by the AFM.

### 3.3.2 Dispensation regime requirements

As stated above under paragraph 2.1, as of 1 April 2016 the rules that apply for dispensation holders have been enhanced to more closely follow the typical regulatory requirements that apply to license holders. As such, the Crowdfunding framework that applies to dispensation holders now partly follows from the Wft and partly from decrees promulgated under the Wft in addition to AFM administrative regulations imposed on dispensation holders by an AFM administrative decision.

These rules are largely aimed at protecting the investors against investing in fraudulent or financially weak companies through Crowdfunding platforms without knowing the risks associated with such investments upfront. To that extent, the platforms must:

- Analyze the borrowers it places offers for on its website;
- Connect certain risk categories to the borrower's projects and match the risk with suitable interest rates; and
- Warn the investors in various ways of the risks associated with borrower projects.

This has to be done by the platform in such a way that the investor is able to make an informed investment decision based on the information provided by the platform.

In addition, investors that are consumers have the ability to unwind their investment decision during a 14 days period. Alternatively, a consumer investor must actively confirm its investment to the platform after it has initiated an investment through the website of the Crowdfunding platform.

Other regulatory requirements that apply to dispensation holders are the following:

- The daily policy makers (board and management) of the Crowdfunding platform must meet the suitability and integrity test of the AFM. The same applies to supervisors of the daily policy makers (such as non-executive board member or other supervisory council members. The test are largely the same as for investment firm license holders and are based on the criteria the AFM has bound itself to under the Policy Rule on Eligibility 2012 (*Beleidsregel Geschiktheid 2012*) of the AFM and DNB.
- The Crowdfunding platform must maintain transparent governance structures. This means that the Crowdfunding platform may not be connected to persons in a formal or factual control structure which is opaque to the extent that it constitutes or may hamper proper and adequate supervision by the AFM of the Crowdfunding platform.
- The platform must have a complaints procedure through which investors can effectively handle of complaints.
- The platform must have a business conduct policy that guarantees sound and controlled business conduct by the platform. This includes – amongst other things – safeguarding the investors' funds as described next and incident reporting to the AFM and incidents record keeping.
- The Crowdfunding platforms safeguard the funds that flow through it, even if the platform goes bankrupt. Platforms must use a foundation (*stichting*) that has the sole purpose to hold the investor's funds and to the extent applicable security packages connected to the loans. This segregates the investor's funds from the platform's estate in case of bankruptcy.

- The platform has to comply with certain monitoring obligations, allowing the AFM to track the platforms' activities.

These requirements that apply as of 1 April 2016 have brought the dispensation regime much closer to the MiFID regime. One of the aspects that sets the MiFID regime apart from the dispensation regime is the minimum own funds and solvability requirements that apply to investment firms.

### 3.4 Donations and Rewards Model

In principal, donations and reward based Crowdfunding is not regulated in the Netherlands by the AFM. Investors that support a project or company, against a (non-financial) consideration or reward is considered sponsorship or reward based Crowdfunding by the AFM.<sup>5</sup> Investors that donate funds whereby the investors do not receive a financial interest in return for their funds is considered charity by the AFM. So long as the financial aspect is for the investor is inferior to the project or aim pursued by the receiving party, acting as platform in between investors and receiving parties is not considered as regulated Crowdfunding. More legally speaking, the test is whether the investor becomes entitled a financial product or interest rate related payment.

#### 3.4.1 Tax

For donations, including donations via Crowdfunding, specific tax rules apply. For instance, donation tax for larger donations and limited tax benefits for donation purposes that hold a specific tax status such as Dutch PBO status holders, being organizations that focuses largely on public benefits.

### 3.5 Consumer credit

If a Crowdfunding platform mediates in offering credit to consumers, the platform in principle requires a license to provide consumer credit under Article 2:60 of the Wft. The definition of consumers in the Netherlands is reserved for people acting outside the course of occupation or business. This means that sole traders and other natural persons that acting in the course of occupation or business are not considered consumers. The fact that a platform itself does not originate the consumer credit funds is not relevant as the offering (as opposed to originating) is captured as the regulated activity under Article 1:1 of the Wft under the definition of offering (*aanbieden*).

Advice or mediation in respect of consumer credit is captured as the regulated activity of providing advice under Article 2:75 of the Wft or mediation in relation to financial products (i.e. consumer credit) under Article 2:80 of the Wft. Important regulatory requirements that apply to consumer credit license holders are regulations in respect of:

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<sup>5</sup> <https://www.afm.nl/nl-nl/professionals/onderwerpen/Crowdfunding-overig>

- Credit advertising requirements, including the warning banner with the text: “Attention! Borrowing money, costs money!” (“*Let op! Geld lenen kost geld*”).
- Information provision requirements;
- Preventing over indebtedness; and
- Content of the credit agreement.

The AFM is especially keen on preventing over indebtedness part of the code of conduct of the platform. In this context, the platform must obtain information on the consumer's financial position so that it can be judged whether the credit can be provided the relevant consumer.

### 3.6 Payment services directive

Transfer of funds through a Crowdfunding platform can constitutes money remittance services within the Article 1:1 of the Wft under payment services (*betaaldiensten*). Such regulated transfer of funds could occur if the investors pay their investment amounts to the operator of the Crowdfunding platform who then passes the funds to the company / project. However, DNB has so far showed a liberal interpretation of money remittance services. This is likely to change when PSD2 (the Revised Payment Service Directive) takes effect on 13 January 2018.

In order to avoid a licencing requirements the operator of a Crowdfunding platform could cooperate with a bank, a licenced payment institution or a licenced electronic money issuer for the handling of payments rather than acting as an intermediary itself.

#### 3.6.1 Mediating in payment services

Crowdfunding platforms that do contract with a bank, payment institution or electronic money issuer to handle the flow of funds between the investors and the borrowers may still trigger an authorization requirement to offer mediation services in respect of payment accounts or electronic money.

More specifically, this will be the case when investors open a payment account through mediation of a Crowdfunding platform or where investors take electronic money issued to them through mediation of a Crowdfunding platform. The Crowdfunding platform will be considered to mediate in this context if it provides more than the name, address, zip code, telephone number and e-mail address (**NAZTE**) of an investor to a payment institution or electronic money institution. For instance, when next to NAZTE information on the investment amount, payment account number or other information is provided by a Crowdfunding platform to an electronic money issuer of payment institution, the Crowdfunding platform will triggers authorization as financial services provider.

##### 3.6.1.1 Exemption for investment firms

A Crowdfunding platform does not require to license as a mediator in payment accounts or electronic money, if the platform is regulated as an investment firm. Holders of a license as an investment company are exempted from this.

### 3.6.2 E-wallets

A trend we see is that Crowdfunding platforms increasingly explore the use of e-wallets and associated apps. The e-wallets explored are envisaged to hold the investors' investments much like a securities account does for securities. Next to holding Crowdfunding investments, e-wallets are envisaged to hold investor funds (e.g. to receiving interest rate payments). These received funds can be stored as a balance in an e-wallet as electronic money, also allowing investors to reinvest those funds through an app associated with the e-wallet in further Crowdfunding projects.

### 3.7 Alternative investment funds – AIFMD regime

The Alternative Investment Fund Manager Directive (**AIFMD**) as implemented in the Wft regulates alternative investment funds (**AIFs**) managed by an alternative investment fund manager (**AIFM**).

The Wft provides that AIFs (*beleggingsintellingen*) include a collective investment undertaking which:

- raises capital from a number of investors,
- with a view to investing it in accordance with a defined investment policy for the benefit of those investors;
- is not an operating company conducting business outside the financial sector and
- does not require authorisation pursuant to Article 5 of Directive 2009/65/EC (UCITS).

#### 3.7.1 Operating company seeking funding

The AIFMD under the Wft does not apply to operating companies outside the financial sector which do not invest in accordance with a defined investment policy.

The AFM upholds the EMSA Guidelines on key concepts of the AIFMD, ESMA/2013/600 that clarify that clarifies that companies are operating companies if – briefly put:

- their business strategy is simply the commercial success of their business;
- they do not intend to follow any defined investment policy but want to finance their on-going day-to-day business; and
- they operate the facility, production or project themselves within their day-to-day business or make use of the service of an intra-group company or an external service provider (as long as the day-to-day discretion remains at the company)

In general, these requirements are met by the "typical" start-up or developing company seeking funding for its general commercial business by means of a Crowdfunding platform. Such companies should therefore fall outside the scope of the Dutch AIFMD regulations.

### 3.7.2 Project Company seeking funding

#### 3.7.2.1 Equity Model

However, certain companies (especially in the sectors real estate, infrastructure or renewables) could fall under the AIFMD regulations. For instance, project companies might constitute an AIF within the meaning of the Dutch AIFMD regulations if they seek funding in return for a share in the profits or revenue generated by the project as in the equity model and do not conduct operative activities (e.g. the operative activities are outsourced).

The AFM in the past year has challenged some initiatives that presented themselves as equity Crowdfunding to trigger AIFMD. This has resulted in the retreat of the initiatives as the Dutch AIFMD regime is much more stringent to comply with the Dutch MiFID regime and the exemptions provided under the Dutch AIFMD sub-threshold regime (offerings to less than 150 people, offerings with a total value of at least EUR 100,000 per investor or to professional investors) only is not suitable for typical Crowdfunding project.

#### 3.7.2.2 Lending Model

Investments by means of subordinated loans or other debt-based investments can generally be structured as non-AIF investments because the investors do not share liability for any losses (e.g. investors receive an fixed interest rate).

#### 3.7.3 Crowdfunding Platform

Due to the fact that an operator of a Crowdfunding platform does not raise capital from investors for its own business, it should not qualify as an AIF. Further, there are sound arguments to state that a typical Crowdfunding platform does not "manage" the underlying investment as an AIFM does, but merely arranges investments into projects or companies.

Hence, the operator of a Crowdfunding platform does not qualify as an AIF or an AIFM.

### 3.8 Taking repayable funds as borrower

As a final aspect under the Dutch Crowdfunding regulations, under both variants of the lending model (dispensation and MiFID-regime), the borrowers have to take into account the prohibition on attracting repayable funds of Article 3:5 of the Wft. Attracting deposits or other repayable funds is defined in the definition of a 'credit institution' in article 4 of the Capital Requirements Regulation, and the prohibition is laid down in Article 3:5 of the Wft. Deposits or other repayable funds, commonly jointly referred to as "repayable funds" are funds that must be repaid at a certain point in time, for any reason whatsoever, and of which it is clear in advance what nominal amount must be repaid. Examples include borrowing money and issuing bonds. More concrete, borrowers that take loans from the public using a Crowdfunding platform must stick to the following rules:

- The borrower takes the funds for its own account: With "for its own account" is – briefly put – meant that the borrower does not attract or obtains repayable funds with a view to granting credits or loans by the borrower acting as lender.

- The borrower does not act as a business in taken funds: the borrower does not attract repayable funds by acting as a business in attracting such funds. The borrower can act as a business if it attracts repayable funds on a regular basis and the attracting of repayable funds does not strictly serve the support of other principal activities of the borrower.

Briefly put: If the above conditions are met, a loan can be attracted by a borrower in the context of Crowdfunding, without breaching the prohibition on attracting repayable funds.

The prohibition of repayable funds does not apply under the equity model, because funds raised by issuing shares are not repayable, as shares do not entail the obligation to repay the nominal amount.

### 3.9 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- The Dutch Civil Code (*Burgerlijk Wetboek*);
- The Dutch Personal Data Protection Act (*Wet bescherming persoonsgegevens*);
- The Dutch Telecommunication Act (*Telecommunicatiewet*);
- The Dutch Consumer Credit Act (*Wet op het consumentenkrediet*); and
- The Dutch Money Laundering and Terrorist Financing (Prevention) Act g (*Wet ter voorkoming van witwassen en financiering van terrorisme*).

## 4 Regulatory barriers for Crowdfunding crossing borders

Although we see an increase in loan model investment firm Crowdfunding, currently still 48 out of the total of 57 Dutch Crowdfunding platforms are operating under the dispensation regime (see paragraph 3.3) by mediating only in non-transferable loans which. This means that for the vast majority of the Dutch Crowdfunding platforms a passport to cross borders with their platform is not available. Furthermore, the Prospectus Directive and the upcoming Prospectus Regulation are mostly for the Dutch Crowdfunding sector.

### 4.1 Applicable law

According to the Dutch<sup>6</sup> financial regulation applies in case Dutch investors are approached by (foreign) financial actors (such as issuers of financial instruments or mediators, etc.). In this regard the AFM follows a marketing focussed approach. This means that not only providers of financial services that have their registered office or ordinary residence in the Netherlands fall under Dutch regulatory law but also in case the financial actor targets the Dutch market in order to offer financial services to companies / persons in the Netherlands. Indicators for the AFM to assume that a financial actor targets the Dutch market are

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<sup>6</sup> See AFM policy rule 'Being active in the Netherlands' (Beleidsregel Actief in Nederland).

- addressing of potential Dutch investors by direct mail, fax or e-mail
- regarding internet offers: whether it is clear from the content of the website (and not its technical accessibility on the internet) that these products are targeted to the Dutch market, i. a. the following criteria are considered by BaFin
  - domain name
  - (in particular) the Dutch language
  - product description
  - providing information on the Dutch tax regime
  - financial or other country-specific client information and legal framework
  - prices and methods of payment
  - provision of Dutch contact details
  - fact that financial services are actually being sold to Dutch clients
  - content of possible advertising
  - disclaimer is only one of many indications

As a conclusion, also foreign financial actors not having their place of business or residence in the Netherlands are captured by Dutch regulations in case they approach Dutch investors.

## 4.2 Inbound

The question is whether the Crowdfunding platform addresses Dutch investors or wants to present Dutch companies / projects on its platform.

### 4.2.1 Foreign Crowdfunding platform addresses Dutch investors

Dutch regulatory law can apply to the Crowdfunding platform (mainly licence, information and compliance obligations) and/or the company / project seeking funding (mainly prospectus and information obligations).

The main criterion for the AFM is whether the Dutch language is used to present the investment opportunities. Therefore, in case the investment opportunities are presented in the Dutch language, the AFM will (most likely) come to the conclusion that Dutch regulatory law applies.

#### 4.2.1.1 Crowdfunding platform

##### (1) Licence obligations

The applicable regulatory law (and its extent) depends on whether the Crowdfunding platform has a (passportable) MiFID licence in another EU member state.

##### (a) The platform holds a MiFID licence in another EU member state

##### Scope of MiFID

Financial instruments pursuant to MiFID i. a. comprise of transferable securities and financial instruments equal to transferable securities, see further paragraph **Fehler! Verweisquelle konnte nicht gefunden werden.** (share and certificates of shares) and paragraph 3.1.3(bonds and notes). The second Markets in Financial Instruments Directive (**MiFID2**) which came into force on 3 July 2014 and will take effect in January 2018 does not change the scope of relevant financial instrument for Crowdfunding.

In the Netherlands, most start-up companies are organised in the legal form of a limited company (*besloten vennootschap*). Project companies are usually also structured as limited liability companies. This is due to the fact that these company forms can be easily established and handled without causing high costs. Shares in a limited liability company are considered transferable by the AFM (even though the transfer of such shares required a notarial deed and contain transfer restrictions, see paragraph 3.1.1).

However, equity model Crowdfunding only represents a negligible percentage of Dutch Crowdfunding as illustrated under paragraph 1 and as such use of MiFID passporting rights in of little relevance here. As stated above under paragraph 4, over 80% of Dutch Crowdfunding platforms mediate in non-transferable loans that are not captured by the definition of financial instrument under MiFID as implemented in Article 1:1 of the Wft. Hence, the vast majority of Dutch Crowdfunding platforms cannot make use of MiFID passporting rights.

### EU Passport

As a general rule, a foreign Crowdfunding platform with a MiFID licence can conduct business in the Netherlands without applying for a licence and without having a presence in the Netherlands via completing a so-called notification procedure (**EU Passport**).

However, in case the Crowdfunding platform holds a MiFID licence and intends to address Dutch investors it is unclear whether the MiFID licence is sufficient also for providing financial services with regard to financial instruments *not* covered by this MiFID licence – e. g. mediating non-transferable loans as most Dutch Crowdfunding platforms mediate in.

Further, it is not entirely sure whether a foreign MiFID license holder would be able to mediate in shares of a Dutch limited liability company. Whilst that is possible for Dutch MiFID license holders it could well be the case that foreign regulators have a different interpretation of shares under MiFID. That could create differences, because it is the home state regulator that determines what is allowed under an EU Passport. By the purpose of the introduction of an EU Passport as well as the intention of the European legislator (intending to create a level playing field across the EU) these MiFID licences should also cover financial instruments covered by the MiFID licence of the target country.

As a conclusion of these different scopes, it cannot be excluded that a Crowdfunding platform with a foreign MiFID licence might need – in addition – a dispensation under Article 4:3 of the Wft or even a Dutch MiFID license (which will require the foreign company to

incorporate in the Netherlands) in order to be allowed to mediate in Dutch company shares as well as non-transferable loans.

### **(b) The platform has no MiFID licence**

As already mentioned, if the Crowdfunding platform intends to address Dutch investors, Dutch regulations are applicable. Therefore, the Crowdfunding platform must – as a principle – must obtain a dispensation under Article 4:3 of the Wft to mediate in non-transferable loans or a MiFID license under Article 2:99 of the Wft if the platform targets the Dutch market in order to mediate in financial instruments targeted by MiFID.

## **(2) Other financial regulation**

The Dutch Money Laundering and Terrorist Financing is the only Dutch regulatory law which – in principle – is not connected to a Dutch license but rather to the type of service that is delivered in the Netherlands. Since the foreign Crowdfunding platform will be active in the Netherlands it will be subject to Dutch anti-money laundering regulations (but may be subject to the local anti-money laundering regulation of its home (EU) country too).

### **4.2.1.2 Company / project**

#### **Dutch prospectus regulations**

As mentioned above according to the AFM – as a general rule – Dutch financial regulations applies in case the Dutch market (Dutch investors) is approached by (foreign) financial actors. The main criterion of the AFM to assess whether Dutch regulatory laws are applicable comprises whether the Dutch language is used to present the investment opportunities.

The applicable prospectus regime depends on whether the foreign company / project offers financial instruments covered by MiFID (which is often the case in foreign (EU) countries, e.g. France). So, what could be exempt from the prospectus regulations in one country (Germany for instance in respect of certain shares that involve a notarial deed to be transferred) is likely not exempt in the Netherlands from the Dutch prospectus regulations.

As a principle, the respective Dutch prospectus regime is applicable which means that the company / project must prepare a prospectus.

### **4.2.2 Foreign Crowdfunding platform addresses Dutch companies**

Again Dutch regulatory law can apply to the:

- Crowdfunding platform (mainly licence and information obligations);  
and/or
- company / project intending to be funded on the Crowdfunding platform (mainly prospectus and information obligations).

As mentioned above the AFM considers several criteria in order to assume that the Dutch market is approached and (therefore) Dutch regulatory laws are applicable. The main

criterion of the AFM is whether the Dutch language is used to present the investment opportunities. Other criteria may be that Dutch companies / projects are involved. However, this criterion alone will (most likely) not be sufficient for the AFM to conclude that Dutch regulatory laws are applicable.

Therefore, in case the investment opportunities are not presented in Dutch language the AFM will (most likely) come to the conclusion that Dutch regulatory law does not apply. This is because the offer is presented on a foreign website / language (e. g. German) by a foreign Crowdfunding platform.

#### **4.2.2.1 Crowdfunding platform**

##### **(1) Licence obligations**

Here, the foreign Crowdfunding platform does not approach Dutch investors. In this case Dutch regulatory laws do not apply such that there are no Dutch licence requirements.

##### **(2) Other financial regulation**

Dutch companies / projects almost never issue equity-based securities in the Crowdfunding market. This is because Dutch companies / projects are (almost always) structured as limited liability companies (*besloten vennootschappen*) and the transfer of shares in Dutch limited liability companies require a notarial deed (driving effort and up cost significantly). Nonetheless, the AFM qualifies shares in Dutch limited liability companies as transferable securities. This means that if the Crowdfunding platform provides other MiFID related services to project companies (such as investment advice) they can still trigger Dutch regulatory laws (i.e. a MiFID license in this example).

#### **4.2.2.2 Company / project**

##### **(1) Prospectus regulation**

The Dutch prospectus regulations establish a prospectus requirement only in case the transferable financial instruments are offered *in the Netherlands*.

As mentioned above according to the AFM – as a general rule – Dutch regulatory laws do not apply here since the investment opportunities are not presented in the Dutch language.

##### **(2) Other financial regulation**

Dutch AIFMD regulations could be triggered for the company / project in the exceptional circumstance that its vehicle is captured as an AIF and managed by a Dutch AIFM (see paragraph 3.7).

### **4.3 Outbound**

In this situation a Dutch Crowdfunding platform enters foreign (European) markets and therefore addresses foreign investors.

Again, two different alternatives must be considered:

- Dutch Crowdfunding platform approaches foreign (EU) investors; or
- Dutch Crowdfunding platform approaches Dutch investors and presents a company / project from another EU member state on its platform.

#### **4.3.1 Dutch Crowdfunding platform addresses foreign (EU) investors**

As mentioned above the AFM considers several criteria in order to assume that the Dutch market is approached and (therefore) Dutch regulatory laws are applicable.

Here, only foreign investors (e.g. a Dutch platform addresses German investors) are addressed.

However, here the Crowdfunding platform and the companies / projects are based in the Netherlands and therefore the main actors have a Dutch reference. If several further indicators – e. g. Dutch speaking contact persons and the information on investment opportunities is clearly adjusted to Dutch regulatory laws – tend to the assumption that the Dutch market is approached.

However, within the overall view of all criteria the AFM will most likely come to the conclusion that Dutch regulatory law is not applicable in this case. This is because only foreign investors are addressed and only foreign (e. g. German) language is used. Therefore, Dutch regulatory laws will (likely) not be applicable.

##### **4.3.1.1 Crowdfunding platform**

###### **(1) Licence obligation**

As mentioned above Dutch regulatory laws will not be applicable to the Dutch Crowdfunding platform. This is because the Dutch Crowdfunding platform exclusively addresses foreign investors and also does not use the Dutch language (but e.g. German). Therefore, the Dutch Crowdfunding platform will (likely) not have licence requirements.

###### **(2) Other financial regulation**

We do not see any particular Dutch regulatory laws being applicable here. At the same time, we note that it will likely be very difficult for a Dutch based company to be strictly active cross border for tax purposes and also because as a Crowdfunding platform without incorporation in the county it targets (regulatory laws of the target jurisdiction will likely be triggered and cannot be met without local incorporation).

##### **4.3.1.2 Company / project**

###### **(1) Prospectus regulation**

The Dutch prospectus regulations establish a prospectus requirement only in case the transferable financial instruments (securities) are offered in the Netherlands.

In case that a company / project only addresses foreign investors (e.g. a French platform addresses French investors) the company / project does not target the Dutch market / Dutch investors. The Dutch prospectus regulation is – as a general rule – not applicable.

## **(2) Other financial regulation**

We do not see any particular Dutch regulatory laws being applicable here to the Company / Project.

### **4.3.2 Dutch Crowdfunding platform addresses foreign companies / projects**

As mentioned above the AFM considers several criteria in order to assume that the Dutch market is approached and (therefore) Dutch regulatory laws are applicable. The main criterion of the AFM is whether the Dutch language is used to present the investment opportunities. Therefore, in case the investment opportunities are presented in the Dutch language the AFM will (most likely) come to the conclusion that Dutch regulatory laws apply.

Here, Dutch investors are approached – Dutch language will be used. The AFM will come to the conclusion that Dutch regulatory laws will be applicable.

#### **4.3.2.1 Crowdfunding platform**

##### **(1) Licence obligation**

In case the Dutch Crowdfunding platform approaches Dutch investors and presents foreign companies / projects, e. g. French companies, on its platform it – as already stated – must obtain a dispensation under Article 4:3 of the Wft to mediate in non-transferable loans or a MiFID license under Article 2:99 of the Wft if the platform targets the Dutch market in order to mediate in financial instruments (equity- / debt-based) securities captured by MiFID.

##### **(2) Other financial regulation**

In addition, - in exceptional cases where the Dutch Crowdfunding platform provides services mainly related to (equity- / debt-based) securities – it might be subject to other additional regulations. E.g. when providing investment advice pursuant to the Wft must provide investors with information about itself, the provided services and the financial instruments to which the services are related; conduct an appropriateness test vis-à-vis investors, etc.

#### **4.3.2.2 Company / project**

##### **(1) Prospectus regulation**

As mentioned above the European prospectus regulations only apply to financial instruments within the meaning of MiFID / MiFID II.

Since foreign companies / projects often offer equity-based or debt-based securities (e. g. bonds or notes) the (European and Dutch) prospectus regulations are applicable to these

financial instruments offered on the Dutch Crowdfunding market. Also the upcoming European Prospectus Regulation that provides for an exemption from the prospectus requirement up to EUR million will in this case apply to financial instruments within the meaning of MiFID / MiFID II.

Moreover, the foreign company / project might face (local) prospectus requirements pursuant to its home state in the EU. We cannot assess whether a (local) prospectus requirement exists if the Dutch Crowdfunding platform presents foreign companies / projects in a campaign to Dutch investors. However, it may be that a foreign (EU) country / the respective financial regulation authority might not follow the marketing focussed approach of AFM but another approach (e. g. simply connected to the seat / place of residence of the member state in the EU. Here, a double regulation cannot be excluded.

## **(2) Other financial regulation**

We do not see any particular Dutch regulatory laws being applicable here to the Company / Project.

### **4.4 Impact of EU regulation**

#### **4.4.1 Prospectus rule / regimes**

Equity model Crowdfunding only represents a negligible percentage of Dutch crowdfunding as illustrated under paragraph 1 company and as such use of MiFID passporting rights in of little relevance here. As stated above under paragraph 4, over 80% of Dutch Crowdfunding platforms mediate in non-transferable loans that are not captured by the definition of financial instrument under MiFID as implemented in Article 1:1 of the Wft. Hence, the vast majority of Dutch Crowdfunding platforms cannot make use of MiFID passporting rights.

That vast majority relies on a local Crowdfunding regime tailored around a dispensation that originates from the Capital Requirements Directive in respect of repayable funds. In result, the majority of Crowdfunding campaigns in the Netherlands are not affected by European prospectus regulations but (pure) national regulations, including local decrees and even AFM administrative decisions (*voorschriften*).

#### **4.4.2 AIFMD**

The AIFMD could affect equity-based Crowdfunding. In case project companies do not operate the facility or production themselves or by means of an outsourcing company leaving the day-to-day discretion to the "Project Companies" they are no operating companies and – as a general rule – fall under subject to quite heavy AIFMD regulations.

In theory, there might exist a (regulatory) barrier here since the AIFMD could apply to the company / project. This could cause a barrier for cross-border offerings since the interpretation whether there exists a collective investment undertaking (and therefore an AIF) or not remains with the respective local authorities (e. g. the AFM in the Netherlands).

It cannot be excluded that if a local supervisory authority comes to the conclusion that an entity is *not* considered as an AIF, another local supervisory authority might come to another conclusion and classify this company / project as an AIF. Adding to this, it is our experience that local interpretations of AIFMD highly differ from member state to member state.

Further, also the fact that the definition and the requirements regarding retail offerings by an AIF are not harmonized on a European level might lead to frictions in the intensity of regulation: In some EU member states there exist lower / higher regulations (so-called retail top-ups) as is the case in the Netherlands for retail AIF whereas in some EU member states retail AIF are completely prohibited.

#### 4.4.3 MiFID / MiFID2

Although MiFID and MiFID2 i. a. deal with financial instruments and Dutch shares of limited liability companies are considered in scope, the Dutch equity model Crowdfunding market is so small that its impact is negligible. Equity model Crowdfunding only represents a negligible percentage of Dutch Crowdfunding as illustrated under paragraph 1 and as such the impact of MiFID in yet of little relevance in the Netherlands. As stated above under paragraph 4, over 80% of Dutch Crowdfunding platforms mediate in non-transferable loans that are not captured by the definition of financial instrument under MiFID as implemented in Article 1:1 of the Wft. Hence, the vast majority of Dutch Crowdfunding platforms cannot make use of MiFID passporting rights.

#### 4.4.4 PSD / PSD2

The Payment Services Directive has been implemented in the Wft. The Payment Services Directive 2 (entered into force in 2016) and will take effect in the Netherlands on 13 January 2018. Payment services in Europe are generally harmonized, but regarding the details there is still room for interpretation of the national legislators and (especially) financial regulation authorities which does not lead to a fully harmonized single market in Europe. For example, the commercial agent example is interpreted far more liberal in the UK than in the Netherlands. In result, a Dutch Crowdfunding platform can be confronted with a license requirement in respect of payment services, while an equivalent platform in the UK is not.

The commercial agent exemption is tightened in PSD2 and DNB has indicated it will interpret it accordingly when PSD2 takes effect early next year.

Therefore these two directives have a great impact for Crowdfunding regarding the transaction of the investments.

### 4.5 Summary

With the growing number of countries implementing specific Crowdfunding regulation it is be-coming more burdensome for European market participants to develop a pan-European crowd-funding business and for foreign Crowdfunding platforms to enter into the European

market. This development is contrary to the aim of establishing a European single market and promoting Crowdfunding as a method of financing on a European level.

Especially the following (regulatory and subsequent practical or factual) barriers hinder cross-border activities of Crowdfunding platforms from a Dutch perspective:

- Wide scope of application of Dutch regulatory law with the AFM following its marketing focussed approach.
- Inbound as well as outbound: frictions regarding the scope of MiFID licence and local (Dutch) licence with regard to covered financial instruments and usage of the EU Passport which at least leads to uncertainty of Crowdfunding market participants.
- Foreign Crowdfunding platforms can face factual and practical barriers when applying for an AFM dispensation in the Netherlands (no base in the Netherlands and proof of expertise).
- The vast majority (more than 80%) of the Dutch Crowdfunding platforms cannot passport local AFM dispensation within the EU.
- Almost every investment in companies / projects by means of Crowdfunding in the Netherlands is made through non-transferable loan which are not covered by MiFID / MiFID2 or the European prospectus regulation. Therefore, Dutch Crowdfunding platforms do not have access to the European prospectus regulation.
- Dutch companies / projects might face different (or even double) local prospectus regimes in case they approach foreign investors and investors of their home (EU) country for the same project.

## 5 Lessons learned from Dutch regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model ("dos")

We see it as a positive signal that the Dutch minister of Finance has recognised the importance of Crowdfunding as a new kind of funding and has introduced a specific local Crowdfunding framework (tailored to non-transferable loan platforms) and a dispensation for the ban on taking commissions for MiFID license Crowdfunding platforms in the Netherlands.

For a possible harmonised European the following aspects can serve as a role model:

- exception of Crowdfunding from most regulatory requirements (in particular prospectus requirement)
- three-page fact sheet for investors
- only lighter regulation of the Crowdfunding platform
- unlimited investment amounts for "professional" investors

## 5.2 Aspects that should be avoided ("don'ts")

- However, the predominant part of the Dutch Crowdfunding regulations should not build the basis for a possible European Crowdfunding regulation.
- In particular, the following aspects should not be inherited:
- Limitation of the Crowdfunding regime to non-transferable loans resulting in a different regulatory regime between non-transferable loans and financial instrument such as bonds and notes that otherwise are highly similar in Crowdfunding context; and
- Leave too much room for local regulators to top-up European Crowdfunding requirements in respect of license requirements on local level – although certain local retail investor protection differences can be handled by Crowdfunding operating cross borders (as is, for instance, the case under AIFMD).

## 6 Conclusion

In conclusion, the (regulatory) barriers deriving from the frictions between European and Dutch regulation as well as the partial European regulation hinder all participants to extend their activities also to cross-border situations.

The increasing fragmentation of the European Crowdfunding regulation due to the introduction of national Crowdfunding regulations even aggravates the barriers for cross border Crowdfunding.

The following measures on a European legislative / administrative level should be taken in order to create a level playing field around the EU from a Dutch perspective:

- Regulation of all types of financial instruments used in Crowdfunding (especially also non-transferable financial instruments) and not only securities – with regard to MiFID2 as well as European prospectus regulation;
- Clarification that a MiFID (2) licence (and the EU Passport) cover all financial instruments covered by national legislation in the host EU member state when crossing border.
- Consider to introduce short a regulation that connects and otherwise fills the gaps between MiFID(2), AIFMD and CRD4 (in respect of repayable funds) that specifically deals with Crowdfunding under these directives and regulations. The European Venture Capital Fund regulation (EuVECA) can serve as an example in this context.

## 7 Summary – Crowdfunding regulation

| Country   | Netherlands   |
|---|---|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Enhanced Crowdfunding regime for non-transferable loan Crowdfunding platforms</li> <li>• Dispensation for ban on taking commissions by MiFID license Crowdfunding platforms</li> <li>• In the legislative letter of 2016, the AFM requested the Minister of finance to push the local Crowdfunding framework even further and migrate the framework completely into the Dutch financial supervisor regulation the Wft.</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>                            |   |
| <b>General regulation</b>   | <ul style="list-style-type: none"> <li>• Non-transferable loan Crowdfunding platforms have to comply with a local dispensation regime based on a dispensation for mediating in attracting repayable funds.</li> <li>• Equity and loan (bonds and notes) based Crowdfunding platforms require a MiFID license from the AFM (for transmitting orders or as a placing agent) but to not always have to also comply with the above local Crowdfunding regime.</li> </ul>  |
| <b>Prospectus requirement</b>   | <ul style="list-style-type: none"> <li>• Relevant for Crowdfunding:               <ul style="list-style-type: none"> <li>– Total offering maximum: EUR 2.5 million per year per instrument type (shares or bonds);</li> <li>– Information documents; and</li> <li>– Warning banner.</li> </ul> </li> </ul>  |
| <b>AIFMD-regulation</b>   | <ul style="list-style-type: none"> <li>• AIFMD not applied in the Netherlands (but has been tried) for Crowdfunding.</li> <li>• Typical start-up company in general does not constitute an AIF;</li> <li>• "Project Company" might constitute AIF;               <ul style="list-style-type: none"> <li>– extensive AIFMD regulation for AIF and its manager (AIFM);</li> <li>– AIFM requires AFM authorisation;</li> </ul> </li> <li>• "Project Companies" that constitute operating companies (general business purpose) are no AIF; and</li> <li>• Funding by means of subordinated loans does not entail an AIF.</li> </ul> |
| <b>Payment service regulation</b>   | <ul style="list-style-type: none"> <li>• Transfer of funds through operator may constitute money remittance service               <ul style="list-style-type: none"> <li>– AFM authorisation required</li> </ul> </li> <li>• Cooperation with a payment institute / bank is required, but could also trigger a license for mediation in payment account or electronic money.</li> </ul>   |

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| <p><b>Further possible requirements</b></p> | <ul style="list-style-type: none"> <li>• The Dutch Civil Code (<i>Burgerlijk Wetboek</i>);</li> <li>• The Dutch Personal Data Protection Act (<i>Wet bescherming persoonsgegevens</i>)</li> <li>• The Dutch Telecommunication Act (<i>Telecommunicatiewet</i>);</li> <li>• The Dutch Consumer Credit Act (<i>Wet op het consumentenkrediet</i>); and</li> <li>• The Dutch Money Laundering and Terrorist Financing (Prevention) Act (<i>Wet ter voorkoming van witwassen en financiering van terrorisme</i>).</li> </ul>   |
| <p><b>Regulatory barriers</b></p>           |  |
| <p><b>Inbound</b></p>                       | <p><b>Foreign Crowdfunding platform addresses Dutch investors</b></p> <ul style="list-style-type: none"> <li>- Dutch regulatory laws are applicable since Dutch investors are approached by presenting the investment opportunities in Dutch language</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- The platform has a foreign MiFID / MiFID2 licence and intends to address Dutch investors                 <ul style="list-style-type: none"> <li>→ as a general rule, a platform with a foreign MiFID licence can conduct business in the Netherlands without applying for a licence and without having a presence in the Netherlands (so-called notification procedure / EU Passport)</li> <li>→ it cannot be excluded that a Crowdfunding platform with a foreign MiFID licence might need – in addition – a (local) Dutch licence – in order to be allowed to offer all kinds of company shares as well as subordinated loans in the Netherlands</li> <li>→ Generally, the foreign Crowdfunding platform might be subject to other Dutch regulations in exceptional cases (e. g. the Dutch Act on Money Laundering).</li> </ul> </li> <li>- The platform has no MiFID / MiFID2 licence and intends to address Dutch investors</li> </ul> </li> <li>• The Crowdfunding platform must apply for the Crowdfunding platform must – as a principle – obtain a dispensation under Article 4:5 of the Wft to mediate in non-transferable loans or a MiFID license under Article 2:99 of the Wft if the platform targets the Dutch market in order to mediate in financial instruments targeted by MiFID. Foreign Company / project             <ul style="list-style-type: none"> <li>- Dutch prospectus regime is applicable since the foreign companies / projects offer investment opportunities in the Netherlands (provided the offer entail financial instruments).</li> </ul> </li> </ul> <p><b>Foreign Crowdfunding platform addresses Dutch companies / projects</b></p> |

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|                        | <ul style="list-style-type: none"> <li>- The AFM will (most likely) come to the conclusion that Dutch regulatory laws do not apply in case the investment opportunities are not presented in the Dutch language</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- as a general rule since the foreign Crowdfunding platform will not target the Dutch market / Dutch investors, Dutch regulatory laws are not applicable – no licence requirements pursuant to Dutch regulatory laws</li> <li>- Generally, the foreign Crowdfunding platform might be subject to other Dutch regulations (e.g. the Dutch Act on Money Laundering).</li> </ul> </li> <li>• Dutch Company / project             <ul style="list-style-type: none"> <li>- in case Dutch companies / projects issue debt-based securities (e.g. bonds) they might – in exceptional cases – be subject to other Dutch regulation.</li> </ul> </li> </ul>  |
| <p><b>Outbound</b></p> | <p><b>Dutch Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>- Here, only foreign investors (e.g. a Dutch platform addresses German investors) are addressed. However, if several further indicators – e.g. Dutch contact persons and details or investment opportunities are clearly adjusted to German regulatory law, English language – tend to the assumption that the Dutch market is approached the AFM might come to the conclusion that the Dutch market is approached and Dutch regulatory laws are applicable.</li> <li>- However, within the overall view of all criteria, the AFM will (most likely) come to the conclusion that Dutch regulatory laws are not applicable in this case.</li> <li>• Crowdfunding platform             <ul style="list-style-type: none"> <li>- as a general rule since the Crowdfunding platform will not target the Dutch market / Dutch investors, German regulatory laws are not applicable – no prospectus requirements</li> <li>- Crowdfunding platform might be subject to other Dutch regulation in exceptional cases (e. g. the Dutch Act on Money Laundering).</li> </ul> </li> <li>• Company / project             <ul style="list-style-type: none"> <li>- None in particular</li> </ul> </li> </ul> <p><b>Dutch Crowdfunding platform addresses foreign companies / projects</b></p> <ul style="list-style-type: none"> <li>- here, Dutch investors are approached – Dutch language will be used. The AFM will come to the conclusion that Dutch regulatory laws will be applicable.</li> <li>• Crowdfunding platform</li> </ul> |

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|                                | <ul style="list-style-type: none"> <li>- regular Dutch regulation applies to the Crowdfunding platform (licence obligation)</li> <li>- Crowdfunding platform might be subject to other Dutch regulation in exceptional cases (e.g. the Dutch Act on Money Laundering).</li> <li>• Company / project <ul style="list-style-type: none"> <li>- Dutch prospectus regimes are applicable since the foreign companies / projects offer investment opportunities in the Netherlands</li> <li>- applicable prospectus regime depends on whether the foreign company / project offers transferable securities (which is often the case in foreign (EU) countries, e. g. France) or other financial instruments.</li> <li>- in addition to the Dutch regulatory laws, the company / project might face (local) prospectus requirements pursuant to its home (EU) country, e. g. in case the home (EU) country / financial regulation authority follow another approach than the AFM (marketing focussed approach)</li> <li>- in this case the prospectus requirements of the host (EU) country as well as the Dutch regulatory laws might apply to the company / project which might lead to double regulation</li> </ul> </li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | These EU regulations have no great impact to Crowdfunding in the Netherlands   |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• AIFM-Directive and its implementation in Dutch law have a very small to no impact on Crowdfunding since the “typical” company (start-up) or project seeks funding for its general operative activity (commercial business) by means of a Crowdfunding platform</li> <li>• only so called Project Companies that do not operate the business themselves might be subject to the fund regulation</li> <li>• different interpretations of local authorities regarding the definition of collective investment undertaking (constituting an AIF) might lead to different application of AIFMD and local implementations <ul style="list-style-type: none"> <li>- severe consequences for company / project as well as (at least economically) for Crowdfunding platforms.</li> <li>- also retail AIFs are regulated differently across the EU which complicates cross-border situations.</li> </ul> </li> </ul>   |
| <b>MiFID / MiFID2</b>          | In the Netherlands most of the Crowdfunding platforms facilitate the offering of non-transferable loans which do not fall under MiFID / MiFID2. In doing so they are subject to the local Dutch Crowdfunding framework attached to a dispensation granted by the AFM. This local dispensation  |

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|                   | has less requirements, but is not passportable into other EU member states.  |
| <b>PSD / PSD2</b> | <ul style="list-style-type: none"> <li>Any transfer of funds through the operator of a Crowdfunding platform may constitute money remittance services within the meaning the Wft, implementation of PSD / PSD2 in Dutch law</li> <li>Great impact for Crowdfunding regarding the fund processing of the investments</li> </ul> |

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# Poland

## 1 Recent developments in the market for Crowdfunding in Poland

Poland is a prospective market for the development of (various models of) Crowdfunding. Recent significant developments in the markets for Crowdfunding models in Poland are described below.

It is also worth mentioning that there are other Polish initiatives on the Crowdfunding market as broadly understood that may influence the future of this method of raising capital. The so called token crowdsales or initial coin offerings (ICOs) are based on issuance of tokens on public block chains such as *Ethereum*. Tokens may have various functions depending on their construction and may even constitute equity and debt-like financial instruments.

One of the most widely known Crowdfunding projects of this type so far has been the Crowdfunding campaign of Project Golem, which develops the Golem Network as a decentralized sharing economy of computing power. In November 2016, its creators and developers managed to raise cryptocurrency (ether), the value of which at the time was equivalent to USD 8.6m, in 29 minutes through a Crowdfunding campaign based on a smart contract in the Ethereum blockchain. Each contribution in ether sent by a backer was rewarded by sending back Golem Network Tokens, which will be necessary to use services of the Golem Network in the future. Similar Crowdfunding campaigns are becoming increasingly popular throughout the world.

Token crowdsales cannot be easily qualified as any of the well-established types of Crowdfunding (such as the Equity Model, Debt Model or Donations or Rewards Model). Moreover, they put into question the current regulatory approach to Crowdfunding, in which a lot of attention is devoted to Crowdfunding platforms. In token crowdsales, fund raising and distribution of tokens are usually done with use of smart contracts without the need for a third party's intermediation.

It remains to be seen how this new type of Crowdfunding will develop in the future, but it should be subject to close attention by regulators.

During recent years, we have seen the following significant developments in Poland regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Over recent years, development of Crowdfunding using the Equity Model has seen steady growth. At present, there are numerous Crowdfunding platforms operating using this model, such as: *CrowdAngels*, *GetFunded*, *Beesfund*, *FindFunds*.

No regulations that would specifically concern the Equity Model of Crowdfunding have been adopted so far. Therefore, the legal barriers for the development of the Crowdfunding market in Poland still inhibit its growth (see points 2. and 3. below for further details).

The basic prospectus threshold is relatively low and amounts to EUR 100,000. In principle, exceeding the threshold would trigger a prospectus requirement. Usually, the value of a project campaigned on a Crowdfunding platform that facilitates issuance of shares that are financial instruments, and thus are subject to securities offering requirements (such as shares in joint-stock companies – *spółki akcyjne*), is set below the threshold to avoid regulatory requirements.

Some Crowdfunding platforms in Poland have chosen an alternative path, which is to use the Polish limited liability company (*spółka z ograniczoną odpowiedzialnością*) instead of joint-stock company. In Poland, shares in limited liability companies are not considered securities and thus there is no requirement for fulfilment of public offering conditions. However, using a limited liability company as a vehicle comes with its own problems – the minimum value of a share should amount to PLN 50 and the sales contract has to be confirmed by a notary public.

At the moment, Crowdfunding platforms use one of the two above indicated strategies. The market structure is quite stable due to lack of regulatory developments so far (see, however, point 2. below). According to the Crowdfunding platforms' representatives, market sentiment is positive and we will see a growing number of equity based Crowdfunding campaigns in 2017 and onwards.

## **1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)**

Alternative methods for granting loans (social loans, online loans, etc.) are enjoying great and constantly growing popularity in Poland. Part of this growing market is in platforms acting on a lending based Crowdfunding model, in particular peer-to-peer lending.

## **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

The model based on rewards is the most developed model in Poland. The largest numbers of Crowdfunding platforms operate and the largest numbers of projects are being implemented on the basis of this model. In this model, financiers receive a specified type of reward, which is a mutual performance for the contribution of a specified monetary amount.

Similarly, the Donations Model is also popular in Poland. The most prominent examples include charitable Crowdfunding platforms, which very often do not charge project originators except for fees to cover costs related to a platform's operations.

## 1.4 Role of “Real Estate Crowdfunding” and “Renewable Crowdfunding” in Poland

Irrespective of the aforementioned categories, there is an emerging trend in Poland to facilitate Crowdfunding to finance real estate and renewable projects. New Crowdfunding platforms are emerging specializing in these kinds of projects and existing platforms are extending their business.

In Poland during the last two years there has been a significant increase in real estate Crowdfunding.

Under Polish law, each registered and adult user of a platform that has capacity to act in law is able to invest online in real estate Crowdfunding. The first Polish real estate Crowdfunding platform was established in October 2015. Three projects have been accomplished through this platform so far.

Another platform came up with an idea of organizing a group of investors that would, as a SPV, purchase shares in a development venture and would then rent flats in the building built by this venture.

The last-mentioned platform gained PLN 1.5m from small investors for the town house in Łódź at the beginning of 2015.

In comparison to the other EU member states, the share of RES projects in Crowdfunding is relatively small. Thus, in Poland only a few Crowdfunding platforms have emerged through which investors can support renewable energy projects.

As of April 2017, these RES Crowdfunding Platforms have already financed around ten wind power plants in Poland. However, these are usually not necessarily typical Crowdfunding platforms. They are not just intermediaries between the crowd and project initiators. They both gather funds from investors and develop their own RES projects. They are usually registered as Polish limited liability companies (*spółka z ograniczoną odpowiedzialnością*), where individual investors obtain shares (*udziały*) in the company.

## 1.5 International approach in your country

There are only Polish platforms operating on the market.

## 2 Recent developments regarding Crowdfunding regulation in Poland

Poland has not yet adopted any regulations that would specifically concern Crowdfunding in any of its models. However, a growing interest can be observed on the part of regulators.

In 2014, the Polish government published its position on Crowdfunding and its potential regulation in the future. It was stressed that there is currently no need to introduce binding legal regulations, because the Crowdfunding market in Poland is still in its early stage of development. Attention was also drawn to the significant differences between investment and non-investment Crowdfunding (different purposes, use in different sectors, difference in legal

regulations, different risks, etc.), which might entail different regulations in the future for different types of Crowdfunding.

At the beginning of the development of Crowdfunding in Poland, it was sometimes compared to public collections. The comparison of Crowdfunding and public collections was particularly popular before the entry into force of the new Public Collections Act dated 14 March 2014, which has replaced the Public Collections Act adopted on 15 March 1933. Nonetheless, Crowdfunding is not subject to these new regulations stemming from the new Public Collections Act. Putting Crowdfunding outside the scope of the Public Collections Act is in accordance with the abovementioned position of the government, which stated that at the present stage of market development there is no need to introduce particular regulations for Crowdfunding.

The Coalition for Polish Innovations published a draft bill in October 2015, which amends several items of legislation in order to facilitate Crowdfunding. The bill, which was drafted with the participation of representatives of the Polish Crowdfunding community (Wardyński & Partners coordinated the working group), aimed to introduce exemptions for Crowdfunding in several legal acts. The exemptions focused on equity Crowdfunding and aimed to ease its regulatory burden related to public offering regimes and requirements for trade in financial instruments. The bill also proposed introducing an exemption related to the payment services regime, which would facilitate the growth of all types of Crowdfunding.

A development which took place on 1 April 2016 was potentially important for the future of equity based Crowdfunding in Poland. Due to an amendment to the Polish Code of Commercial Companies, disposal of shares in a LLC became possible not only through a notary public, but also in a computerized system. The statements of the seller and the purchaser should be furnished with a secure electronic signature verified with the help of a valid qualified certificate or signature confirmed by a trusted ePUAP profile. This may potentially facilitate an equity based Crowdfunding model that uses limited liability companies (*spółki z ograniczoną odpowiedzialnością*). However, this has not happened yet due to low popularity of electronic signatures and ePUAP profiles. This may change together with the EU's eIDAS regulation and the ongoing development of the national electronic identifications system. The usefulness of the described change is further limited by the fact that only a specific category of limited liability companies can take advantage of this, i.e. those established using an online system using the template agreement provided in regulations issued under the statute. If such a template company agreement is amended in any manner (outside of amendments predefined in the online system), the company's shares can no longer be disposed of electronically. In effect, companies seeking to benefit from this amendment must sacrifice preparing a tailor-made company agreement.

Moreover, since mid-2016, the Polish Ministry of Economic Development has been working on a new kind of company – the simple joint-share company, also known as simple capital company. The aim is to make this new type of company a convenient startup vehicle that could

also be used for raising capital through equity based Crowdfunding. However, no details have yet been revealed with regard to this proposal.

In April 2017, the Polish Ministry of Development and Finance declared that it was working on an amendment to the Foreign Exchange Law that would regulate online foreign exchange services, but no draft bill has yet been made available at the time of writing. Crowdfunding platforms should carefully monitor the development of this legislation.

Finally, in 2017 the Polish Financial Supervision Authority initiated a joint market and government working group tasked with identifying legal barriers to financial innovations. Among several task forces, one is working on Crowdfunding regulations and legal barriers concerning social lending. This task force has already prepared an initial document describing and analysing legal barriers hindering the development of Crowdfunding in Poland.

### 3 Current Regulation of Crowdfunding in Poland

There is no clear and explicit regulation of Crowdfunding in Poland. The government, fearing hindering innovative initiatives, has during the last few years limited its activities to observing and monitoring development of Crowdfunding platforms, without introducing any laws. Therefore, the basic framework for Crowdfunding transactions in Poland is still the Polish Civil Code and several other acts. Certain types of Crowdfunding related activities may trigger application of financial regulations.

The basic function of a Crowdfunding platform is to bring together someone seeking financing with an investor, which can take place on the basis of acting on behalf of the originator of a project, through presenting his offer to potential investors, or by bringing together a seeker of finance with an investor, so as to bring about the conclusion of a transaction between them. In this second case, the platform would not represent the originator of an idea and would not act in his name. In addition, platforms can provide both sides with an indispensable “vehicle”, or in other words a company, on the basis of which the originator’s undertaking will be conducted after the necessary financial resources for this purpose have been obtained from participants.

The scope of regulations applicable to platforms participating in organizing equity Crowdfunding will be determined to some degree by the type of equity rights participants will obtain in exchange for the provided financing. Simplifying, this boils down to determining whether the equity rights received by a financing participant in the company, which is to conduct financing of the undertaking, will qualify as a financial instrument in the meaning of the Trade in Financial Instruments Act dated 29 July 2005.

Should Crowdfunding be organized on the basis of a limited liability company (*spółka z o.o.*), and participants financing the originator’s project receive shares in such a company, then the platform’s activity will not be a regulated activity, irrespective of which of the two formulae indicated above is taken, and more specifically brokerage activity.

If, however, the participants should acquire shares, whether in joint-stock companies (*spółka akcyjna*) or limited joint-stock partnerships (*spółka komandytowo-akcyjna*), then it will be necessary to assess the activity of the platform from the point of view of the requirements for brokerage activity. This will be so because shares comprise financial instruments in the meaning of the Trade in Financial Instruments Act and intermediation in trade therein is subject to the regulations of this act.

Where the platform should happen to act and appear in the name of the project originator, carrying out a collection of funds in his name, this can be understood as an offer for participation in the company and in consequence a kind of brokerage activity may come into play, based on offering financial instruments. On the other hand, where the role of the platform is to bring together the parties to the transaction for the purpose of concluding a transaction between them, consideration should be given to brokerage activity as based on accepting and passing on instructions for the acquisition of financial instruments.

### 3.1 Regulation under the Banking Act – All Models

The general rule encapsulated in Article 171 Section 1 of the Banking Law states that whoever carries out, without authorisation, a business consisting in pooling of funds of other natural or legal persons, or organizations without legal personality in order to extend credits or loans, or exposes such funds to risk in another way, shall be liable to a fine of up to PLN 10m and to imprisonment of up to 5 years.

In certain Crowdfunding models, the nature of activity by platforms might bring to mind the depositary activity conducted by banks. This can be seen particularly in lending based Crowdfunding, which can take various forms. In many cases, loans are granted directly between the financier and the beneficiary. In such cases, the role of the Crowdfunding platform operator comes down to bringing together the financier and the beneficiary, which in itself is not a regulated activity. However, other issues may arise in such a model with regard to the status of financiers, who depending on the extent of their activity may be considered as entrepreneurs, which increases their regulatory burdens. The latter creates a degree of regulatory uncertainty with regard to peer-to-peer lending in Poland.

A significantly more complicated situation arises in the model where, apart from bringing together the financiers and beneficiary, the platform operator also aggregates the resources coming from the financiers and then grants loans to the beneficiary itself. Such a model is intended to simplify the financing structure. This is because, in effect, the beneficiary only enters into one loan agreement with the operator, not into many loan agreements with particular financiers. On the other hand, in granting the loan the operator uses resources gathered from the financiers. At the moment the loan is repaid, the operator distributes the repayment received in proportion among the financiers. In this model, platform activity constitutes de facto banking activity.

The platform collects financial resources from the financiers (which is the equivalent of deposit-taking activity by the banks) and aggregates them, after which it grants loans to the

beneficiary, financing the loan from the resources obtained from the financiers (which is the equivalent of credit granting activity by the banks). The resources gathered from the financiers are encumbered by risks in the sense that there is no guarantee that they will be repaid.

The regulation mentioned in the first paragraph shows that certain lending based Crowdfunding models can be encumbered with significant legal risk, based on possible attempts to qualify this type of Crowdfunding as banking activity requiring permission. Thus, in practice and given the present legal status, operators of platforms envisaging lending based Crowdfunding who wish to avoid unnecessary administrative burdens or penal liability should seek to create models that envisage financing taking place directly between the financier and beneficiary (the operator's role in this case is limited to bringing together the financier and beneficiary and to handing over the monetary resources), while bearing in mind that the latter is not entirely without its own problems.

## 3.2 Prospectus requirements

### 3.2.1 General remarks

Under the Polish Trading in Financial Instruments Act (*ustawa o obrocie instrumentami finansowymi*) of 29 July 2005 ("TFIA"), respective activities are regulated and require a licence. TFIA is essentially an implementation of the MiFID directives. Equity Crowdfunding can potentially fall within the scope of TFIA. This depends on two factors: (i) whether the instruments involved in Crowdfunding qualify as financial instruments and (ii) whether the activities of a Crowdfunding platform are investment services as defined in MiFID, referred to in TFIA as brokerage activities (*działalność maklerska*) – as defined by TFIA.

### 3.2.2 Financial instruments

TFIA divides financial instruments into two groups: securities (*papiery wartościowe*) and other instruments that are not securities, such as units of ownership in collective investment schemes (*tytuły uczestnictwa w instytucjach wspólnego inwestowania*) or derivatives (*instrumenty pochodne*). In most cases, equity Crowdfunding consists of trading in company shares, which fall into the category of securities. However, it is crucial to remember that not all kinds of company shares are considered securities under TFIA. This depends on the type of company used as Crowdfunding vehicle.

The shares (*akcje*) of a joint-stock company (*spółka akcyjna*) and of a limited joint-stock partnership (*spółka komandytowo-akcyjna*) are securities under TFIA. On the other hand, the shares (*udziały*) of a limited liability company (*spółka z ograniczoną odpowiedzialnością*) are not considered to be securities, so their trading falls outside the scope of TFIA. To sum up, a Crowdfunding platform will not be regulated under TFIA if the investors participate in Crowdfunding projects by obtaining shares in a limited liability company, but it may be regulated if the shares belong to a joint-stock company or a limited joint-stock company.

### 3.2.3 Brokerage activities

If equity Crowdfunding involves financial instruments in the above meaning, the activities of a Crowdfunding platform must be carefully evaluated to determine if they are brokerage activities. Usually, one of two types of brokerage activities comes into play. Firstly, if a Crowdfunding platform's role is to bring together the two parties in order to conclude a transaction between them, such as sale of securities (shares), this may be considered to be brokerage activity that consists of accepting and transmitting orders to acquire financial instruments. Secondly, if a Crowdfunding platform's role is to present the possibility of acquiring shares on behalf of a SPV and carry out collection of funds in the name of the project's initiator, this may be considered to be brokerage activity that consists of offering financial instruments (the so-called placing of securities). To summarize, some types of equity Crowdfunding may fall into the scope of TFIA and constitute investment services.

### 3.2.4 Prospectus

Crowdfunding project initiators that make a public offering of securities to investors can be obliged to prepare and publish a prospectus under the Polish Public Offering, Conditions for the Introduction of Financial Instruments to Organized Trading, and Public Companies Act (*ustawa o ofercie publicznej i warunkach wprowadzania instrumentów finansowych do zorganizowanego systemu obrotu oraz o spółkach publicznych*) ("Public Offering Act"). Again, the notion of 'securities' does not include shares in a limited liability company, but it does apply to shares in a joint-stock company. This is a significant burden for initiators, since the prospectus, which contains extensive information, must be prepared in a formal procedure, with the intermediation of an investment firm, and receive approval from the Financial Supervision Commission.

Under the Public Offering Act, a public offering is defined as "making available to at least 150 persons in one Member State or to an unspecified addressee, in any form and by any means, information about securities and conditions for their acquisition, that constitute a sufficient basis for making a decision to acquire these securities." There are a number of exemptions from the prospectus requirement. The initiator does not need to prepare a prospectus e.g. if the acquired financing is of relatively low value – up to EUR 100,000 over a 12-month period. This exemption is often used by the Poland-based Crowdfunding project originators.

## 3.3 Regulation of Crowdfunding under the Investment Funds Act and the AIFMD regime

In planning the obtaining of funds for a certain kind of undertaking through Crowdfunding, the beneficiary will have to consider the possible application to his planned activity of the regulations in the Investment Funds and Alternative Investment Funds Management Act dated 27 May 2004 ("Investment Funds Act").

At present, activities based on placing funds in certain rights (e.g. securities, receivables, derivative instruments), where these funds have been gathered from other persons through a

proposal to enter into an agreement, the object of which is participation in such an undertaking, can be performed solely through the form of an investment fund or alternative investment fund on principles regulated by the Investment Funds Act.

Thus, should an originator seek to make use of Crowdfunding to obtain financial resources which would then be invested in rights to assets such as shares, securities or derivative instruments, for the purpose of increasing the value of the funds obtained, it should carry out a thorough-going analysis of the planned activity from the point of view of the requirements specified in the Investment Funds Act. The regulations concerning investment fund activity will not, on the other hand, constitute a barrier to obtaining resources through Crowdfunding for financing commercial undertakings based on manufacturing, trading or services activity, or in other words the activities typically undertaken by start-ups.

It cannot be excluded that some project initiators will fall under the scope of the Polish implementation of the AIFMD and will have to comply with the regulatory requirements—here a higher level of caution should be exercised.

### **3.4 Regulation under the Payment Services Directive**

Operators of Crowdfunding platforms normally gather funds paid-in by funders and then, after collecting a specified amount, transfer these to the target beneficiary. Intermediation may also be involved within the framework of specified Crowdfunding models in transferring funds from beneficiaries to financiers (e.g. in the framework of equity Crowdfunding). There is no doubt that they thereby perform a payment transaction in the meaning of the Payment Services Act dated 19 August 2011 (that implements PSD), which in turn implies that essentially they are providing a regulated payment service in the meaning of the Payment Services Act.

Despite the intermediation in payments performed by Crowdfunding platform operators being a payment transaction in the meaning of the Payment Services Act, it should be assumed that in most cases operators will not have to obtain permission for providing payment services. This is because most platforms will fulfil the prerequisite for applying an exception specified in article 6 point 2 of the Payment Services Act. Pursuant to this regulation, the requirements specified in the Payment Services Act do not apply to payment transactions between a payer and recipient of the actions carried out through the intermediation of the performing person, intended to bring about the conclusion between the payer and recipient of the said agreement, or containing such an agreement in the name of or on behalf of the payer or recipient. It can be argued that in facilitating for beneficiaries the presentation of their offers on a platform, the operator of such a Crowdfunding platform performs an activity aimed at the conclusion of an agreement between a funder and a beneficiary.

Soon, Poland will have to implement PSD2 into its national system (the deadline is in January 2018). While no draft implementing bill is yet available, it is expected that amendments to the Payment Services Act will hinder the ability of Crowdfunding platforms to rely on the exception described above. This is because PSD2 significantly narrows the

exception, reducing its application basically to cases where a commercial agent (intermediary) is acting on behalf of either only the payer or only the payee. As explained above, Crowdfunding platforms usually act on behalf of both parties to the transaction.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

#### 3.5.1 Anti-money laundering regulation

On account of the binding regulations concerning money laundering and the financing of terrorism, all activity based on intermediation in transferring monetary resources should also be analysed from the point of view of the requirements imposed by the Counteracting Money Laundering and Financing of Terrorism Act dated 16 November 2000. From the perspective of the Crowdfunding platform operator, the key thing is to determine whether it will be one of the obligated institutions in the meaning of the Counteracting Money Laundering Act.

At the moment, there are no regulations which would refer directly to the operators of Crowdfunding platforms. Determining whether an operator is subject to the regulations on counteracting money laundering will depend in great measure on the Crowdfunding model adopted by the given operator. It seems that the most disseminated Crowdfunding models in Poland at the moment and simultaneously the simplest Crowdfunding models (donations based and rewards based Crowdfunding), will essentially not be subject to the regulations concerning counteracting of money laundering. Crowdfunding platform operators active in the framework of the models referred to do not conduct regulated activity which would imply the necessity of applying the regulations of the Counteracting Money Laundering Act. The role of the operators in this case comes down to just bringing together financers with beneficiaries.

The situation of platform operators based on the equity or lending models seems to be significantly more complicated. In this case, depending on the activity structure adopted for the platform, the operator may conduct regulated activity or activity in the nature of a financial institution in the meaning of article 4 section 1 point 7 of the Banking Law.

In such a case, the operator would be treated as an institution that was obligated in the meaning of the Counteracting Money Laundering Act and would be obliged to apply the preventative measures against money laundering and financing of terrorism envisaged by this act.

Further, attention should be drawn that a Crowdfunding platform operator performing exchange of currencies (e.g. converting the financer's currency to the beneficiary's currency) will be subject to the Counteracting Money Laundering Act due to the regime of this act clearly encompassing activity based on the exchange of currency.

Currently, the Polish government is working on implementation of the new EU Directive (AMLD4) to Polish law. However, the new law should not materially influence the above conclusions.

### **3.5.2 Act on Rendering Electronic Services dated 18 July 2002**

Since Crowdfunding platforms are run using the Internet, there should be no doubt that the services provided by platform operators (even if they just come down to bringing together financers and beneficiaries) should be qualified as being, as to principle, services provided by electronic means in the meaning of the provisions of the Act on Rendering Electronic Services. In association with such a qualification, Crowdfunding platform operators should possess regulations for the provision of services and adhere to the regulations concerning processing the personal data of persons using a platform, as specified in the Act on Rendering Electronic Services.

### **3.5.3 Consumer Credit Act dated 12 May 2011**

A loan agreement is a standard lending based Crowdfunding instrument. In this context, it should be determined whether agreements entered into within the framework of a Crowdfunding platform should be treated as being consumer credit agreements in the meaning of the act on consumer credit. Also of key importance in this case is the specified model for lending based Crowdfunding. The Consumer Credit Act refers only to loan agreements in which the creditor is an entrepreneur in the meaning of the Polish Civil Code. It should be assumed that in the case of most models where loans are entered into directly between the financer and beneficiary, we will not be dealing with an entrepreneur on the financer's side (though the exact point at which the extent of financer activity makes him an entrepreneur is controversial). Practice hitherto shows that in most cases these are consumers. In such case, a loan agreement entered into between a financer and beneficiary will not be qualified as being a consumer credit agreement in the meaning of the Consumer Credit Act. On the other hand, the regulations on loan agreements contained in the Civil Code might apply thereto.

### **3.5.4 Foreign Exchange Law dated 27 July 2002**

Crowdfunding platform operators may also carry out currency exchanges in the course of their activity. This occurs in particular when a financing payment is provided in a currency other than a currency accepted by the beneficiary. In such a case, the platform operator converts the currency at an exchange rate determined in advance, and thus conducts activity based on the exchange of currencies.

Due to the definitional limitations encompassed by the Foreign Exchange Law, this nonetheless does not automatically mean that an operator conducts bureau de change activity. This is because the regulations of the Foreign Exchange Law imply that bureau de change activity relates to foreign currency in physical form (banknotes and coinage). Meanwhile, it should be assumed that in the decided majority of cases, if not always, the exchange of currency in Crowdfunding platforms will relate to currency in non-physical form. Thus, so

long as Crowdfunding platform operators do not perform currency exchanges in physical form, they will not have to register their activity in the register of bureau de change activity maintained by the chairman of the National Bank of Poland (*Narodowy Bank Polski – NBP*).

The conducting of foreign exchange activity by a Crowdfunding platform operator may, on the other hand, give rise to the necessity of the operator applying the regulations of the Countering Money Laundering Act.

## 4 Regulatory barriers for Crowdfunding crossing borders

As indicated above, many equity Crowdfunding platforms operate through using limited liability companies. Shares in LLCs are not deemed financial instruments and thus securities regulations do not apply. In the cases where shares in joint-stock companies are being offered to investors, the situation is the opposite. Therefore, such offers are usually designed to fall into regulatory exemption (their value is below EUR 100,000). This, however, may cause that specific activity of Crowdfunding platforms may fall into the scope of TFIA and constitute investment services.

As regards debt based Crowdfunding, Crowdfunding platforms operating in this model are usually structured so as to avoid application of regulations such as the Polish implementation of the PSD (the Payment Services Act).

### 4.1 Applicable law

The primary approach used in Poland to determine the application of regulatory law is the registered seat approach. Providers of financial services that have their registered office or ordinary residence in Poland fall under Polish regulatory law. In addition, financial actors that target the Polish market from outside the jurisdiction in order to offer financial services to companies / persons in Polish (such as issuers of financial instruments or brokers with their registered seat outside Poland) may also fall under its scope.

There is no explicit law that specifies the criteria used to determine that a financial actor targets the Polish market. It can be assumed that criteria taken into account by the Polish Financial Supervision Authority (*Komisja Nadzoru Finansowego – KNF*) would include the methods and contents of advertising, language and currency used, direct addressing of Polish clients, endorsements by Polish clients, etc. Recently, KNF has been very active in the field of foreign platforms which offer various financial services to potential Polish customers.

### 4.2 Inbound

The question is whether the Crowdfunding platform addresses Polish investors or wants to present Polish companies / projects on its platform.

### 4.2.1 Foreign Crowdfunding platforms addressing Polish investors

Application of the Polish financial regulatory framework to a foreign Crowdfunding platform addressing Polish investors would mainly depend on the Crowdfunding model and structure adopted by such platform.

As already mentioned, there are no specific Crowdfunding regulations in Poland. Generally, there is no requirement of having a licence in order to operate a Crowdfunding platform, nor are there any other conditions set for foreign Crowdfunding platforms, unless the platform's activity can be qualified to be MiFID investment service. Unless any specific financial regulations apply, Crowdfunding platforms would have to comply with general regulations on conducting economic activity in Poland (including consumer protection regulations, etc.). If platforms are registered in one of the EU Member States, they can take advantage of fundamental rules of freedom of establishment and freedom to provide services specified in the Treaty on the Functioning of the European Union (TFEU). Because of that, they have a right to offer services and target the Polish market.

However, should the foreign Crowdfunding platform operate in a model that falls into the Polish financial regulatory framework (such as offering financial instruments to the public), the relevant regulations will apply. In principle, if such Crowdfunding platform has a relevant MiFID licence in another EU member state, it can passport the licence to Poland.

### 4.2.2 Company / project

#### 4.2.2.1 Prospectus regulation

The Public Offering Act establishes a prospectus requirement in case financial products are publicly offered in Poland. Thus, if any company is targeting Polish users in this way, in principle it should follow prospectus regulations.

This act envisages a series of exceptions from the prospectus requirement, for instance waivers from this obligation for low value public offerings, where the total financial value of financing obtained in this way is not to exceed EUR 100,000 over a 12-month period.

As already mentioned, Crowdfunding can also be organized on the basis of participation in a limited liability company (*spółka z o.o.*). Shares in a limited liability company are not securities, and the Public Offering Act will not apply to public proposals for taking hold of these, and in consequence such a share sale offer does not need to be accompanied by a prospectus.

## 4.3 Outbound

In this situation, a Polish Crowdfunding platform enters foreign (European) markets and therefore addresses foreign investors.

In principle, the Polish regulatory law will not be applicable in this case. This is because only foreign investors are addressed.

### **4.3.1 Crowdfunding platform**

#### **Licence obligation**

As mentioned above, Polish regulatory law will not be applicable to the Polish Crowdfunding platform. This is because the Polish Crowdfunding platform exclusively addresses foreign investors. Therefore, the Polish Crowdfunding platform will have to abide with licence requirements, depending on the regulations in addressed jurisdictions.

### **4.3.2 Company / project**

#### **Prospectus regulation**

The Polish Public Offering Act establishes a prospectus requirement only in case the financial products are publicly offered in Poland.

## **4.4 Impact of EU regulation**

### **4.4.1 Prospectus rule / regimes**

As stated above, the EU Prospectus Directive was transposed into Polish law under the Public Offering Act.

### **4.4.2 AIFM-Directive**

The AIFM-Directive and the implementing Investment Funds and Alternative Investment Funds Management Act of 2004 (as amended in 2016) with four executive regulations implementing AIFM – Directive mainly concern the equity-based Crowdfunding model.

The laws implementing the AIFM-Directive also relate to the Polish Financial Authority Supervision's control over investors and funds. Also, Crowdfunding initiators (especially those offering an equity model) could be registered as funds on the basis of the AIFM-Directive.

### **4.4.3 MiFID / MiFID II**

Some of equity based Crowdfunding platforms use the regime of the Polish implementation of the MiFID. Many Crowdfunding campaigns fall within the regulatory exceptions.

In the alternative model, where the limited liability companies are used, MiFID does not apply (shares in LLCs are not deemed financial instruments).

MiFID II is in the process of implementation to the Polish legal system.

### **4.4.4 PSD / PSD II**

The Payment Services Directive was implemented by the Payment Services Act in 2009 ("PSA"). Many Crowdfunding platforms in Poland either rely on regulated payment services providers or structure their business in such a way as to be covered by one of exemptions in the PSA, in particular the so called commercial agent exemption.

The Payment Services Directive II (entered into force in 2016) must be implemented by January 2018 and has not yet been transposed in Poland. Due to the fact that PSD2 significantly narrows the above mentioned exception, it might be expected that some of the Crowdfunding platforms in Poland may be brought under the payment services regulatory regime.

#### 4.5 Summary

So far, Crowdfunding in Poland is a local phenomenon. Some startups organize Crowdfunding campaigns abroad (e.g. in the US), but neither are Polish Crowdfunding platforms expanding abroad nor do foreign ones have a prominent presence in Poland.

At least to some degree, this state of affairs follows from the regulatory regime in place. Polish Crowdfunding platforms usually want to avoid regulatory burden and try to not fall under MiFID or PSD regulation. They consider regulations too restrictive and difficult and structure their business accordingly. This, however, causes many limitations for scaling up and international expansion. The MiFID regulatory regime can be avoided by using limited liability companies as Crowdfunding ventures (in the case of equity based Crowdfunding), but at the same time this has many disadvantages (such as the legal barrier of public notary requirement in the case of sale of shares in LLC).

It seems that introducing a new, EU-wide regulatory regime might create a space for larger growth of the Crowdfunding market in Poland. However, should the regulations be too restrictive, they might also hinder the growth of this still nascent industry.

### 5 Lessons learned from Polish regulation for a possible harmonized European Crowdfunding regulation

Taking into account that Poland has not implemented specific regulations regarding Crowdfunding, we can only offer recommendations based on assumptions and observations.

#### 5.1 Role model ("dos")

For a possible harmonized European system, the following aspects can serve as a role model:

- light-touch regulatory regime that would be bearable by Crowdfunding platforms that still are, at least in Poland, relatively small and operate on a limited scale;
- clear determination of when the payment services regulations should be applied to various Crowdfunding models and elimination of regulatory uncertainty in this area;
- exploration of schemes in which Crowdfunding and VC funding is used complementarily;
- exploration of how block chain might be used in the context of Crowdfunding in the EU and its regulation.

## 5.2 Aspects that should be avoided ("don'ts")

In particular, the following aspect should not be inherited:

- it is important not to overregulate the Crowdfunding platforms.

## 6 Conclusion

At least partially due to the regulatory regime, Crowdfunding platforms in Poland seem to be insufficiently robust to undertake cross-border activities. The potential regulatory measures should take this into account. On the one hand, they should provide a clear and unambiguous regime for conducting Crowdfunding activity (the lack of which is apparent, at least in Poland). On the other hand, when working on the future regulation one should be aware of the still nascent level of development in the industry, at least in Poland.

## 7 Summary – Crowdfunding Regulation

| Country   | Poland  |
|---|---|
| <b>Summary</b><br><br><b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Poland has not yet adopted any regulations that would specifically concern Crowdfunding in any of its models</li> <li>• In 2014, the Polish government published its position on Crowdfunding and its potential regulation in the future:               <ul style="list-style-type: none"> <li>→ there is currently no need to introduce binding legal regulations, because the Crowdfunding market in Poland is still in its early stage of development</li> </ul> </li> <li>• Since mid-2016, the Polish Ministry of Economic Development is working on a new kind of company – simple joint-share company               <ul style="list-style-type: none"> <li>→ the aim is to make this new type of a company a convenient startup vehicle that could be also used for raising capital through equity based Crowdfunding</li> </ul> </li> <li>• In 2017 the Polish Financial Supervision Authority initiated a joint market and government working group with a task to identify legal barriers regarding financial innovations               <ul style="list-style-type: none"> <li>– among several task forces, there is one working on Crowdfunding regulations and legal barriers concerning social lending</li> <li>– this task force has already prepared an initial document describing and analysing legal barriers hindering the development of Crowdfunding in Poland</li> </ul> </li> </ul> |
| <b>Current / planned Crowdfunding regulation</b>                            |   |
| <b>General regulation</b>   | <p>There is no clear and explicit regulation of Crowdfunding in Poland</p> <ul style="list-style-type: none"> <li>• the framework for the Crowdfunding transactions in Poland is still the Polish Civil Code and several other acts</li> <li>• certain types of Crowdfunding-related activities may trigger application of financial regulations</li> </ul>   |
| <b>Investment services/ prospectus requirement</b>                          | <ul style="list-style-type: none"> <li>• Under the Polish Trading in Financial Instruments Act (<i>ustawa o obrocie instrumentami finansowymi</i>) of 29 July 2005 (“TFIA”), investment services are regulated and require a licence               <ul style="list-style-type: none"> <li>→ TFIA is essentially an implementation of the MiFID directives</li> </ul> </li> <li>• Crowdfunding project initiators can be obliged to prepare and publish a prospectus under the Polish Public Offering, Conditions for the Introduction of Financial Instruments to Organised Trading, and Public Companies Act:               <ul style="list-style-type: none"> <li>– the notion of ‘securities’ does not include shares in a limited liability company, but it applies to shares of joint-stock company</li> </ul> </li> </ul>   |

|                                      |  |
|--------------------------------------|--|
|                                      | <ul style="list-style-type: none"> <li>- under the Act, a public offering is defined as “making available to at least 150 persons in one EU Member State or to an unspecified addressee, in any form and by any means, information about securities and conditions for their acquisition, that constitute a sufficient basis for making a decision to acquire these securities.”</li> <li>- there are a number of exemptions from the prospectus requirement. The initiator does not need to prepare a prospectus e.g. if the acquired financing is of relatively low value – up to EUR 100,000 over a 12-month period</li> </ul>  |
| <b>AIFMD-regulation</b>              | <p>It cannot be excluded that some projects initiators will fall under the scope of the Polish implementation of the AIFMD and will have to comply with the regulatory requirements.</p>   |
| <b>Payment service regulation</b>    | <ul style="list-style-type: none"> <li>• Polish Payment Services Act dated 19 August 2011 implements PSD <ul style="list-style-type: none"> <li>- it implies that Crowdfunding platforms are providing a regulated payment service in the meaning of the Payment Services Act.</li> <li>- despite the intermediation in payments performed by Crowdfunding platform operators in most cases they will not have to obtain permission for providing payment services</li> <li>- the requirements specified in the Payment Services Act do not apply to payment transactions between a payer and recipient of the actions carried out through the intermediation of the performing person, intended to bring about the conclusion between the payer and recipient of the said agreement, or containing such an agreement in the name of or on behalf of the payer or recipient</li> </ul> </li> <li>• Poland will have to transpose PSD2 into its national system (the deadline is in January 2018). Revision of Payment Services Act may concern the issue of Crowdfunding platforms</li> </ul>                          |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Anti-money laundering regulation <ul style="list-style-type: none"> <li>- all activity based on intermediation in transferring monetary resources should be analysed from the point of view of the requirements imposed by the Counteracting Money Laundering and Financing of Terrorism Act dated 16 November 2000</li> <li>- the key thing is to determine whether the Crowdfunding platform operator will be one of the obligated institutions in the meaning of the Counteracting Money Laundering Act</li> </ul> </li> <li>• Act on Rendering Electronic Services dated 18 July 2002 <ul style="list-style-type: none"> <li>- the services provided by platform operators should be qualified as being, as to principle, services provided by electronic means in the meaning of the provisions of the Act on Rendering Electronic Services</li> <li>- Crowdfunding platform operators should possess regulations for the provision of services and adhere to the regulations concerning processing the personal data of persons using a platform</li> </ul> </li> </ul> |

|                            |  |
|----------------------------|--|
|                            | <ul style="list-style-type: none"> <li>• Consumer Credit Act dated 12 May 2011 <ul style="list-style-type: none"> <li>– it should be determined whether agreements entered into within the framework of a Crowdfunding platform should be treated as being consumer credit agreements in the meaning of the act on consumer credit</li> <li>– the Consumer Credit Act refers only to loan agreements in which the creditor is an entrepreneur in the meaning of the Polish Civil Code</li> <li>– it should be assumed that in the case of most models where loans are entered into directly between the financier and beneficiary, we will not be dealing with an entrepreneur on the financier’s side</li> <li>– practice shows that in most cases these are consumers. In such case, a loan agreement entered into between a financier and beneficiary will not be qualified as being a consumer credit agreement in the meaning of the act on consumer credit</li> </ul> </li> <li>• Foreign Exchange Law dated 27 July 2002 <ul style="list-style-type: none"> <li>– Crowdfunding platform operators may also carry out currency exchanges in the course of their activity</li> <li>– when a financing payment is provided in a currency other than a currency accepted by the beneficiary, the platform operator converts the currency at an exchange rate determined in advance</li> </ul> </li> </ul> |
| <b>Regulatory barriers</b> |  |
| <b>Inbound</b>             | <ul style="list-style-type: none"> <li>• Application of the Polish financial regulatory framework to a foreign Crowdfunding platform which addresses Polish investors would mainly depend on the Crowdfunding model and structure adopted by such platform.</li> <li>• Unless any specific financial regulations apply, Crowdfunding platforms would have to comply with general regulations on conducting economic activity in Poland</li> <li>• If platforms are registered in one of the EU Member States, they can take advantage of fundamental rules of freedom of establishment and freedom to provide services specified in the Treaty on the Functioning of the European Union (TFEU).</li> <li>• They have a right to offer services and target Polish market.</li> <li>• However, should the foreign Crowdfunding platform operate in a model that falls into the Polish financial regulatory framework (such as offering financial instruments to the public), the relevant regulations will apply. <ul style="list-style-type: none"> <li>→ if such Crowdfunding platform has a relevant MiFID licence in another EU member state, it can passport the licence to Poland.</li> </ul> </li> </ul>  |
| <b>Outbound</b>            | <ul style="list-style-type: none"> <li>• In principle, the Polish regulatory law will not be applicable in this case. <ul style="list-style-type: none"> <li>→ This is because the Polish Crowdfunding platform exclusively addresses foreign investors. Therefore, the Polish Crowdfunding</li> </ul> </li> </ul>   |

|                                |   |
|--------------------------------|---|
|                                | <p>platform will have to abide licence requirements depending on the regulations in addressed jurisdictions.</p> <ul style="list-style-type: none"> <li>Polish Public Offerings, Terms and Conditions for Introducing Financial Instruments into Organised Trade, and Public Companies Act dated 29 July 2005 establishes a prospectus requirement only in case the financial products are offered in Poland.</li> </ul>  |
| <b>Impact of EU regulation</b> |   |
| <b>Prospectus regulations</b>  | The Public Offerings, Terms and Conditions for Introducing Financial Instruments into Organised Trade, and Public Companies Act dated 29 July 2005, which transposed EU law into Polish legal system.   |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>The AIFM-Directive and the implementing Investment Funds Act of 2004 (as amended in 2016) with four executive regulations implementing AIFM – Directive</li> <li>The laws implementing AIFM-Directive regard also Polish Financial Authority Supervision’s control over the investors and funds.<br/>→ on the basis of the AIFM-Directive Crowdfunding platforms (especially those offering equity model) could be registered as fund.</li> </ul>  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>Some of equity based Crowdfunding platforms use the regime of the Polish implementation of the MiFID. Many Crowdfunding campaigns fall within the regulatory exceptions.</li> <li>In the alternative model, where the limited liability companies are used, MiFID does not apply (shares in LLCs are not deemed financial instruments).</li> <li>MiFID II is in the process of implementation to the Polish legal system.</li> </ul>   |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>The Payment Services Directive was implemented by the Payment Services Act in 2009 (“PSA”).<br/>→ many Crowdfunding platforms in Poland either rely on regulated payment services providers or structure their business in a way to be covered by one of exemptions in the PSA, in particular the so called commercial agent exemption.</li> <li>Due to the fact that PSD2 significantly narrows the above mentioned exception, it might be expected that some of the Crowdfunding platforms in Poland may be brought under the payment services regulatory regime.</li> </ul> |

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# Portugal

## 1 Recent developments in the market of Crowdfunding in Portugal

The recent development of Crowdfunding in Portugal is related with the newly approved legal regime followed by the approval of the regulation of CMVM regarding the Lending and Equity models which were not possible to implement in Portugal until now due to the lack of a specific legal framework.

### 1.1 The Equity Model

The Equity Model implies, in exchange for a contribution or investment, the assignment of shares or warrants to buy shares of the company or the granting of a percentage share or fixed return from any revenues (or profits) generated by the company in the future.

Until August 2015, the Equity Model was very difficult to implement in Portugal due to the lack of specific legislation on this subject. In fact, the offering of shares or any kind of equity interest in share companies would probably imply the compliance with the requirements of the Portuguese Securities Exchange Commission (“CMVM”) including the registry of the platform as a financial intermediary at the CMVM and (eventually) the approval of a prospectus (according to the requirements established in the Portuguese Securities Code).

The approval of the regulation of CMVM will allow the offer of securities without having to comply with the CMVM general requirements for offers. However, although the legal framework as well as its regulation have been recently approved, the regulation will not enter into force until the approval of the respective penalties' legal regime. So we will have to wait to see additional developments.

### 1.2 The Lending Model

The Lending Model involves a loan to fund the project, with an expectation of monetary reimbursement in the form of interest. This model has been very difficult to implement in Portugal in the last years, once it would be qualified as a credit or financial transaction (which may only be carried out in Portugal by duly authorised credit or financial institutions), but now the new Legal Framework for Crowdfunding has created specific and faster registration procedures at the CMVM.

Until August 2015, also the Lending Model was very difficult to implement in Portugal without the registry as a financial intermediary at the CMVM or/and at the Banco de Portugal.

In Portugal, the two main types of Crowdfunding platforms operate under the Pre-sale Lending Model and the Rewards Model. But with the approval of the legal framework of Crowdfunding the Equity and Lending Model may see more development in the next years.

### 1.3 The Donations or Rewards Model

In the Rewards Model foreseen by the new Legal framework, individuals make a financial contribution to a project in exchange for the delivery of the funded product or service.

The law approved the Rewards Model as a usually so-called **Pre-sale Lending Model** that is often combined with the pure Rewards Model<sup>1</sup>. In this Pre-sale Lending Model, finished product or service is promised in return for and according to the contributor's loan (usually through an assessment of the fair market value of the product/service).

With the new legal regime this Crowdfunding model has also been developed by a regulation that requires a prior registry at the Portuguese Authority for Consumer's Protection to comply with several information requirements. This entity will also be responsible to disclose a list of Crowdfunding Platforms in its site.

### 1.4 Role of the „Real Estate Crowdfunding“ and „Renewable Crowdfunding“ in Portugal

Portugal is now giving its first steps in the emerging market of the Real Estate Crowdfunding which is a crowdfunding sector that had already great developments in other EU countries, once this kind of projects benefit from a higher investor confidence (due to the underlying real estate assets of the beneficiaries companies).

With the approval of the Crowdfunding legal regime, followed by the approval of the CMVM Regulation regarding the Equity and Lending based Crowdfunding, it became possible to finance real estate projects through Crowdfunding, once the investment in real estate projects are made under equity or lending models, which were difficult to implement in Portugal until the approval of the legal regime of Crowdfunding, once they would require a license for financial intermediation or for credit institution, under supervision of CMVM or Banco de Portugal respectively.

We will certainly see new developments in this area during the year of 2017, especially upon the entry into force of the CMVM Regulation.

Also in the Renewable Crowdfunding the Portuguese market is giving its first steps, once the most adequate models for RES Projects are the Lending and Equity based Crowdfunding,

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<sup>1</sup> In the „Pure“ Rewards Model, individuals make a financial contribution to a project without any expectation of a financial return on that contribution. This is the most common model in Portugal, where the individuals that fund the project are often recognized for their support with rewards that can increase according to the amount of money provided by each individual.

which were very difficult to implement in Portugal before the approval of the Crowdfunding legal regime (approved in 2015) and the CMVM Regulation (approved in 2016 but still not in force until the present date). We hope to see great developments in these two markets once the CMVM Regulation entries into force.

### 1.5 International approach in Portugal

Due to the lack of an harmonized European legislation on Crowdfunding, especially in Lending or Equity based Crowdfunding platforms, other EU platforms must comply with the mandatory Portuguese law (legal regime already approved and supervision entities regulation) in order to enter Portuguese market.

## 2 Recent developments regarding the Crowdfunding regulation in Portugal

Further to the legal framework of Crowdfunding approved in 2015, the access to the activity of Equity or Lending Crowdfunding Intermediation is made through a prior registry of the platforms operators at the CMVM, being this entity responsible for the regulation and supervision of their activity.

CMVM will control the compliance with requirements for the access to the activity, the causes of rejection, the supervision and will assure the integrity of the platforms operators, deadlines, suspension, cancellation of the registry, as well as establish the annual limit for investment in Crowdfunding per investor.

As so, on May 5<sup>th</sup>, 2016, CMVM approved a Regulation of the referred legal regime in what concerns the Platforms operating under the Equity and Lending Models.

In general terms this new Crowdfunding regulation establishes several information requirements applicable to the Crowdfunding beneficiaries (including transparency obligations), limits to the amounts invested (applicable to the investors, either per project as per year) and means to prevent conflicts of interest applicable to the platforms operators.

As already said above, the access to the activity of Equity or Lending Crowdfunding Intermediation is made through a registry of the platforms operators at the CMVM, being this entity responsible for the regulation and supervision of their activity. This Regulation also establishes the requirements to be complied with to obtain such registry, as well as the causes for its rejection, suspension or cancelation.

The Regulation also governs the requirements to guarantee the integrity of the platforms operators, the transparency of the operations and to avoid any conflict of interests.

In order to guarantee an informed decision by the investors (i) a list of Crowdfunding platforms duly registered at CMVM will be disclosed at CMVM's website, (ii) several information requirements are established to be disclosed at the Crowdfunding platforms and (iii) a list of essential information to be disclosed to the investors, prior to each offer, will be mandatory to Crowdfunding platforms.

The investors will also be subject to the following investment limits: (i) EUR 3.000,00 per offer and (ii) EUR 10.000,00 of total Crowdfunding investment/per year. These limits are not applicable to companies, to individuals with an income of EUR 70.000,00 or more or to qualified investors (according to article 30<sup>th</sup> of the Portuguese Securities Code).

The Regulation (if approved) will also establish a maximum limit for fund raising through Crowdfunding per each 12 months (by a single offer or by the total of offers within the European Union: EUR 1.000.000,00 (one million euros). Except if the offers are subscribed only by companies, investors with an income of EUR 70.000,00 or more or qualified investors, in which case, the maximum limit will be of EUR 5.000.000,00 euros (five million euros).

For the purpose of making the investment, the regulation also requires the intervention of an entity duly authorized to provide payment services.

### 3 Current Regulation of Crowdfunding in Portugal

On 2015 was approved the Law nr. 102/2015, dated August 24<sup>th</sup> that approved the legal framework applicable to the Crowdfunding, governing the models of Crowdfunding that may be adopted, the requirements to access the activity, the platforms, its property and the access to it by the beneficiaries, the investors, the supervision of the activity and the sanctions legal regime.

Essentially, the new legal framework sets the following:

- Four broad types of Crowdfunding models: (i) the Donations Model, (ii) the Rewards Model, (iii) the Equity Model and (iv) the Lending Model.
- A mandatory written agreement to adhere to a Crowdfunding platform (this agreement must be disclosed at the platform and should contain the parties' identification, the models of Crowdfunding to be used, the identification of the project or the activity to be funded and the amount and time period established for the fund raising).
- In case the total amount is not raised within the established deadline, all the agreements executed with the investors will be null and void, being the beneficiaries obliged to return all the received amounts, except if the offer expressly foresees the possibility of alteration of the total amounts and deadlines and that fact is duly communicated in the offer to all investors. In this event, the platforms must notify all investors of the subsequent alteration of the maximum amount to be raised and/or the new deadline for subscription. The extension of amounts and deadline for fundraising can only be executed once per offer and must be given to the investors a deadline to cancel the investments already made.
- The legal regime applicable to the agreements executed between the investors and the beneficiaries of the fund raising will depend on the type of agreement executed (donation, sell an purchase, services agreement, shares subscription or loan agreement).

The new legal framework also establishes the requirements to access this activity, depending on the model of Crowdfunding to be developed by the platforms (Donations/Rewards or Equity/Lending):

### **3.1 Equity and Lending Crowdfunding Platforms**

The access to the activity of intermediation by equity or lending Crowdfunding is made through a prior registry to be made at the CMVM.

This entity is responsible for the supervision and the regulation of the activity. It is also responsible for establishing the requirements to access the activity, the causes of rejection and to assure the integrity of the platforms operators, deadlines, suspension, cancellation of the registry, as well as establish the annual limit for investment in Crowdfunding per investor.

For that purpose, it was approved on May 5<sup>th</sup>, 2016, the CMVM Regulation nr. 1/2016, concerning Platforms operating under the Equity and Lending Models that globally foresees the following:

#### **3.1.1 Requirements to access the activity**

At the date of submission of registry's request the managing entity of the Platform must comply at least with two of the following financial requirements:

- A. Minimum share capital of EUR 50.000,00 totally paid up at the incorporation date;
- B. Civil liability insurance or any equivalent guarantee to cover liability arising from professional negligence, that at least covers an amount of 1.000.000,00/per casualty and, globally, 1.500.000,00 for all the casualties occurred during one year;
- C. A combination of the referred in (i) and (ii) in a form which results in a degree of protection equivalent to that conferred by any of the preceding paragraphs.

The registry is made by electronic means and the registry must be granted in a maximum period of 30 business days as of the date of the submission of the request or as of the date of the request by CMVM of complementary informations.

The registry request is made through the submission of a form (approved by the CMVM's Regulation) that includes the crowdfunding models to be adopted by the applicant, as well as the platforms' site name and address and must be instructed with the following information:

- A. applicant's identification, including the identification of the shareholders of the crowdfunding platform managing entity and the holders of qualified participations in the platform;
- B. Identification of the directors, as well as documents to assess the suitability and professional experience of the directors;
- C. Identification of all members of the corporate bodies;
- D. Registered office;
- E. Commercial certificate and by laws of the company and liability insurance contract proof;

- F. Management Report, Balance and further Company's financial statements, duly approved, of the last three financial years, if applicable;
- G. Business plan and descriptive memorandum of the structure, organization and human, material and technical resources appropriate to the type and volume of the activity to be carried out;
- H. Description of the business model including a description of how will be processed the financial flows and/or the subscription of financial instruments by investors;
- I. Indication as to whether or not it has the nature of financial intermediary or tied agent of a financial intermediary and, in the latter case, an indication of the financial intermediary to which it is linked;
- J. Compilation of policies and procedures for internal organization and conduct;
- K. Expected date to start the activity.

Any alteration to the information included in the request must be notified to CMVM within a 10 business days period as of the date of the fact caused the alteration (by submitting a specific form approved by this Regulation).

### **3.1.2 Causes of rejection of the registry**

- A. Lack of information instructing the request or of complementary information required;
- B. Inaccuracies or falsehoods of the request;
- C. If CMVM concludes for the unsuitability of the managing entity or its directors;
- D. If the managing entity does not have the human, technical and material resources or the financial resources appropriate to the type of the activity to be carried out.

The registry of the Crowdfunding platform at the CMVM will expire: (i) in case of dissolution of the managing entity or (ii) if the platform does not initiate its activity within a 12 months period as from the registry's date.

The registry may be suspended or even cancelled by the CMVM: (i) if the registry is obtained through false declarations or other illicit means; (ii) if the activity does not correspond to the authorized scope of activity; (iii) if any of the requirements for granting the registration ceases to be verified; (iv) in the event of serious irregularities in the internal organization and violation of the duties of conduct and the rules that govern the activity of the Crowdfunding platform; or (v) by request of the managing entity of the Crowdfunding platform.

The Regulation also establishes in article 9 the requirements of suitability applicable to the directors and holders of qualified participations on the capital of the managing entities of the Crowdfunding platforms

### **3.1.3 Internal organization and duties of conduct**

It is mandatory for the managing entities of Crowdfunding platforms to have written policies and procedures appropriate and effective to govern: (i) the internal control of the activity; (ii) the guarantee of compliance with the information obligations towards que

investors; (iii) prevention of fraude, money laundering and terrorism financing; (iv) treatment of investors and beneficiaries' complaints; (v) Security of data preservation and essential functions; (vi) Security and identification procedures to guarantee the identity and authenticity of the investors access to the platform, specially to submitt the essential information on the offer to disclose to the investors. The policies (ii) to (iv) must be available at the platform to be consulted.

Regarding the conflict of interests prevention, the disclosure of a written policy concerning the identification and reduction of the occurrence of conflict of interests is mandatory at the Crowdfunding platform. The managing entities also have to assure that its shareholders, directors and employees are not allowed to invest in the respective platform offers.

#### **3.1.4 Investment Limits**

- A. EUR 3.000,00 /per offer; and
- B. EUR 10.000,00 of total Crowdfunding investment/per year

These limits are not applicable to: (i) companies, (ii) to individuals with an income of EUR 70.000,00 or more or to qualified investors (according to article 30<sup>th</sup> of the Portuguese Securities Code).

#### **3.1.5 Information duties of the managing entities of Crowdfunding Platforms**

The managing entitis must disclose in the platform all relevant information to allow an informed investment decision making by the investors, including:

- A. information concerning the registry at the CMVM;
- B. prior information on each offer;
- C. information on the current offers (including the beneficiary's identification, the model of crowdfunding, deadline, remuneration rate, total amount, percentage of the amount raised, any risk ratings and guarantees provided, as well as any other material information on the terms and conditions of the offers);
- D. historic information concerning the financed projects, including the number of projects and amounts raised, separated by Crowdfunding model and indicating the current situation of the funds raising (not expired, repaid on time or not repaid on time), indicating also the average rate of return and average term of financing;
- E. price list;
- F. information on the procedures to protect the investors that should be adopted in the event of insolvency, dissolution or prolonged inactivity of the managing entity of the crowdfunding platform.

The managing entities must also disclose, concerning each capital loan that does not correspond to the acquisition of a share in the capital of the beneficiary or a loan not yet repaid: (i) the investment amount already used by each entity, activity or product financed; (ii) state of development of the activity or product financed; (iii) State of implementation of the respective business plan; (iv) all material alteration concerning the entity, activity or product

financed that may have an impact in the repayment or in the estimated profitability of the invested amounts. This information must be updated or must have a disclaimer indicating the foreseen date for the update which, in any case, may not be longer than 15 days.

### 3.1.6 Information duty of Crowdfunding beneficiary

For the purpose of disclosing to the investors, the beneficiary must submit to the platform a document with the “key information for crowdfunding investor” (which form has been approved by the regulation of CMVM) that includes:

- A. complete identification of the beneficiary;
- B. in the beneficiary is a company, the balance and management report of the previous exercise;
- C. key characteristics of the activity or product to allow the investors to understand the nature and the risks inherent to the product or activity to be funded;
- D. costs of the activity or product to be funded as well as a brief description duly substantiated of the estimated profitability of the invested amounts;
- E. offer processing details;
- F. deadline for withdrawal of acceptance by the recipients of the offer, where applicable;
- G. Time and form for the transfer of the amounts raised, namely the mechanisms for subscription and for the refund of the amounts invested if the fundraising is higher than expected or in case the expected amounts are not raised and the offer does not provide the possibility of changing the conditions;
- H. Warning on the risk of partial or total loss of the invested amounts;
- I. Warning on the risk of not verifying the estimated profitability of the amounts invested;
- J. Warning on the liquidity risk or lack of a secondary market for financial instruments or credits subscribed by investors;
- K. Warning as to the fact that the activities and products to be funded are not subject to any authorization or supervision of CMVM or by any other financial supervisor, nor do these entities approve the information disclosed on them;
- L. Warning on the fact that the investment is not covered by the Investor Compensation Scheme (except if resulting of financial intermediation and if verified the requirements of its application);
- M. Warning on the fact that the invested capital is not guaranteed under the Deposit Guarantee Fund;
- N. Warning on the fact that, in case of issuance of financial instruments, this will not be subject to CMVM’ supervision nor this entity will approve the information disclosed by the beneficiary to the investors;
- O. Warning on the fact that, in case of loan grant, this will not be subject to the supervision of Banco de Portugal, nor this entity will approve the information disclosed by the beneficiary to the investors;

- P. Applicable tax legal regime;
- Q. Procedures to be adopted, including, without limitation, the destination of the amounts invested in the platform's current offer with the liquidation or the suspension, for any reason, of the managing entity activity;
- R. Procedures to be adopted to guarantee the continuity of the payment of the amounts invested in the platform's current offer with the liquidation or the suspension, for any reason, of the managing entity activity.

The key information for crowdfunding investor shall be disclosed to the investor prior to the acceptance of any offer and must be written in Portuguese language and must be clear (without technical terms) in order to be understood by the average investor.

### 3.1.7 Offer's limit

The Regulation also establishes a maximum limit for fund raising through Crowdfunding per each 12 months (by a single offer or by the total of offers within the European Union: EUR 1.000.000,00 (one million euros). Except if the offers are subscribed only by companies, investors with an income of 70.000,00 or more or qualified investors, in which case, the maximum limit will be of EUR 5.000.000,00 euros (five million euros).

### 3.1.8 Payment services entity

For the purpose of making the investment, the regulation also requires the intervention of an entity duly authorized to provide payment services.

Finally it is important to stress that, although already approved, this Regulation is not yet in force, since its entry into force is dependent on the entry into force of the regime applicable to the violation of the legal regime of crowdfunding by equity and loan.

## 3.2 Banking / Financial Service licence requirements

No banking or financial services license is applicable once the approval of the new legal framework created a specific and simplified registry at CMVM to access the activity of Crowdfunding intermediation, which will be applicable to Crowdfunding platforms that adopt the Equity or Lending models.

## 3.3 Donation and Rewards Crowdfunding Platforms:

The access to the activity for Donations and Rewards Crowdfunding Platforms will imply a prior notice procedure at the Portuguese Authority for Consumer's Protection (" *Direcção Geral do Consumidor* ") to be made at least 30 days prior to the start of the activity of the platform.

The requirements for this prior notice to be made were regulated by the  *Portaria n° 344/2015*  of October 12<sup>th</sup> that also approved the forms to make this prior notice. The procedure is made online through the site <http://www.consumidor.pt>, is free and must include: the complete identification of the platforms owners or, in case the owner is a company, the

complete identification of its directors and its shareholders, the Crowdfunding platform' site and the identification of the Crowdfunding Model to be adopted by the platform. The prior notice must also include the access code to the permanent commercial certificate of the company that owns the platform and a declaration of inexistence of any conflict of interests (as per declaration form approved by this regulation).

The Portuguese Authority for Consumer's Protection shall be responsible to disclose a list of the Crowdfunding Platforms in its site.

Each offer made through the donation and rewards Crowdfunding platforms is subject to a limit for the fund raising of 10 (ten) times the global amount of the activity to be funded and each offer may only be offered by one Crowdfunding platform.

Information requirements, concerning each offer, to be provided by the beneficiaries to the Crowdfunding platforms for the purpose of informing the investors:

- A. Activity or product description to be funded and the purpose of the fund raising;
- B. The amount and the deadline for the fund raising;
- C. The price of each unit to be subscribed or the method for calculation of the price.

All information to be provided to the investors must be complete, true, actual, clear, objective and lawful, to allow informed decisions by all investors.

### **3.4 Prospectus requirements**

According to the new legal framework, no Prospectus will be required, except for the key information for crowdfunding investor already described above.

### **3.5 Regulation of Crowdfunding under the AIFMD regime**

The implementation of the Alternative Investment Fund Managers Directive (AIFMD) has been partially executed in Portugal through the Law nr. 16/2015 of February 24<sup>th</sup> as amended by Decree Law nr. 124/2015 of July 7<sup>th</sup> that approves the legal regime of the Collective Investment Undertakings.

According to this legal regime, a collective investment undertaking is an institution, with or without legal personality, which purpose is the collective investment of capital obtained from investors whose operation is subject to a principle of risk-sharing and to the pursuit of the exclusive interest of the participants and may be divided in two sub types: (i) Collective Investment Undertaking in transferable securities (ii) Alternative Investment Undertaking.

As for the AIFMD regime, a start-up company as the ones that typically benefit from crowdfunding does not constitute an Alternative Investment Fund, once the AIF is an entity that raises capital from a number of investors with the purpose to investing it in accordance with a defined investment policy for the benefit of those investors and does not require authorization pursuant to article 5<sup>th</sup> of Directive 2009/65/CE.

### **3.6 Requirement of a License under the Payment Services regulation**

According to article 10 number 3 of Law nr. 102/2015, this legal framework does not prejudice the application the exercise of the supervision by Bank of Portugal whenever the activity of the operators determines such supervision (which would be the case if the Crowdfunding platforms opt for receiving and handling directly the amounts received by the investors instead of according with a bank or a licensed financial institution to handle the payments).

In fact, the Crowdfunding legal regime and the approved Regulation of CMVM established the need for the intervention of an entity duly authorized to provide payment services for the purpose of making the investment.

### **3.7 Possible additional requirements (such as anti-money laundering laws, data privacy laws, consumer credit regulation)**

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

Portuguese Civil Code – concerning the specific legal frameworks applicable to purchase and sale agreement, donation and services agreement;

Law nr. 25/2008, dated June 5<sup>th</sup>, concerning the prevention of money laundering;

## **4 Regulatory barriers for Crowdfunding crossing borders**

### **4.1 Applicable Law**

Although already approved the legal regime for Equity and Lending Crowdfunding, the regime is not yet in force due to the lack of regulation, once the CMVM regulation is still waiting for the approval of the sanctions regime to enter into force.

This lack of regulation results in the difficulty for Crowdfunding Platforms to adopt equity and lending models, once it will fall under the general securities offers legal regime and may also require a licence for financial intermediation.

Notwithstanding the above, when the Crowdfunding Legal Regime is in force, as well as its regulation, the lack of a uniformed UE regulation requires foreign platforms and companies / projects that want to address the Portuguese market, to comply with the specific local requirements.

### **4.2 Inbound**

#### **4.2.1 Crowdfunding platform from another EU country addresses investors in Portugal**

In the event a foreign Crowdfunding Platform intends to approach Portuguese investors, local regulatory framework that comprises license, information and compliance requirements,

before CMVM or / and Banco de Portugal (depending on the funding models adopted) will be applicable.

Also the Project company that intends to collect funds through a Crowdfunding platform in Portugal must comply with the local legal regime, mainly compliance and information requirement for investors protection.

#### 4.2.1.1 Crowdfunding platforms

Crowdfunding platforms that operate under donation and rewards model will have to give notice to the Portuguese Authority for Consumer's Protection at least 30 days prior to the start of the activity of the platform according to the requirements established in the Portaria n.º 344/2015 of October 12th (as described in 3. above). The registry is free and is made online at <http://www.consumidor.pt>.

As for the crowdfunding platforms operating under equity and lending model, the access to the activity must be done through prior registry to be made at CMVM, by electronic means, through the submission of a form (approved by CMVM's regulation) to be instructed with the information requirements established in CMVM regulation nr. 1/2016 of May 5th (as described in 3. above).

#### 4.2.1.2 Companies / Projects

The companies and projects that intend to be funded by crowdfunding platforms operating under donation and rewards model, must comply with the following information requirements:

- A. activity or product description to be funded and the purpose of the fund raising;
- B. The amount and the deadline for the fund raising;
- C. The price of each unit to be subscribed or the method for calculation of the price.

As for the companies and projects that intend to benefit of crowdfunding platforms operating under equity and lending models, the following “key information for crowdfunding investor” as per CMVM Regulation nr. 1/2016 must be provided to the crowdfunding platform to be disclosed to the investors:

- A. complete identification of the beneficiary;
- B. in the beneficiary is a company, the balance and management report of the previous exercise;
- C. key characteristics of the activity or product to allow the investors to understand the nature and the risks inherent to the product or activity to be funded;
- D. costs of the activity or product to be funded as well as a brief description duly substantiated of the estimated profitability of the invested amounts;
- E. offer processing details;
- F. deadline for withdrawal of acceptance by the recipients of the offer, where applicable;

- G. Time and form for the transfer of the amounts raised, namely the mechanisms for subscription and for the refund of the amounts invested if the fundraising is higher than expected or in case the expected amounts are not raised and the offer does not provide the possibility of changing the conditions;
- H. Warning on the risk of partial or total loss of the invested amounts;
- I. Warning on the risk of not verifying the estimated profitability of the amounts invested;
- J. Warning on the liquidity risk or lack of a secondary market for financial instruments or credits subscribed by investors;
- K. Warning as to the fact that the activities and products to be funded are not subject to any authorization or supervision of CMVM ou by any other financial supervisor, nor do these entities approve the information disclosed on them;
- L. Warning on the fact that the investment is not covered by the Investor Compensation Scheme (except if resulting of financial intermediation and if verified the requirements of its application);
- M. Warning on the fact that the invested capital is not guaranteed under the Deposit Guarantee Fund;
- N. Warning on the fact that, in case of issuance of financial instruments, this will not be subject to CMVM' supervision nor this entity will approve the information disclosed by the beneficiary to the investors;
- O. Warning on the fact that, in case of loan grant, this will not be subject to the supervision of Banco de Portugal, nor this entity will approve the information disclosed by the beneficiary to the investors;
- P. Applicable tax legal regime;
- Q. Procedures to be adopted, including, without limitation, the destination of the amounts invested in the platform's current offer with the liquidation or the suspension, for any reason, of the managing entity activity;
- R. Procedures to be adopted to guarantee the continuity of the payment of the amounts invested in the platform's current offer with the liquidation or the suspension, for any reason, of the managing entity activity.

The key information for crowdfunding investor shall be disclosed to the investor prior to the acceptance of any offer and must be written in Portuguese language and must be clear (without technical terms) in order to be understood by the average investor.

#### **4.2.2 Crowdfunding platform from another EU country addresses companies / projects in Portugal**

Companies and projects that intend to benefit from crowdfunding through a crowdfunding platform operating in another EU country will only have to comply with Portuguese law requirements in the event the crowdfunding platform addresses Portuguese investors. In this case the company or project will have to comply with the disclosure information requirements referred in 4.1.1.2. above.

If a Crowdfunding platform from another EU country addresses Portuguese companies as investors, the crowdfunding legal regime shall not be applicable once the protective measures are only applicable to individual investors. According to the Portuguese Securities Code, the offers made to professionals are qualified as particular offers, which will only require a subsequent notification just for statistic purposes.

### 4.3 Outbound

#### **Portuguese Crowdfunding platform addresses foreign investors / companies / projects**

In the event a Portuguese Crowdfunding Platform addresses foreign investors and / or project companies it is not evident from the new Crowdfunding legal regime and further regulation which is the main criteria for crowdfunding platforms to fall under Portuguese regulatory requirements.

The protective measures established by Portuguese crowdfunding legal regime as well as in Portuguese Securities Code, are intended to protect individual investors and to guarantee that the decision to invest is made based in true, accurate and complete information. Each jurisdiction will have similar protection measures to be complied with when the intention is to address investors in that jurisdiction. However the portuguese platforms are bound by a legal regime that also establishes licence and compliance requirements which are applicable to all crowdfunding platforms incorporated and governed by Portuguese law, independently of the investors to be addressed or the companies / projects to be funded.

Therefore Crowdfunding Platforms incorporated and governed by Portuguese law must comply first of all with licence, compliance and information requirements of Portuguese Law and also with regulatory requirements of the investor's jurisdiction.

For that matter the Crowdfunding Platforms may require a licence before the supervision authority of each target jurisdiction or may choose to acquire a local company that already comply with local requirements.

### 4.4 Impact of EU regulation

#### 4.4.1 Prospectus rule / regimes

Most of the Portuguese start-ups are "sociedades por quotas" whose shares are no securities, therefore the Portuguese Securities Code and its prospectus regulation shall not be applicable.

#### 4.4.2 AIFM-Directive

AIFM Directive has a small impact in crowdfunding once the start-up companies that typically benefit from crowdfunding do not constitute Alternative Investment Funds (it is a company or a project that seeks investment for its general activity through crowdfunding platform).

#### 4.4.3 MiFID / MiFID II

The new Portuguese legal regime for crowdfunding establishes an exception of Crowdfunding from most regulatory requirements as well as simplified requirements to a local crowdfunding license.

#### 4.4.4 PSD / PSD II

The new legal framework of Crowdfunding does not prejudice the application and the supervision of Banco de Portugal whenever required. In fact the Crowdfunding legal regime and its regulation establish the need for the intervention of an entity duly authorized to provide payment services for the purpose of making the investment.

### 5 Lessons learned from Portuguese regulation for a possible harmonised European crowdfunding regulation

#### 5.1 Role Model (dos)

With the approval of the Crowdfunding legal regime and respective regulations the Portuguese legislator recognized the importance of the crowdfunding as an alternative form to fund start-up companies and small projects in Portuguese market. This recognition has been expressed by the approval of a simplified regime, free from the requirements established in the Securities Code.

This recognition has also been accompanied by the measures concerning to protect small investors from misleading investments which lead to new information and disclosure requirements as well as the establishment of investment limits for crowdfunding investments.

To build the basis for a possible European Crowdfunding regulation the following aspects can serve as role model:

- A. exception of Crowdfunding from most regulatory requirements (in particular prospectus requirement);
- B. information requirements to protect individual investors;
- C. lighter regulation for Crowdfunding platforms;
- D. unlimited investment amounts for "professional" investors and for individuals with an income equal or above EUR 70.000,00.

#### 5.2 Aspects that should be avoided ("don'ts")

Notwithstanding the above, the following aspects of the Portuguese Crowdfunding Legal Regime should not build the basis for a possible European Crowdfunding regulation:

- A. the concern of the Portuguese legislator to protect small investors is limited to the initial decision of investment, not including any protective measures applicable to minority shareholders during the course of life of the company, as information disclosure requirements or tag along clauses applicable in the event of sale of the shares by the majority shareholder.

## 6 Conclusion

During the last years, as the legal regime of Crowdfunding was not yet approved, only the Donations or Rewards Model and the Pre-sales Model have seen development among Portuguese Crowdfunding platforms.

However, the new legal regime and the recent regulatory framework approved by CMVM will certainly cause developments in this activity and will give confidence to the operators and investors to adopt such models.

As for the Crowdfunding cross border main legal barriers in UE, we stress the local frameworks that have been approved in the last years and that supersede the application of the UE legislation.

The key objective to develop the cross border crowdfunding in Europe should be the approval of a broad regulatory framework within UE, allowing project companies to offer financial instruments (loans and securities) to investors in any UE state without the need to comply with local prospectus regulation (of course within a limited amount of investment) but instead a simple information to enable the investor to make an informed investment decision.

We also consider to be essential to foresee the possibility to passport the crowdfunding licence obtained in Portugal (for example) to other UE countries without the need to start a new local licence procedure whenever the platforms intends to make offers in a different UE country.

Of course this two main objectives require an real convergence of the EU local laws concerning Crowdfunding legal regime.

## 7 Summary – Crowdfunding Regulation

|   |  |
|---|--|
| <b>Country</b>  | <b>Portugal</b>  |
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• Approval of specific legal regime applicable to Crowdfunding platforms</li> <li>• Approval of specific regulation from CMVM that is not yet in force due to the lack of a sanctions legal regime</li> </ul>   |
| <b>Current Crowdfunding regulation</b>                |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Crowdfunding Platforms operating under the Donation and Rewards Model (including pre-sales model) are subject to a prior notice to DGC</li> <li>• Crowdfunding Platforms in Portugal that offer services under Lending and Equity Models must be registered at Securities Exchange Commission (CMVM) and be subject to the supervision of this entity.</li> <li>• <b>License requirements</b> (two of the following financial requirements): <ul style="list-style-type: none"> <li>- Minimum share capital of EUR 50.000,00 totally paid up at the incorporation date;</li> <li>- Civil liability insurance or any equivalent guarantee to cover liability arising from professional negligence, that at least covers an amount of 1.000.000,00/per casualty and, globally, 1.500.000,00 for all the casualties occurred during one year;</li> <li>- A combination of the referred in (i) and (ii) in a form which results in a degree of protection equivalent to that conferred by any of the preceding paragraphs.</li> </ul> </li> <li>• <b>Investment Limits:</b> <ul style="list-style-type: none"> <li>- EUR 3.000,00 per offer; and</li> <li>- EUR 10.000,00 of total Crowdfunding investment/per year</li> <li>- These limits are not applicable to: (i) companies, (ii) to individuals with an income of EUR 70.000,00 or more or to qualified investors (according to article 30th of the Portuguese Securities Code).</li> </ul> </li> <li>• Information requirements towards CMVM and towards the investors to enable an informed decision-making.</li> <li>• The Regulation also establishes a maximum limit for fund raising through Crowdfunding per each 12 months (by a single offer or by the total of offers within the European Union: EUR 1.000.000,00 (one million euros).</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Description of the activity or product to be funded and the purpose of the funds to be raised;</li> <li>• Price of each unit to be subscribed or method to calculate such price;</li> <li>• Other information requirements to be established by Regulation of CMVM.</li> </ul>  |

|                                      |   |
|--------------------------------------|---|
| <b>AIFMD-regulation</b>              | <ul style="list-style-type: none"> <li>• A start-up company as the ones that typically benefit from crowdfunding does not constitute an Alternative Investment Fund.</li> </ul>   |
| <b>Payment service regulation</b>    | <ul style="list-style-type: none"> <li>• For the purpose of making the investment, the regulation also requires the intervention of an entity duly authorized to provide payment services.</li> </ul>   |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Portuguese Money Laundering Regime</li> </ul>  |
| <b>Regulatory barriers</b>           |   |
| <b>Inbound</b>                       | <ul style="list-style-type: none"> <li>• Foreign crowdfunding platforms must comply with regulatory license, information and compliance requirements.</li> <li>• Also the Project company that intends to collect funds through a crowdfunding platform in Portugal must comply with legal regime, mainly compliance and information requirement for investors protection.</li> </ul>                     |
| <b>Outbound</b>                      | <ul style="list-style-type: none"> <li>• Crowdfunding Platforms incorporated and governed by Portuguese law must comply with licence, compliance and information requirements of Portuguese Law and also with regulatory requirements of the investor's jurisdiction.</li> </ul>  |
| <b>Impact of EU regulation</b>       |   |
| <b>Prospectus regulations</b>        | <ul style="list-style-type: none"> <li>• Most of the Portuguese start-ups are "sociedades por quotas" whose shares are no securities, therefore the Portuguese Securities Code and its prospectus regulation shall not be applicable.</li> </ul>  |
| <b>AIFM-Directive</b>                | <ul style="list-style-type: none"> <li>• AIFM Directive has a small impact in crowdfunding once the start-up companies that typically benefit from crowdfunding do not constitute Alternative Investment Funds (it is a company or a project that seeks investment for its general activity through crowdfunding platform).</li> </ul>  |
| <b>MiFID/MiFID II</b>                | <ul style="list-style-type: none"> <li>• The new Portuguese legal regime for crowdfunding establishes an exception of Crowdfunding from most regulatory requirements as well as simplified requirements to a local crowdfunding license.</li> </ul>   |
| <b>PSD/PSD II</b>                    | <ul style="list-style-type: none"> <li>• the new legal framework of Crowdfunding does not prejudice the application and the supervision of Banco de Portugal whenever required.</li> <li>• In fact the Crowdfunding legal regime and its regulation establish the need for the intervention of an entity duly authorized to provide payment services for the purpose of making the investment.</li> </ul> |

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# Romania

## 1 Recent developments in the market of Crowdfunding in Romania

During the last years, there were the following significant developments in Romania regarding Crowdfunding:

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Most of the Crowdfunding platforms existing in the Romanian market continue to provide financing for small to medium-size companies. As such, the following platforms supported projects during the last years:

*Multifinantare*<sup>1</sup> platform remains an important Crowdfunding platform in Romania, supporting capital, creative and charity projects, managing to intermediate a distance phone and video-phone project amounting to EUR 800,000, in the past years.

*AngelConnect*<sup>2</sup> (a platform of Venture Connect Foundation) reports it has grown to become one of the most important entrepreneurial initiatives in Romania with the goal to expand and build a community of business angels.

*TechAngels*<sup>3</sup> reports to facilitate the development of tech businesses from South-Eastern Europe through investment, expertise and social connections.

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

As in the past years, no Romanian platform offers financing based on the Lending Model.

### 1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)

As in the past years, most of the Romanian Crowdfunding platforms promote the Donation or Rewards Model.

*Multifinantare* platform financed one project in the artistic sector in amount of EUR 1,500. Other projects are still pending, such as the organization of a virtual environment community expressing interest to participate in the acquisition of stocks, to be exploited by experts through the existing legal systems and institutions, amounting Lei 1,000,000 (approx. EUR 220,000).

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<sup>1</sup> <http://multifinantare.ro>

<sup>2</sup> <http://www.angelconnect.ro>

<sup>3</sup> <http://www.techangels.ro>

In the last 4 years, *Crestem Idei* platform has registered a total of 87 projects, out of which 43 were funded, some of them having an innovative character. *We are Here*<sup>4</sup> and *Pot si EU*<sup>5</sup> supported social, cultural, creative, instructive and technologic projects.

#### 1.4 Real Estate Crowdfunding / Renewable Crowdfunding

Currently Romania does not have any Crowdfunding platforms specialised in financing real estate or renewable energy projects.

However, there are some Crowdfunding platforms that occasionally present real estate and/or renewable energy projects in order to get the necessary financing.

Most of the proposed projects are made by individuals.

On the general platform *microfinantare.ro* was presented a project aiming to find financial support for the development of some energy efficient residential micro-districts. The project aimed to build energy-efficient houses with solar thermal panels for the heating as well as photovoltaic panels for indoor and outdoor lighting. However, the project has not obtained the targeted amount of 120,000 lei (i.e. approx. EUR 26,000) for the financing.

Also, a group of 70 students sought support to build a solar house on *crestemidei.ro* platform. The solar house was designed in order to build an energy efficient, sustainable and intelligent house that does not destroy the environment (EFdeN solar house). The purpose of the fund-raising was to collect 8,000 lei (i.e. approx. EUR 1,777).

#### 1.5 International approach

Up to now, we have no information about Crowdfunding platforms from other European countries intending to enter the Romanian market.

## 2 Recent developments regarding Crowdfunding regulation in Romania

Since December 2015, no legislative changes have been implemented in relation to Crowdfunding in Romania.

The draft proposal of the law for participatory financing development<sup>6</sup> (“Crowdfunding Project”) initiated by the Department for SME Business Environment and Tourism in September 2014 has not been adopted yet.

In case the Crowdfunding Project will be adopted in the current version, it will apply only to the Equity and Lending Model, requiring that the investor receives shares, stocks or receivables which produce interests for a period of time. The maximum amount that can be collected is EUR 1.000.000 for one project, provided that an individual cannot participate with

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<sup>4</sup> <http://www.we-are-here.ro>

<sup>5</sup> <http://potsie.ro>

<sup>6</sup> [http://www.cdep.ro/pls/proiecte/upl\\_pck2015.proiect?cam=2&idp=14923](http://www.cdep.ro/pls/proiecte/upl_pck2015.proiect?cam=2&idp=14923)

more than EUR 1,000 per project and EUR 5,000 cumulated per projects on each platform within a 12 month-period.

The entities operating Crowdfunding platforms shall have a minimum share capital of EUR 25,000, shall maintain professional liability insurance and shall be registered with the register held by the Romanian Financial Supervisory Authority (“FSA”).

The “all or nothing” principle will guide the financing, which means that if the financing is not raised, the amounts shall be reimbursed to the investors. The initial contribution of the developer shall be of minimum 5%.

It is expected that a tax exemption shall apply to dividends returning to the business angels (without exceeding the amount of the loan granted) and to the exiting package.

### 3 Current Regulation of Crowdfunding in Romania

There are numerous laws that might potentially apply to the Equity and Lending Model, depending on the finance structure used by the Crowdfunding platform, including:

- rules regarding intermediation, solicitation and distance selling, irrespective of the model used by the platform;
- banking regulation, when the funding takes the form of loans;
- securities regulation, when equity investments (or investments in debt securities) are requested;
- regulation of payment services, when funds are paid in through the Crowdfunding platform;

Also, other regulations may apply, such as anti-money laundering, combatting the financing of terrorism laws.

The Donation/Reward Model usually falls well outside the definition of financial services, financial or investment instruments and therefore falls outside the restrictive aspects of financial regulation.

#### 3.1 Banking / Financial Service licence requirements

##### 3.1.1 Equity Model / Lending Model

The lending activity in Romania, if ordinarily conducted, is subject to supervision by the National Bank of Romania (“NBR”) and may be carried out only by financial institutions, as well as non-banking financial institutions (“IFN”).

The main regulation applicable to financial institutions is the Government Emergency Ordinance no. 99/2006 regarding credit institutions and capital adequacy as further amended, (the “Banking Law”), as well as a series of laws, ordinances and decisions, as well as special regulations issued by NBR. Also, the operation of IFN acting in the field of granting loans (such as leasing companies and non-banking financial institutions) is subject to dispositions of Law no. 93/2009 regarding non-banking financial institutions (“IFN Law”).

In this respect, any entity providing loans (including leasing companies and non-banking financial institutions) must be licenced or, as the case may be, registered with the NBR and therefore, Crowdfunding platforms in Romania do not provide financing pursuant to this lending regulation.

However, currently financing pursuant to the Lending Model is theoretically possible, provided that the investor is a regulated entity and the initiator of the project complies with the applicable requirements of the financial institution and the general regulations applicable to lending activity.

In case the Crowdfunding Project becomes law, it shall apply to the Lending Model, requiring the Crowdfunding platform is registered with FSA and provides certain information to the users. In this respect, the Crowdfunding Project defines the participative loan as a loan made through alternative financing platforms, under which receivable titles are issued granting the investors the right to interest during the period until final maturity.

Crowdfunding platforms currently operating in Romania doesn't fall within the scope and limits of the Banking Law or the IFN Law.

### **3.1.2 Donations or Rewards Model**

The donations model is not regulated.

## **3.2 Prospectus requirements**

### **3.2.1 Equity Model/ Lending Model**

According to Romanian law, public offering of securities as well as the admission to trading on a regulated market of company shares is subject to the approval of a prospectus by the FSA, pursuant to Law no 297/2004 on capital markets ("Capital Markets Law"). In order to be listed on the capital markets, a company shall be a joint stock company or a public company (i.e. one per cent of its stocks is owned by public). The Capital Markets Law applies to offers of securities in Romania, irrespective of where the issuer is located.

However, preparation and publication of a prospectus is not required for the offer of securities (i) addressed solely to qualified investors and/or (ii) addressed to fewer than 150 natural or legal persons other than qualified investors for each Member State; and/or (iii) addressed to investors who acquire securities each the equivalent in RON of EUR 100.000 at the most, for each separate offer; and/or (iv) whose denomination per unit is the equivalent in RON of EUR 100.000 at the most; and/or (v) whose total amount in the EU is lower than the RON equivalent of EUR 100.000, calculated for a period of 12 months<sup>7</sup> as well as in relation to certain securities (such as securities offered, allotted or to be allotted in connection with a merger or division, for dividends paid in the form of shares to existing shareholders in the

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<sup>7</sup> Pursuant to article 15 of FSA Regulation no 1/2006.

same class as those which give right to such dividends) and in other cases specified by regulations issued by ASF, under the law.

The Capital Market Law defines securities as shares in companies and other securities equivalent, traded on the stock market, bonds and other debt securities, including government securities with maturity more than 12 months, negotiable on the capital market as well as any other securities normally dealt in, giving the right to acquire any such transferable securities by subscription or exchange, giving rise to a cash settlement, excluding instruments of payment. Therefore, a donation, even with financial return, will not be considered to fall within the public-offering rules.

### **3.2.2 Donations or Rewards Model**

Donations or Rewards Model does not fall within the concept or limits of the Capital Markets Law.

## **3.3 Regulation of Crowdfunding under the AIFMD regime**

### **3.3.1 Equity Model/ Lending Model**

Romania transposed the Directive 2011/61/EU of the European Parliament and of the Council on Alternative Investment Fund Managers („AIFMD“) by adopting the Law no. 74/2015 on managers of alternative investment funds („Law on alternative investment fund managers“).

This law applies to entities established in Romania whose main business activity is the management of one or more alternative investment funds („AIF“), irrespective of whether the AIF is established in Romania, in another Member State or in another third country, including investment compartments thereof, which raise capital from at least two investors in order to place the funds in accordance with a defined investment policy for the benefit of those investors.

This law also applies to alternative investment fund managers („AIFM“) established in third countries that manage and/or distribute equities of one or more AIF established in Member States or third countries for which Romania is a reference member state of that AIFM.

Romanian AIFMD regulation does not apply to operating companies outside the financial sector which do not invest according to a defined investment policy.

Do to the fact that an operator of a Crowdfunding platform does not raise capital from investors for its own business is should not qualify as an AIF.

However, if a Crowdfunding undertaking intends to structure its operation as an AIF it must comply with the requirements of Law no. 74/2015 in respect of licencing and regulatory requirements applicable to the AIFs and their managers.

### 3.3.2 Donations or Rewards Model

Donations or Rewards Model does not fall within the concept or limits of the Law on alternative investment fund managers.

### 3.4 Licence under the Payment Services Directive

Payment services in Romania are mainly regulated by the Government Emergency Ordinance no. 113/2009 regarding payment services (“Payment Services Law”), which transposed the Payment Services Directive 2007/64/EC, as well as by the provisions of the NBR Regulation no. 21/2009 regarding the payment institutions.

In Romania, payment services may be provided by payment services providers, including credit institutions, entities issuing electronic money and payment institutions, authorized by the NBR. The authorization to provide payment services is not applicable to entities licenced as deposit-taking banks, as e-money issuers or as IFN.

A payment institution authorized in another EEA member state can use the EEA passport system under the payment Services Directive 2007/64/EC by making a notification in its home member state in accordance with the procedures in that member state.

Pursuant to the information available to us, no Crowdfunding platform in Romania currently provides payment services. However, should the investors pay their investment amounts to the operator of the Crowdfunding platform who then passes the funds to the entrepreneur, such transfer of funds could occur and the operator of the Crowdfunding should be licenced as a payment services provider.

As an alternative, to avoid licencing requirements the operator of a Crowdfunding platform may use an external provider for processing payments rather than acting itself as a services provider.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

#### 3.5.1 Regulation of marketing and distance selling

Marketing and distance-selling (including through web-sites, telephone, fax, e-mail) are subject to dispositions of Law no. 365/2002 on electronic commerce, Government Emergency Ordinance no. 34/2014 on consumers’ protection in contracts concluded with professionals, which transpose the Directive no. 2011/83/UE regarding the consumer rights, and Government Ordinance no. 85/2004 on consumers’ protection in case of distance contracts for financial services as well as the Consumer Code.

Furthermore, if the financed company is a professional, we could imagine a hypothesis in case of the Rewards Model where the investor receives goods in exchange to its contribution

to a project. In this respect, the obligations provided in Government Ordinance no. 21/1992 regarding the consumer protection may apply.

To avoid sanctions imposed by the National Authority for Consumer Protection (“NACP”), Crowdfunding platforms in Romania shall comply with the restrictions set by the marketing and distance-selling regulations.

### **3.5.2 Anti-money laundering (“AML”) requirements;**

According to the Law no. 656/2002 on preventing and sanctioning money laundering and instituting measures for preventing and fighting against financing the acts of terrorism („Law no. 656/2002“), financial institutions (such as banks, institutions issuing consumer or commercial credit, mortgage / real estate lenders, leasing companies); financial investment service providers as well as individuals or corporate traders of goods and/or services with a minimum EUR 15,000 cash turnover<sup>8</sup> must observe the AML requirements, including rules on client identification, where applicable, identification of the beneficial owner and taking risk-based and adequate measures to verify his identity, obtaining information about the purpose and intended nature of the business relationship as well as conducting ongoing monitoring of the business relationship. Any transaction suspected of involving money, laundering or terrorist financing must be reported to the NOPCML at once<sup>9</sup>.

In this respect, operators of Crowdfunding platforms falling under the dispositions of Law no. 656/2002 must comply with AML rules and perform anti money laundering or terrorist financing checking.

### **3.5.3 Data Protection**

A personal data operator gathering information related to an individual either identified or identifiable (namely an individual that may be directly or indirectly identified by reference to a identification number or to one or several specific factors corresponding to his/her physical, physiological, psychological, economic, cultural or social identity) must obtain the explicit and unequivocal consent of the individual concerned and register with the National Authority for the Surveillance of Personal Data Processing (the “NASPDP”).

Since the Crowdfunding platform may hold sensitive information about its users, it should notify the NASPDP, directly or through a representative, before any processing of personal data. Moreover, if the personal data will be transferred outside Romania, an additional approval must be obtained from the NASPDP in respect of the transfer abroad.

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<sup>8</sup> Pursuant to article 10 of Law no 656/2002.

<sup>9</sup> Article 3 paragraph (6) of Law no 656/2002.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

As the Crowdfunding activities are not regulated in Romania, currently there is no licence to be required to a foreign platform addressing Romanian investors.

However, lending activity may be carried only by financial institutions, as well as IFNs, subject to Banking Law or, as the case may be, IFN Law.

Also, the Capital Markets Law applies to offers of securities in Romania, irrespective of where the issuer is located.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addresses Romanian investors

As the Crowdfunding activities are not regulated in Romania, currently there is no licence to be required to a foreign platform addressing Romanian investors. Should such platform choose to establish a head office in Romania or the effective place of management in Romania, the Capital Markets Law may be applicable.

##### 4.2.1.1 Crowdfunding platform

###### (1) The platform holds a MiFID licence in another EU member state

The Markets in Financial Instruments Directive (“MIFID”) is, starting November 2007, the framework of European Union (EU) legislation for:

- A. investment intermediaries that provide services to clients around shares, bonds, units in collective investment schemes and derivatives (collectively known as ‘financial instruments’); and
- B. the organised trading of financial instruments.

Building on the rules already in place, the second Markets in Financial Instruments Directive („MIFID II“) was published in the EU Official Journal on 12 June 2014, and is designed to take into account developments in the trading environment since the implementation of MIFID in 2007 and, in light of the financial crisis, to improve the functioning of financial markets making them more efficient, resilient and transparent.

The EU member states have to implement MIFID II into their national law until 3 July 2017 and all market participants have to apply the new rules from January 2018.

However, Romania did not transpose MIFID II yet in its internal legislation.

Typically, in Romania start-up companies, as well as project companies are structured in the legal form of a limited liability company (S.R.L.), due to the fact that this company form can be easily established (smaller share capital, of RON 200, i.e. approx. EUR 45) and handled.

Shares in limited liability companies (S.R.L.) are not tradable and transfer thereof usually requires the approval of all or a certain number of existing shareholders of the company. As a consequence, shares of a limited liability company are not financial instruments within the meaning of MIFID and also these companies are not covered under the scope of MIFID.

The Banking Law covers, inter alia, transactions in own account, as well as in the client's account, with investment products (including financial instruments, as well as shares of stock option companies, bonds etc.)

Therefore, the scope of the Banking Law falls within the scope of MIFID covering also investment products.

Generally, in case the foreign platform holds a licence under MIFID in another EU member states, being authorised and supervised by the competent authority of the Member State may supply in Romania, under the authorisation granted by the home Member State the same investment services and activities, based on the principle of the free circulation of services, without being required to obtain any authorisation from the Romanian authorities.

As a general rule, a foreign Crowdfunding platform with a foreign MIFID licence can conduct business in Romania without applying for a licence and without having a presence in Romania based on so-called notification procedure ("EU Passport").

However, in case the Crowdfunding platform holds a MIFID licence and intends to address Romanian investors, as a principle, the MIFID licence should be sufficient for providing financial services covered by the MiFID licence.

### **(2) The platform has no MiFID licence**

In case the foreign platform does not hold a licence under MIFID in its home Member State but it carries out any financial or investments services that fall within the concepts regulated by the Romanian Capital Markets Law, a licence has to be obtained from the FSA.

Generally, Romanian law does not apply to foreign legal persons which are not resident in Romania.

### **(3) Other regulation**

Data protection law could apply even to a foreign actor, processing data of Romanian investors (individuals only) but only in case the foreign actor owns any means of data processing on the Romanian territory.

Since the foreign Crowdfunding platform does not have its place of business in Romania it cannot be subject to AML rules and perform anti money laundering or terrorist financing checking under Law no. 656/2002 (but may be subject to the local anti-money laundering regulation of its home Member State).

#### **4.2.1.2 Company /project**

##### **(1) Romanian prospectus regulation**

Generally, Romanian prospectus regulations apply only to activities and operations carried out on the Romanian territory that fall in the categories regulated by Romanian Capital Markets Law.

However, Capital Markets Law provides for the possibility, in case of a foreign operator, complying with the prospectus regulations under its home Member State, to make a public offer in Romania or to request admission of the securities to trading on a regulated market in Romania using the prospectus approved in its home Member State.

Although no approval or administrative proceedings are required with regards to the prospectus, the foreign operator shall have the obligation to notify in this respect the FSA, as well as the European Securities and Markets Authority (“ESMA”).

##### **(2) Other regulation**

Romanian AML rules are not applicable to the foreign issuing entities companies / projects – since they or any branches are not based in Romania.

#### **4.2.2 Foreign Crowdfunding platform addresses Romanian companies / projects**

##### **4.2.2.1 Crowdfunding platforms**

##### **(1) Licence obligations**

As mentioned above, Romanian law does not provide for a specific licence to be obtained in order to operate a Crowdfunding platform.

Generally, Romanian law is applicable only to companies which are resident in Romania.

##### **(2) Other financial regulation**

Usually, Romanian companies/ projects do not issue equity-based securities in the Crowdfunding market, generally being structured as limited liability companies (S.R.L.), whose shares do not constitute securities.

However, as a general rule the information and compliance obligation may be applicable to the foreign Crowdfunding platform in case it provides services related to debt-based securities (e. g. bonds) which also constitute securities. In this case the foreign Crowdfunding platform might be subject to other Capital Markets Law.

In case the company / project does not offer securities, but other investments (shares / loans) – as a general rule – there are no additional financial regulations applicable to the foreign Crowdfunding platform.

Further, the foreign Crowdfunding platform is not subject to German AML regulations.

#### **4.2.2.2 Company / project**

##### **(1) Prospectus regulation**

Romanian Capital Markets Law provides for the obligation to comply with prospectus requirements only in case the traded securities are offered in Romania and fall within the concepts regulated by the Romanian Capital Markets Law.

Usually, the companies presented on the Crowdfunding platforms are start-ups, organized as limited liability companies and their shares cannot be traded on regulated markets in accordance to Capital Markets Law.

In order that such companies be allowed to trade securities (either stocks or bonds) they have to reorganize as stock companies complying with the provisions of companies' law concerning this form of doing business. Also, in this case the companies intending to trade securities have to comply with all information and regulatory provisions regarding the listing on the organized markets.

##### **(2) Other regulation**

The issuing entities – Romanian companies / projects – generally are within the areal applicability of AML regulations since they are based in Romania. However, they do not constitute an obliged person within the meaning of the Law no. 656/2002.

### **4.3 Outbound**

In this situation, a Romanian Crowdfunding platform enters European markets and addresses foreign investors.

#### **4.3.1 Romanian Crowdfunding platform addresses investors in another EU country**

##### **4.3.1.1 Crowdfunding platform**

###### **(1) Licence Obligations**

As mentioned above, Romanian law does not provide for a specific licence to be obtained in order to operate a Crowdfunding platform.

However, Romanian regulatory law may apply to the Romanian operator of the Crowdfunding platform offering traded securities, provided that such securities are offered in Romania. Therefore, even there is no licence to be obtained for the Crowdfunding activity, the platform shall comply with all financial regulations.

###### **(2) Other financial regulation**

As a general rule the Romanian Crowdfunding platforms provide investment broking and therefore, they do not constitute an obliged person under the Romanian AML regulations.

#### **4.3.1.2 Company / project**

##### **(1) Licence Obligations**

Romanian prospectus regulations, under the Capital Markets law applies only in case the activities carried out by the Romanian based actor are operated on the Romanian territory.

As already mentioned the Romanian Capital Markets law regulating the prospectus conditions shall apply only to the operations that falls under this law.

##### **(2) Other financial regulation**

As a general rule the Romanian Crowdfunding platforms provide investment broking and therefore, they do not constitute an obliged person under the Romanian AML regulations.

#### **4.3.2 Romanian Crowdfunding platform addresses foreign companies / projects**

##### **4.3.2.1 Crowdfunding platform**

##### **(1) Licence obligation**

Romanian law does not provide for a specific licence to be obtained in order to legally perform Crowdfunding activities.

However, if the Crowdfunding platform is a Romanian resident is should comply with Romanian regulatory provisions comprised by Capital Markets Law, if applicable in case of trading securities (either stocks or bonds).

##### **(2) Other financial regulation**

As a general rule the Romanian Crowdfunding platforms provide investment broking and therefore, they do not constitute an obliged person under the Romanian AML regulations.

##### **4.3.2.2 Company / project**

##### **(1) Licence obligation**

In case the foreign companies/ projects would offer either equity-based, either debt-based securities prospectus regulation under Capital Markets Law is applicable to these financial products offered on the Romanian territory.

Also, foreign companies / projects issuing securities in Romania might be subject to additional information or compliance regulations as per Romanian Capital Markets Law.

##### **(2) Other financial regulation**

As a general rule the Romanian Crowdfunding platforms provide investment broking and therefore, they do not constitute an obliged person under the Romanian AML regulations.

## 4.4 Impact of EU regulation

### 4.4.1 Prospectus rule / regimes

In Romania, the prospectus regimes are regulated under Capital Markets Law and provides for specific conditions for a public offering of securities (e.g. shares in stock companies, other securities equivalent traded on the stock market, bonds and other debt securities).

The European legislation covering transferable securities within the meaning of MIFID has been implemented within the Romanian Capital markets law. MIFID II is not implemented yet in Romania.

The implementation of MIFID II will impose a number of legislative changes at the level of primary legislation. Thus, the provisions of Capital Markets Law will be amended with regards to the intermediaries' regime, regulated markets and market operators.

However, taking into account that generally the companies / projects that are presented on the Crowdfunding platforms are start-ups companies, they are usually organized as limited liability companies (the simplest and cost-effective structure) which shares are not tradable according to capital markets regulations. Therefore, in such case the impact of the European regulations is not significant.

### 4.4.2 AIFM Directive

Romanian AIFMD regulation which transposed the AIFM Directive does not apply to operating companies outside the financial sector which do not invest according to a defined investment policy.

However, if a Crowdfunding undertaking intends to structure its operation as an AIF it must comply with the Romanian AIFMD requirements in respect of licencing and regulatory requirements applicable to the AIFs and their managers.

### 4.4.3 MIFID / MIFID II

As already mentioned above only MIFID Directive has been implemented yet in the Romanian legislation, by adopting the Capital Markets Law.

In order that such legislation have an impact on the Crowdfunding platforms (equity model only) the operator of such platforms has to be organized as stock companies and comply with the specific conditions of Capital markets regulations.

### 4.4.4 PSD / PSD II

The Payment Service Directive (PSD) was implemented in Romania by adopting the Payment Services Law in 2009, while PSD II is to be implemented until January 2018.

Pursuant to the information available to us, no Crowdfunding platform in Romania currently provides payment services.

Romanian harmonized legislation on payment services could impact the operator of the Crowdfunding platform in case the investors pay their investment amounts to the operator of the Crowdfunding which then passes the funds to the target company or project.

In order to avoid licencing requirements, the operator of a Crowdfunding platform may use an external provider for processing payments rather than acting itself as a services provider.

#### 4.5 Summary

Up to the date, Romania did not implement any specific Crowdfunding regulation and as a consequence, the general law, mainly, harmonised with the European legislation, applies (e.g. the transposed directives: MIFID, AIFM, PSD).

Therefore, from a Romanian perspective, there are not many regulatory barriers that could hinder Cross-borders activities of Crowdfunding platforms.

However, lack of specific regulation together with some unclear definitions of the financial instruments types, could actually be a real barrier for the cross-boarding Crowdfunding operations, in case Romanian authorities will find difficult to decide which operations would fall within a specific regulated regime (such as Capital Markets Law, Banking Law, IFN Law or AIFM regulations).

### 5 Lessons learned from Romania's regulation for a possible harmonized European Crowdfunding regulation

The small number of operative Crowdfunding platforms in Romania did not raise the burning need for adopting a regulation in this respect until now. However, the Crowdfunding Project is expected to create an important and secure frame for intermediation between companies and the investors.

As such, it is welcomed that the new proposed regulation imposes the Crowdfunding platforms acting according to the Equity Model to meet certain financial and ethical standards, as well as to be subject to regulatory requirements.

However, the licencing and prospectus requirements should rather be excepted and nevertheless not included to a possible European regulation as regards Crowdfunding platforms.

### 6 Conclusion

Some of Crowdfunding platforms which already existed in Romania have developed in the last years and managed to intermediate more projects. Other platforms appeared while other closed their activity.

Our research regarding the activity of Crowdfunding in Romania indicates that 90% of the projects are financed through donations, with a few projects in the field of innovation.

Currently there are a few Equity Model projects. The Lending Model is inexistent.

From the technologic point of view, Romania benefits from a high technology which makes it easier for the operators of Crowdfunding platforms to use the Lending Model.

However, the capital raised from the investors is still low and the main funds are obtained from non-governmental organisations and private companies/individuals.

Also, there is a lack of collaborative movement which is essential in the Crowdfunding activity as well as investment culture. Most of the investors tend to invest their money directly in the collector fund, without contacting platform operators to intermediate the transfer.

An improved legislation at European level could encourage a development of both internal and cross-border Crowdfunding market.

In this respect, it is necessary a clear regulation off all financial instruments that can be used in Crowdfunding.

## 7 Summary – Crowdfunding Review

| Country   | <b>Romania</b>   |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• a law project regarding participatory financing development is in legislative procedure before the Romanian Chamber of Deputies;</li> <li>• currently there is no specific regulation in force with regards to Crowdfunding;</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | Directive 2011/61/EU regarding alternative investment fund managers has been transposed in the Romanian legislation by adopting Law no. 74/2015 on managers of alternative investment funds;   |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Public offering of securities is subject to the approval of a prospectus by ASF with several exceptions.</li> <li>• Trading of shares of a company on regulated markets is subject to the approval of a prospectus by ASF. This rule shall apply to the Equity Model.</li> </ul>  |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• typical operator of a Crowdfunding platform does not qualify as an AIF;</li> <li>• the AIFM law could apply in case the structure operated by the platform or the project company falls within the legal concept of an AIF;</li> </ul>  |
| <b>Payment service regulation</b>                     | Providers of payment services need an authorization by NBR. Authorization by NBR is not applicable to entities licenced as deposit-taking banks, e-money issuers or IFN.   |
| <b>Consumer credit regulation</b>                     | <ul style="list-style-type: none"> <li>• Currently in Romania, no Crowdfunding platform offers financing pursuant to the lending regulation; in principle, any financial institution which finances its clients for development of an activity/business by public issuance of stocks/bonds falls under the Banking Law or NFI Law requirements;</li> <li>• In order to avoid breaching the requirements on lending activity, some Crowdfunding organisations act as intermediaries between the initiator of the project and the banks and/or NFI.</li> </ul> |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Regulations of marketing and distance selling;</li> <li>• Anti-money laundering regulations;</li> <li>• Data protections regulations.</li> </ul>  |
| <b>Regulatory barriers</b>                            |  |
| <b>Inbound</b>  | <b>Foreign Crowdfunding platform addresses Romanian investors</b>  |

|                                 |  |
|---------------------------------|--|
|                                 | <ul style="list-style-type: none"> <li>• Crowdfunding platform: no licence applicable under Romanian law; in case the platform benefits of MIFID licence in its home Member State there is no need to apply for a similar licence in Romania (however a notification procedure is required);</li> <li>• Company / project: Romanian prospectus regulation applies, if required by law; however, as exception is provided in case the foreign platform complies with prospectus regulations in its home Member State (the notification procedure will be necessary);</li> </ul> <p><b>Foreign Crowdfunding platform addresses Romanian companies/projects</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform: there is no specific Crowdfunding licence required;</li> <li>• Company / project: Capital Markets Law is applicable for the operations carried out on Romanian territory, if the case;</li> </ul> |
| <b>Outbound</b>                 | <p><b>Romanian Crowdfunding platform addresses foreign investors</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform: no licence applicable under Romanian law in respect of Crowdfunding; however Romanian regulatory law will apply as the platform is a Romanian resident;</li> <li>• Company / project: Romanian prospectus regulation applies, if required by law for the operations carried out on Romanian territory.</li> </ul> <p><b>Romanian Crowdfunding platform addresses foreign companies/projects</b></p> <ul style="list-style-type: none"> <li>• Crowdfunding platform: there is no specific Crowdfunding licence required; Romanian legislation applies to the platform;</li> <li>• Company / project: Capital Markets Law is applicable for the operations carried out on Romanian territory, if the case.</li> </ul>   |
| <b>Impact of EU legislation</b> |  |
| <b>Prospectus regulations</b>   | MIFID has been transposed in Romanian law by adopting Capital Markets Law; however, the impact of the European legislation is not significant for most of start-up organized as limited liability companies.   |
| <b>AIFM- Directive</b>          | AIFM -Directive, transposed in Romanian law, could impact on the operator of a Crowdfunding platform only in case it is structured as an AIF or as an AIF manager.   |
| <b>MIFID / MIFID II</b>         | MIFID II was not implemented yet in Romanian legislation; MIFID implemented by adopting the Capital Markets law can have an impact in case platforms organized as stock companies comply with the specific conditions in this respect.   |
| <b>PSD /PSD II</b>              | PSD II was not implemented yet in Romanian legislation. PSD could have an impact in case the investors pay their investments amounts directly to the operator of the Crowdfunding platform.  |

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# Slovakia

## 1 Recent developments in the market of Crowdfunding in Slovakia

### 1.1 Introduction

In the last 6 years, there has been a significant increase of start-up investment in Slovakia. There are a notable number of funds, investors, incubator & co-working platforms and business angels in the Slovak start-up community. Previously, Slovak start-ups and businesses preferred to use well-established foreign Crowdfunding platforms (e.g. *Kickstarter* or *Indiegogo*) or newly established Crowdfunding platforms in the Czech Republic (e.g. *HitHit*) while at the same time Crowdfunding as such was not a common sight in Slovakia.

However, in the last two years Slovakia witnessed the arrival of both purely domestic as well as foreign Crowdfunding platforms. It seems that success stories of some of the Slovak companies on the international Crowdfunding platforms (e.g. “Cool Charge” on *Kickstarter*) are helping to change the traditionally conservative attitude of the Slovak market towards Crowdfunding and investing in general. Although there are now several Crowdfunding platforms operating in Slovakia, most of them are focused on charitable activities and still only a few have potential to positively impact the business. Another trend in Slovakia seems to be arrival of already established Czech Crowdfunding platform like *HitHit*. In fact, Czech Crowdfunding platforms might be the first ones to deal with cross-border regulatory aspects of Crowdfunding in Slovakia. Some of the Czech Crowdfunding platforms are only available for Slovak market due to the language and geographical proximity but some of them are actively campaigning in Slovakia. Just to mention a few Crowdfunding platforms currently active in Slovakia:

- A. *Crowdberry* – Slovak Crowdfunding platform developing its own equity model that strategically partners with Tatra Banka Private Banking ([www.crowdberry.sk](http://www.crowdberry.sk))
- B. *Conda Crowdinvesting* – operating as a Slovak subsidiary of well-established Austrian Crowdfunding platform Conda Crowdinvesting Europe which seems to operate based on equity model ([www.conda.sk](http://www.conda.sk));
- C. *Zlty Melon* – Slovak P2P lending platform (<https://www.zltymelon.sk/>);
- D. *Zinc Euro* – Slovak P2P lending platform (<https://www.zinceuro.sk/>);
- E. *HitHit* – a well-established Czech Crowdfunding platform focusing on creative industry that started to be visible in Slovakia via its Slovak domain ([www.hithit.com/sk/home](http://www.hithit.com/sk/home));
- F. *Startovac* – Czech start-up Crowdfunding platform operating on lending model ([www.startovac.cz](http://www.startovac.cz));
- G. *Marmelada* – Slovak Crowdfunding platform supporting mainly creative and artistic projects ([www.marmelada.sk](http://www.marmelada.sk));
- H. *Dobra Krajina* – mainly a charity and volunteering platform that also offers an option to donor certain causes, people or matters ([www.dobrakrajina.sk](http://www.dobrakrajina.sk));

- I. *Dakujeme* – a charity fundraising platform supported by daily news SME ([www.dakujeme.sme.sk](http://www.dakujeme.sme.sk));
- J. *Darujme* – a donor model Crowdfunding platform that has already supported more than 250 organisations with donations worth of EUR 1.5 million ([www.darujme.sk](http://www.darujme.sk));
- K. *WellGiving* – a fundraising philanthropy group that runs number of Crowdfunding projects for their corporate clients (<http://www.wellgiving.sk/>).

In addition, there has already been a Crowdfunding platform that has ceased to operate in Slovakia (*Ideasstarter*) from unknown reasons.

Overall, the Crowdfunding in Slovakia has been historically seen a method of charity support thanks to several well-established foundations and NGOs. Therefore, the majority of Crowdfunding platforms are still based on donations and rewards model. Only recently, Crowdfunding has started to be seen as a business case for Crowdfunding platforms on one side and easy access to resources for entrepreneurs on the other side. Most of these Crowdfunding platforms now charge the company/project a fee of app. 3-10 per cent from the raised/collected funds for their services. From the investor side, most of the available Crowdfunding platforms operate on donations and reward model. We have identified only two Crowdfunding platforms in Slovakia operating based on the equity model and two P2P lending platforms operating under the lending model.

However, to the best of our knowledge, there are no publicly available and verified data regarding the size of the Crowdfunding market in Slovakia that would allow us to conclude what business model attract the most investment in Slovakia.

## **1.2 Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)**

Offering of securities by the company would constitute a public offer of securities under the Act No. 566/2001 Coll., on Securities and Investment Services (the “Securities and Investment Services Act”) implementing the MIFID I Directive and Prospectus Directive among others. A public offer of securities is usually subject to the obligation to publish a prospectus. The issuer may be exempt from such obligation, if the total value of shares issued within the EU would be less than EUR 100,000 calculated over the period of 12 months with certain other standard exemptions exist, but these are unlikely to apply in this case).

If the Crowdfunding platform facilitates the offering of securities, this activity constitutes an investment service. Subject to Section 54 of Securities and Investment Services Act, the Crowdfunding platform would have to obtain a licence to provide such investment services from the National Bank of Slovakia (the “NBS”). There are no specific exemptions from this obligation available to Crowdfunding platforms. However, the Securities and Investment Services Act allows passporting of the relevant licence from other EEA Member States.

*Crowdberry* – the main Slovak Crowdfunding platform – refers to itself as an equity investment platform and develops its own equity model in the Slovak regulatory environment. Second Crowdfunding platform operating based on the equity model is *Conda Crowdinvesting* that benefits from experience of its founders from Austria. However, as mentioned above, we are not able to confirm the amount of investment channelled through these Crowdfunding platforms up to date.

Although we have not identified other Crowdfunding platforms based on equity model, there are many start-up incubators, hubs or co-working centres in Slovakia which serve as a channel for investor introduction. In terms of private investment, the equity model still plays a major role in Slovakia, however, it seems that due to the various complex regulatory obstacles equity model is not evolving into a popular Crowdfunding model in Slovakia as it could.

### **1.3 Lending Model (individuals lend money to a company or a project in report for repayment of the loan and interest on their investment)**

In the Lending Model a person lends certain amount of money and expects to receive the principal with interest. Two legal frameworks are in theory applicable, depending on the nature of lenders. Lending is in general a regulated business that may not be performed without a licence under the Slovak Banking Act. It is however possible to be engaged in lending services based on a simple ‘trade licence’, if performed in a non-banking manner – i.e. using personal funds of the lender. If the respective loan agreement is concluded by entrepreneurs who are acting within their regular business, upon the entrepreneurs’ own responsibility, independently with the intention to make profit, the loan would be governed by the Act No. 513/1991 Coll., the commercial code, as amended (the “Commercial Code”). Interest is a mandatory element of such relationship, which may or may not be mentioned expressly, but will nonetheless accrue.

By contrast, if the loan is provided as a one-off investment by a private person, i.e. is not provided systematically as a business of the lender, the relationship will be governed by Act No. 40/1964 Coll., the civil code, as amended (the “Civil Code”). Interest may or may not be agreed under such relationship and its regulation under the Civil Code is rather liberal.

Depending on the manner in which the Crowdfunding platform would function, it may be classified as an agent, assisting in the conclusion of the loan agreement between the parties. A simple trade licence for such activities would be required. However, it has to be noted that there is not sufficiently clear line between the scope of the relevant simple trade licences of ‘economic, business and organisational advisory services’ and ‘brokering loans or borrowings from funds received exclusively without a public call’ and regulated activities such as provision of investment advisory or ancillary services under the Securities and Investment Services Act.

We have identified at least two P2P lending platforms in Slovakia which operate on the basis of lending model.

#### **1.4 Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

Two alternatives are in theory possible. The first one would be via the conclusion of donation agreement. Pursuant to Section 628 of Civil Code, the donator transfers something or promises to transfer something free of charge and the donee accepts such gift or promise. The donation agreement has to be in written form, if the gift is real estate, or if the gift is not transferred at the time of the agreement's conclusion.

A second option would be via the collection of funds. A Crowdfunding platform which would organise collection of funds under donations or rewards model would have to obtain a simple trade licence. The requirements of a relatively new Act No. 162/2014 Coll. on public collections (the "Public Collections Act") may apply to the donations model. However, the public collections, as defined in the Public Collections Act and as more explained in point 3.5.1 below are restricted to publicly beneficial purposes only.

Most of the non-charitable Crowdfunding platforms operate or provide their services in Slovakia under the donations or reward model.

#### **1.5 Real Estate Crowdfunding / Renewable Crowdfunding**

Currently, we do not see any indication of real estate or renewables Crowdfunding as an emerging trend in Slovakia. As mentioned above, Crowdfunding has mostly either charitable/community or start-up support purpose in Slovakia.

#### **1.6 International approach in Slovakia**

We are aware of the increasing appetite of North-American Crowdfunding platforms for the European market. However, although this trend might already be visible at the western markets of the EU, Slovakia only witnesses an increased appetite by Czech Crowdfunding platforms. This is of no surprise since Slovak & Czech markets are very much interconnected by business, mentality, language and history. Theoretically, more Crowdfunding platforms from neighbouring countries might follow (mainly from Austria and Poland) but at the moment, we do not see a particular interest from international Crowdfunding platforms in Slovakia. That said, however, use of international platforms such *Kickstarter*, *Indiegogo* or fundraising tools of social networks such as *Facebook* is very popular on the Slovak market already.

## **2 Recent developments regarding Crowdfunding regulation in Slovakia**

Crowdfunding itself is not explicitly regulated in Slovakia. Different available Crowdfunding models are recognized under several different legal regulations; however, there is no single source of law that would give the Crowdfunding a definitive legal status and legal certainty. Subsequently, some Crowdfunding models enjoy a relatively easy regulatory environment whereas some – mainly the equity model – may fall under very strict regulation.

That said, there is no material change of the regulation directly affecting the Crowdfunding in Slovakia as of December 2015. The only notable regulatory development – albeit affecting Crowdfunding only indirectly – is the introduction of a new type of legal entity known simple joint stock company as of 1st January 2017.

Simple joint stock company has been introduced as an ideal corporate structure for start-ups and new business wishing to attract investment combining the simplicity of the limited liability company and shareholding flexibility of a joint stock company. The most significant changes brought with the simple joint stock company are the extremely low capital requirements (registered capital from 1 EUR) and for the first time – explicit recognition of concepts such as drag-along, tag-along and shootout within the shareholder’s agreement. In addition, simple joint stock company can under ‘eased’ corporate regulatory conditions issue special types of shares that allow investors to have interest on company’s profit without having decision-making or voting rights pertaining to such shares or shares that are non-transferable and can only be sold back to the company. Although such shareholding arrangements have been a common market practice in Slovakia for more than two decades, there has been an academic discussion about the enforceability of such arrangements if not explicitly recognised by the law. With these concepts now explicitly recognised by law this discussion – at least in respect to the simple joint stock company – is effectively over.

The reason why this regulatory development affects Crowdfunding only indirectly is the fact that shares of the simple joint stock company cannot be issued by public offer – as opposed to the standard joint stock company. Therefore, even if the Crowdfunding platform operating based on equity model met the strict regulatory requirements related to facilitating investment into the shares – such shares cannot be legally offered to public. Nevertheless, the simple joint stock company might be a viable option for raising capital from a small ‘non-public’ group of investors and might trigger development of alternative equity Crowdfunding models as discussed below.

### **3 Current regulation of Crowdfunding in Slovakia**

#### **3.1 Licence under the Securities and Investment Services Act**

##### **3.1.1 Equity Model / Lending Model**

###### **(1) General Rules**

The Securities and Investment Services Act governs, among others, provision of the investment services and so-called ‘ancillary services’ which are subject to the licence issued by the NBS. Investment services include:

- A. reception and transmission of client orders in relation to one or more financial instruments;
- B. execution of orders on behalf of clients;
- C. dealing on own account;
- D. portfolio management;

- E. investment advice;
- F. underwriting or placing of financial instruments on a firm commitment basis;
- G. placing of financial instruments without a firm commitment basis;
- H. operation of multilateral trading facilities.

The ancillary services include:

- A. safekeeping and administration of financial instruments for the account of clients,
- B. including custodianship and related services, such as cash/collateral management;
- C. granting credits or loans to an investor to allow him to carry out a transaction in one or more financial instruments, where the provider of the credit or loans is involved in the transaction;
- D. advice on capital structure and business strategy, and advice and services relating to the merger, consolidation, transformation or splitting of undertakings or the purchase of undertakings;
- E. foreign exchange services where these are connected to the provision of investment services;
- F. investment research and financial analysis or the other forms of general recommendation relating to transactions in financial instruments;
- G. services related to the underwriting of financial instruments;
- H. services and activities mentioned in paragraph (1)(a) to (f) related to the underlying of the derivatives included in under Article 5(e) to (g) and (j), where these are connected to the provision of investment or ancillary services.

“Financial instruments” within the meaning of the Securities and Investment Act include:

- A. transferable securities;
- B. money market instruments;
- C. fund shares or securities issued by foreign collective investment undertakings;
- D. options, futures, swaps, forwards and any other derivative contracts relating to securities, currencies, interest rates or yields, or other derivative instruments, financial indices or financial measures which may be settled physically or in cash;
- E. options, futures, swaps, forwards and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event);
- F. options, futures, swaps and any other derivative contract relating to commodities that can be settled in cash provided that they are traded on a regulated market or a multilateral trading facility;
- G. options, futures, swaps, forwards and any other derivative contracts relating to commodities that can be settled in cash and are not mentioned in subparagraph (f), and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard to whether they are cleared or

settled through the clearing and settlement system or are subject to regular margin calls;

- H. derivative instruments for the transfer of credit risk;
- I. financial contracts for differences;
- J. options, futures, swaps, forwards and any other derivatives concerning climatic variables, freight rates, emission allowances or inflation rates or other official economic statistics that must be settled in cash or may be settled at the option of one of the parties (otherwise than by reason of insolvency or other termination event), as well as any other derivatives concerning assets, rights, obligations, indices and other factors not otherwise mentioned in subparagraphs (a) to (i), which have the characteristics of other derivative financial instruments, having regard to whether they are traded on a regulated market or multilateral trading facility, are cleared or settled through the clearing and settlement system or are subject to regular margin calls.

## **(2) Exemption from licencing requirements**

Generally, there is no explicit exemption for Crowdfunding platforms from the licencing requirements. For the sake of completeness, we select number of exemptions from the licencing requirements which could be theoretically at least used by the Crowdfunding platforms under certain (quite limited) situations. Of course, relying on any of the below exemptions is always recommended only after prior consultation with the NBS. The licence is not required in respect of the following:

- A. persons which provide investment services exclusively for their parent undertakings, for their subsidiaries or for the subsidiaries of their parent undertakings;
- B. persons dealing on own account in financial instruments or providing investment services in commodity derivatives or derivative contracts to clients, provided this is an ancillary activity to their main business, when considered on a group basis, and that main business is not the provision of investment services within the meaning of this Act or banking services under a separate law; or
- C. persons providing investment advice in the course of providing another professional activity not covered by this Act provided that the provision of such advice is not specifically remunerated.

### **3.1.2 Donations or Rewards Model**

The donations or rewards models are not specifically regulated. However, one cannot exclude risk that large scale rewards model could be viewed by the NBS as a circumvention of the Securities and Investment Act if facilitated without regulatory licence. As mentioned above, there is not a sufficiently clear line between the scope of permitted activities under the relevant simple trade licences and for example, investment advice or other regulated investment or ancillary services.

## 3.2 Prospectus requirements

### 3.2.1 Equity Model / Lending Model

Any public offering of securities is subject to the prospectus requirements. The most relevant exemptions from this requirement under the Securities and Investment Act (in line with the Prospectus Directive) are:

- A. an offer of securities addressed solely to qualified investors;
- B. an offer of securities addressed to fewer than 150 natural persons or legal persons per Member State, other than qualified investors;
- C. an offer of securities addressed to investors who acquire securities for a total consideration of at least EUR 100,000 per investor;
- D. an offer of securities having a denomination per unit of at least EUR 100,000; or
- E. an offer of securities with a total consideration of less than EUR 100,000, which limit shall be calculated over a period of 12 months.

In addition, there are further exemptions from the prospectus requirements generally in line with the Article 4 of the Prospectus Directive.

#### (1) Content of the prospectus

Generally, the prospectus content requirements are in line with the requirements under Prospectus Directive. These requirements are implemented into Section 120 of the Securities and Investment Act.

#### (2) Advertisement

It is prohibited under the Securities and Investment Act to use false or misleading information or conceal facts relevant when deciding on the purchase of securities when promoting the issuance of its securities. In particular, it is prohibited to offer benefits which cannot be guaranteed. The provisions of the Commercial Code on unfair competition are not affected by the Securities and Investment Act.

Public offering of securities without prior publication of an approved prospectus is forbidden. Prospectus can be published in number of ways:

- A. the publication in a daily newspaper with nationwide circulation or sufficient dissemination in the Member States in which the public offer of securities will or is asking for admission to trading on a regulated market;
- B. the publishing in writing form that is free of charge, at the premises of the regulated market on which the securities are admitted to trading, or at the registered office of the issuer and the premises of financial institutions placing or selling the securities and the premises of persons guaranteeing repayment of nominal value of securities and payment of the proceeds of securities;
- C. access in electronic form on the web site of the issuer or the web site of financial institutions placing or selling the securities and persons on the web site of ensuring

the repayment of the nominal value of securities and payment of yields from securities;

- D. access in electronic form on the web site of the regulated market on which the application for admission to trading, or e) publishing in electronic form on the web site of the National Bank of Slovakia where the National Bank of Slovakia decided to provide this kind of service.

Only the above are recognized means of publishing of the prospectus. However, it is not prohibited to publish the prospectus in other ways (e.g. via social media) provided one of the above means is complied with.

### **3.2.2 Donations Model / Rewards Model**

Similarly as mentioned above, there is no explicit requirement to provide and publish prospectus in case in case of donations or rewards models. As a prudent advice mitigating theoretical risk of NBS considering these models to be certain forms of regulated activities, it is recommended to nevertheless provide investors with prospectus information under these models as well, although such risk is currently minimal.

### **3.3 Regulation of Crowdfunding under the AIFMD regime**

AIFMD Directive has been implemented into the Act No. 203/2011 Coll., on the collective investment, as amended (the “Collective Investment Act”). Due to the complex definition of the collective investment undertaking it cannot be ruled out that Crowdfunding platforms might also trigger regulatory requirements under the Collective Investment Act. In general, it has to be noted that investment funds including the alternative investment fund (the “AIF”) do not have separate legal personality in Slovakia and all acts on behalf of them shall be undertaken via its managers (the “AIFM”) which require licence issued by the NBS in order to operate.

It stems from our informal discussions with representatives of the NBS that they are aware of non-sufficient regulatory framework and guidance in respect of Crowdfunding in general and view it as an EU-wide problem while fragmentation is their main concern. NBS is aware of number of small Crowdfunding platforms already being established in Slovakia, however, no official standpoint or approach towards them has been adopted by the NBS as of yet because of the above.

#### **3.3.1 Definition of AIF**

The AIF under the Collective Investment Act is either:

- Special common fund, i.e. a common fund which is not a standard common fund and into which funds are collected through public offer or private offer in order to invest such funds in assets determined by this Act or by a special common fund’s rules. For the purposes of the Collective Investment Act, special common fund is a

common fund which is not subject to a legally binding act of the European Union governing collective investment undertakings in transferable securities; or

- Domestic collective investment undertaking with legal personality, being a commercial company or a cooperative having its registered office in the territory of the Slovak Republic collecting funds from multiple investors in order to invest them according to a defined investment policy in favour of those investors.

### 3.3.2 Equity Model

Whether the Crowdfunding platform triggers the above definition of the AIF also depends on the general test in the Section 2 (3) of the Collective Investment Act which provides collection of funds for the purpose of their further investment is generally prohibited, if:

- the return of such collected funds or a profit of entities whose funds have been collected, shall, even if partially, depend on the value of returns on assets acquired for the funds raised, and
- it is not carried out on the basis of an authorization under this Act or under the conditions provided by the Collective Investment Act.

In the explanatory report to the Collective Investment Act the NBS admits that this general prohibition clause is very wide and it is therefore required that certain regulated activities on the financial market, financing of the common business activities or potentially other common business activities shall be excluded from the scrutiny of the Collective Investment Act. As to the explicit exceptions mentioned in the Collective Investment Act these are, among others:

- collection of funds by the holding company (presumably intragroup financing – although not explained in more detail);
- collection of funds by the municipality, higher territorial unit or foreign public authority of territorial self-administration;
- collection of funds, the main objective of which is to finance an activity having the nature of the production, research or provision of services, other than financial services, and is financed primarily from the own resources of the entity that is raising the funds.

It can be argued that above exemptions could be relied on by the Crowdfunding platforms in certain situations but does not serve as a blanket exemption, mainly having regard to our informal discussion with the NBS.

### 3.3.3 Lending Model

As mentioned above, the purpose of the Collective Investment Act should not be to regulate financing of the common business activities. However, the above-mentioned exceptions are more restrictive in a sense that they only cover intragroup financing, certain municipality financing or financing where (by literal interpretation) half of the funds are collected from own

resources. Therefore, one cannot exclude that the lending model would not trigger the requirements under the Collective Investment Act.

The Collective Investment Act also includes definition of the “debt securities” being bonds and securities established by the transformation of credits or loans issued in Slovakia or abroad. Debt securities fall under the wider definition of transferrable securities under the Collective Investment Act.

### **3.3.4 Donations or Rewards Model**

Generally, the Collective Investment Act is construed in a way that certain profit or return from the investment is expected. We would assume this is not the case of donations or rewards model and therefore requirements under the Collective Investment Act would not be triggered under these scenarios.

## **3.4 Requirements of a Licence under the Payment Services regulation**

The Act No. 492/2009 Coll., on payment services, as amended (the “Payment Services Act”) implementing the Payment Services Directive requires that any provider of payment service shall obtain payment services licence from the NBS. The payment services under the Payment Services Act include, among others any money remittance services or execution of payment transactions on behalf of the client. However, there are number of exemptions which could, depending on circumstances, be relied upon by the Crowdfunding platforms in our view.

## **3.5 Possible additional regulations**

Other common regulations to which the operator of a Crowdfunding platform may be subject to include:

- The Public Collections Act described in more detail in Section 3.5.1 below;
- Act No. Act No. 455/1991 Coll., on trade licencing, as amended;
- Act No. 297/2008 Coll., on protection against legalization of crime proceeds and against financing of terrorism, as amended (AML regulation);
- Act No. 129/2010 Coll., on provision of consumer credit, as amended;
- Act No. 483/2001 Coll., on banks, as amended;
- Act No. 122/2013 Coll., on protection of personal data, as amended.

### **3.5.1 Requirements under the Public Collections Act**

The Public Collections Act governs ‘public collections’ which are defined as acquiring and collecting of the voluntary payment contributions (i) by legal persons entitled to do so in accordance with the Public Collections Act (ii) from prior determined scope of contributors and (iii) for the prior determined publicly beneficial purpose. Crucial determinant of whether Crowdfunding can be covered by the Public Collections Act is whether the purpose of the Crowdfunding can be regarded as publicly beneficial. According to the Public Collections Act the following purposes are regarded as publicly beneficial:

- A. Development and protection of the religious values;
- B. Protection of the human rights;
- C. Protection and creation of the environment;
- D. Preservation of natural and cultural values;
- E. Health protection;
- F. Development of the social services, science, education and sport;
- G. Development of volunteering activities;
- H. Humanitarian and development activities;
- I. Protection of rights of disadvantaged groups;
- J. Support of work with children; or
- K. Individual humanitarian support of individuals.

If the purpose of public collection falls under the above, the Crowdfunding platform would need to be prior registered in the register of public collections maintained by the relevant District Authority or by the Ministry of Interior if the scope of the collection reaches beyond one district. The Public Collections Act further regulates types of legal persons which can organize public collections. However, the most common corporate forms such as limited liability companies and joint stock companies are excluded from such list. The list of allowed types of legal persons includes among others: civil associations, non-investment funds, non-profit organizations, association of municipalities and purpose association of legal persons. These persons are specifically regulated and some of them are country-specific types of legal persons, however, they all have a common feature – having a purely non-profit character. In general, these persons can generate profit but cannot distribute it to its founders but must only use it for the purpose for which such persons were established. This practically means that should a Crowdfunding platform operate under the Public Collections Act it could only do so on a non-profit basis.

As to the forms in which funds can be collected by the Crowdfunding platforms under the Public Collections Act, these are:

- A. Bank transfers on a specified bank accounts;
- B. Via SMS or phone call;
- C. Physical collections to moneyboxes (stationary or portable);
- D. By selling goods or tickets.

All the above means of Crowdfunding can be practiced only for the period 12 months from registration with the exception of the portable moneyboxes which can be practiced only for 14 days. Upon request the 12-month period can be prolonged by the District Authority for additional 12 months in case of specific reasons.

Within 90 days from termination of the public collection, the Crowdfunding platform is obliged to submit to the District Authority a preliminary report and within 12 months from the its termination also the final report which should be later published on the website of the

Crowdfunding platform. These documents evidence use of the funds collected by e.g. bank account extracts or invoices.

### 3.5.2 Regulatory approach towards the P2P lending in Slovakia

On 27th April 2016, the NBS issued a statement on its website (only available in Slovak) in which the NBS very briefly explains its regulatory position towards two providers of P2P lending in Slovakia known as *Zinc Euro* and *Zlty Melon*. It states that the peer-to-peer lending activity in a form of internet auction – as undertaken by these two subjects – does not fall under its regulatory oversight. It further states that the public should assess the risk associated with such lending. The NBS did not, however, explain the legal considerations behind such statement.

## 4 Regulatory barriers for Crowdfunding crossing borders

As mentioned above, most of the Crowdfunding platforms in Slovakia operate based on donations and reward model but there are at least two promising platforms developing their own equity models. Under the donations and reward model we do not see any significant or unusual regulatory barriers regarding cross-border provision of services. This part will therefore analyse only the regulatory barriers for the equity model which is most affected by local financial regulation.

### 4.1 Applicable law

The financial regulation under the Securities and Investment Services Act applies to entities providing investment or ancillary investment services in Slovakia. However, there is no further definition or guidance as to what constitutes provision of such services in Slovakia and the law does not explicitly distinguish between addressing Slovak investors or Slovak companies / projects in this respect. Based on informal discussion with the NBS we understand that their approach is to consider all criteria on a case-by-case basis. Criteria which might be considered by the NBS as constituting the provision of investment or ancillary services in Slovakia might be:

- Whether the marketing campaign is addressed to Slovak market. It is not sufficient if the marketing campaign is only available to Slovak market by means of internet if there is no link to Slovakia. More specifically, the NBS suggested that Slovak investors are free to use foreign Crowdfunding platforms available via internet (such as KickStarter) without triggering the Slovak regulatory regime provided that their marketing activities are not regarded as focused on the Slovak market. In this respect, the NBS would look more closely at whether the campaign is tailored to Slovak market by use of Slovak language, references to Slovak customers, Slovak distribution channels or whether any marketing material is physically available in Slovakia.
- Whether the foreign Crowdfunding platform has any establishment, office or representative in Slovakia.

- In any case, if the Crowdfunding platform has a registered seat in Slovakia, it will most likely fall under the regulatory scrutiny of the NBS.

Depending on the above factors, there are three licence options for undertaking investment and ancillary investment services under the Securities and Investment Services Act in Slovakia:

- A. Licence issued to Slovak entity (only joint stock company) (the “Full Licence”);
- B. Licence issued to a foreign entity via its Slovak branch, provided such foreign entity is licenced in its home state (the “Branch Licence”);
- C. Notification under the EU passport regime without a need to establish a Slovak branch (the “EU Passport”);

the Full Licence, the Branch Licence and the EU Passport jointly as the “Licence Options”.

### (1) Full Licence

Full Licence option is the least attainable licence option posing the most significant regulatory barrier. Company wishing to obtain the Full Licence (the Crowdfunding platform) needs to comply with – among others – the following general requirements before its incorporation:

- legal form of joint stock company (in Slovak: *akciová spoločnosť*) with paid-up registered capital of the company from EUR 50,000 to EUR 730,000 depending on type of licenced services. Requirement of the registered capital may be met by concluding appropriate professional insurance (minimum insurance of EUR 1 million per insurance event);
- transparent and credible source of registered capital and other financial resources of the company;
- suitability of persons with qualified interest in the company and transparency of relations between these persons, in particular transparency of their interests in registered capital and voting rights;
- professional competence and trustworthiness of persons nominated as members of the board of directors or managerial employees, persons responsible for the compliance function, risk management function or internal audit function;
- transparency of a group with close links of which a shareholder with qualified interest in the company is a member;
- such close links within a group mentioned above must not prevent effective supervision;
- the law and its application in the country where a group mentioned above has close links do not prevent effective supervision;
- the company shall have its registered office and head office in the territory of the Slovak Republic; 'head office' means the place from where the operation of the

company is managed or the place where the company keeps the documents on its operation that are required for the exercise of supervision;

- the professional competence and trustworthiness of natural persons who are members of the statutory body of the financial holding company or mixed financial holding company, and the suitability of shareholders controlling the financial holding company or the mixed financial holding company, where the grant of the licence would mean the company becoming part of the consolidated group, of which the financial holding company is a part, or becoming part of the financial conglomerate, of which mixed financial holding company is a part.

All the above-mentioned requirements are subject to additional detailed regulations in decrees of the NBS which provide for type and nature of documents that must be provided to NBS to comply with the above including internal regulations and compliance mechanisms in place.

## **(2) Branch Licence**

In general, Branch Licence requirements are similar to the Full Licence requirements. Branch Licence requirements are not drafted as specifically (e.g. strictly) since the rationale behind them is to give the NBS room for examining whether foreign country's regulatory regime may be considered as equivalent to the Slovak regulatory regime. Although there is further regulation by the NBS as to the type and nature of documents that must be provided in order to comply with these requirements, it is naturally less clear compared to the Full Licence whether particular requirement will be considered as met by the NBS within its licencing proceedings. When requesting Branch Licence, the following general requirements must be met:

- sufficient volume and transparency of finances provided by the company to its branch with respect to the range and risk level of the business of the branch;
- trustworthiness of the foreign company and its financial strength corresponding to the scope of business of the branch;
- professional competence and trustworthiness of persons proposed by the company as executive officers of its branch;
- transparency of a group with close links of which the foreign company is a member;
- such close links within a group do not prevent effective supervision;
- the law and its application in the country where the group mentioned has close links do not prevent effective supervision;
- the foreign company seeking to operate through its branch in the Slovak Republic has its principal place of business in the country where it has its registered office;
- the laws of the country in the foreign securities dealer has its registered office require compliance with conditions regarding the performance of activities and

maintenance of capital adequacy which are not lower than those stipulated for securities dealers under the Securities and Investment Services Act;

- clean criminal register of the applicant.

Branch Licence is also subject to more specific requirements which in practice might prove to be quite burdensome for some foreign companies. These include – among others – providing the NBS with the home country licence of the foreign company, consent with and position towards establishing the branch office in Slovakia by the home supervision authority and declaration of the home supervision authority that it will timely inform the NBS about any events that could impact the ability of the foreign company to fulfil its obligations.

#### **(4) EU Passport**

A Company (Crowdfunding platform) that holds licence in another EU member state may provide investment or ancillary investment services in Slovakia without establishing Slovak branch based on notification to the NBS pursuant to the Section 64 and following of the Securities and Investment Services Act. In this EU-standardised notification, the EU-licensed company must specify the plan of activities it wishes to undertake in Slovakia, including nature and scope of the investment or ancillary services to be provided in Slovakia and information whether it intends to use any tied bound investment agents in Slovakia. The NBS sends this information to the EU home supervisory authority within 30 days. The EU-licensed company is then authorised to provide such services in Slovakia as of the day the NBS sends the information pursuant to the previous sentence and must comply with the applicable Slovak law in respect to such services.

#### **(5) Other applicable law**

It cannot be ruled out that the additional possible regulations would apply to the Crowdfunding platform in Slovakia, as explained in Sections 3.5 above.

## **4.2 Inbound**

### **4.2.1 Crowdfunding platform from another EU member state addresses investors in Slovakia**

Slovak regulatory law may apply to:

#### **4.2.1.1 Crowdfunding platforms**

In this scenario, all three Licence Options are available. For the Crowdfunding platform from another EU member state holding passportable licence in another EU member state, the EU Passport is the most attainable option. If the Crowdfunding is not holding passportable licence in another EU member state or equivalent licence from a third country, the Full Licence is the only option.

#### 4.2.1.2 Company / project seeking funding

Company / project seeking funding might be caught by the Slovak regulatory prospectus requirements provided that the Crowdfunding platform offers its securities to public in Slovakia. Securities are defined in Section 2 of the Securities and Investment Services Act as:

- shares;
- interim certificates;
- shares in investment funds;
- bonds;
- certificates of deposit;
- treasury bills;
- passbooks;
- coupons;
- bills of exchange;
- cheques;
- traveller's cheques;
- bills of lading;
- warehouse certificates;
- warehouse warrants;
- goods warrants;
- shares in cooperatives;
- investment certificates;
- other types of securities designated as such by a separate law.

With respect to shares – under Slovak law – only shares of a joint stock company (in Slovak: *akciová spoločnosť*) fall under this category, since shareholding interests in other types of companies are either not regarded as shares (e.g. in case of the limited liability companies) or cannot be sold based on the public offer (in case of simple joint stock company). In general, the prospectus requirements under the regulatory scrutiny of the NBS apply to situation where the public offer of securities happens in Slovakia, i.e. when Slovak investors are approached / targeted. The Securities and Investment Services Act includes provisions regarding co-operation and free movement within the EEA in its Sections 125d – 125f which implement relevant provisions of the Prospectus Directive. These provisions allow both:

- A. approval of the prospectus in the home member state of the issuer (company/project); and
- B. approval of the prospectus by NBS Slovakia.

In case the company/project has a registered seat outside the EU, the NBS may also approve prospectus from this country subject to compliance with certain equivalency provisions.

Some Crowdfunding platforms report that the prospectus requirements pose the main regulatory barrier to their operation due to the necessary time and budgetary constraints. According to them, there are certain provisions in the Securities and Investment Services Act that would allow the NBS to remove or simplify these requirements if the NBS proactively decided to issue a specific guidance or adopt a policy towards the Crowdfunding. Some Crowdfunding platforms argue that this approach is already taking place in some other EU member states but not in Slovakia. The relevant provisions are Section 125h (1) let. i), Section 125h (3) and Section 125h (4) of the Securities and Investment Services Act according to which:

- A. Requirements regarding public offer and prospectus requirements do not apply (unless the law provides otherwise) to the securities that are subject to public offer with value less than EUR 5 million within the EU in the period of 12 months;
- B. Then the law provides otherwise – by specifying that such requirements indeed apply to securities according to point (a) above if their value is between EUR 100,000 and EUR 5 million; and
- C. If (b) is the case, the NBS is empowered to authorise certain prospectus requirements to be omitted given the circumstances of the public offer.

However, the NBS has not yet so far used the above to put forward any guidance or policy aimed to simplify operation of the Crowdfunding platforms, although we understand certain discussion with market players already takes place.

#### **4.2.2 Crowdfunding platform from another EU member state addresses companies / projects in Slovakia**

As mentioned above, Slovak regulatory law may apply to:

##### **4.2.2.1 Crowdfunding platform**

The applicable law does not explicitly provide that foreign Crowdfunding platform would fall under the Slovak regulatory scrutiny by inviting public to invest into the Slovak company, if there is no other link to Slovak market. We believe that general test explained in Section 4.1 applies in this case too and if not met, then the mere fact that the company in question is a Slovak company is not enough to override this.

For example, if a German Crowdfunding platform offers shares of Slovak company on its German website in German language, the Slovak law should not apply to this German Crowdfunding platform. If, on the other hand, this German Crowdfunding platform would market such offer in Slovakia by using Slovak language on its website or by having a separate marketing campaign focused on Slovak customers, then the Slovak law could apply. In that case, all three Licence Options are available, as mentioned above.

#### 4.2.2.2 Company / project seeking funding

We believe the regulatory barriers to company / project seeking funding are the same as described in point 4.3.1 (ii) above.

### 4.3 Outbound

#### 4.3.1 Crowdfunding platform from Slovakia addresses investors in other EU country

##### 4.3.2 Crowdfunding platform

In case the Slovak Crowdfunding platform approaches investors in other EU member state, the regulatory barriers are primarily governed by the laws of this other EU member state (or several other EU member states) depending on whether the applicability of the foreign regulatory regime is triggered or not. It cannot be ruled out that the Slovak regulatory regime might be also applicable in case the offer has a sufficient link to the Slovak market in addition to links with other EU markets. If that is the case, the Slovak Crowdfunding platform would need to obtain the Full Licence in respect to the planned activities in Slovakia.

In case the Slovak Crowdfunding platform is already duly licenced in Slovakia, the Securities and Investment Services Act recognises two approaches:

- A. either to rely on EU Passport in another EU member state without establishing a branch there; or
- B. to establish a branch in another EU member state subject to local licencing requirements.

These approaches are subject to certain notification obligations towards the NBS, such as:

- notification about the intention to establish a branch in another EU member state together with some basic information about the intended activities including prior notification about every change of such information;
- notification about obtaining the branch licence in another EU member state;
- notification about the intention to provide services in another EU member state based on the EU Passport rules.

In addition, the Slovak Crowdfunding platform under this scenario is obliged under Slovak law to co-operate and provide necessary information to the hosting EU supervisory authority.

##### 4.3.2.1 Company / project seeking funding

We believe the regulatory barriers to company / project seeking funding are the same as described in point 4.3.1 (ii) above.

### **4.3.3 Crowdfunding platform from Slovakia addresses companies / projects in other EU country**

#### **4.3.3.1 Crowdfunding platform**

The law does not specifically deal with situation when a Slovak Crowdfunding platform approaches companies / projects in other EU country. As mentioned above, there are several criteria that are considered by the NBS when considering whether the Slovak market is approached or not and these requirements apply to this scenario too.

#### **4.3.3.2 Company / project seeking funding**

We believe the regulatory barriers to company / project seeking funding are the same as described in point 4.3.1 (ii) above.

## **4.4 Impact of EU regulation**

### **4.4.1 Prospectus rules**

There is only a single regulation of prospectus requirements in Slovakia provided for under the Securities and Investment Services Act implementing the Prospectus Directive. The scope of the securities to which the prospect requirements apply to in case of their public offer as well as relevant exemptions are explained above. As mentioned above, there is very limited number of Crowdfunding platforms in Slovakia operating under the equity model – or developing it rather – and therefore it could be said that majority of the Slovak Crowdfunding market is not covered by the harmonized European legislation implemented into the Slovak law. On the other hand, should Crowdfunding platform operate based on the equity model – the European legislation as implemented into the Slovak law poses very significant regulatory barrier to their operation and/or establishment.

### **4.4.2 AIFM-Directive**

The AIFM-Directive and the implementing the Slovak Collective Investment Act mainly affect equity-based or potentially lending-based Crowdfunding platforms (debt securities). There are several other activities undertaken by businesses in Slovakia which are at the odds with the wide definition of the collective investing. However, there is simply not sufficient regulatory enforcement in Slovakia which would allow drawing clear lines between these non-regulated business activities and regulated collective investment services. Equity-based Crowdfunding platforms fall into that group and it remains to be seen whether the NBS will put forward any guidance or policy explaining how the Collective Investment Act applies to them.

### **4.4.3 MiFID II**

The impact of MiFID II on the Slovak Crowdfunding platforms is very similar with the impact of the prospectus rules described in point 4.5.1 above as both MiFID and MiFID II will have been implemented into the same legislation as the Prospectus Directive, i.e. Securities

and Investment Services Act. The main scope of application of MiFID/MiFID II is the possibility to rely on the EU Passport regime both inbound and outbound.

#### 4.4.4 PSD II

The Payment Services Directive has been implemented into the Slovak Payment Services Act and the same is expected regarding the PSD II. Interestingly, the Slovak Payment Services Act also implements the E-Money Directive which causes certain interpretation difficulties especially with respect to the licence requirements. With respect to PSDI / PSDII the money remittance services and necessary licence requirements might be triggered by the Crowdfunding platform if the investor funds are transferred through it. Alternatively, the Crowdfunding platform may decide to co-operate with licenced payment services operator. Nevertheless, it poses a great administrative, time and financial barrier for Crowdfunding platform to consider all the above complex regulation before it commences to operate.

#### 4.5 Summary

Even in the small European market such as the Slovakia the need for harmonised regulation of Crowdfunding is pressing. Current regulatory environment is too complex for a Crowdfunding platform – which by its nature – should not face the same level of regulation as the established financial institutions, investment firms or security brokerage firms. By its nature – the Crowdfunding should be an easier alternative to the established means of raising money and should be recognised on the EU level in accordance with the aim to establish a European single market. Cross-border flow of the capital facilitated by the less-regulated Crowdfunding within the Union is an important socio-economic factor of the EU integration process.

From a Slovak perspective, the Crowdfunding platforms face mainly the following regulatory barriers:

- No relevant exemption from licence requirements under the Securities and Investment Services Act and the Collective Investment Act; and
- No relevant exemption from the prospectus requirements under the Securities and Investment Services Act.

Apart from regulatory barriers, the Crowdfunding platforms argue that there is almost no official standpoint of the main regulator concerned – the NBS – on position of Crowdfunding platforms (especially based on equity model). Although it seems that there is a formal discussion of the market players with the NBS, there is still no official standpoint of NBS or in fact of any other public authority on the Crowdfunding – except for P2P lending model. In such a situation, it is inevitable that Crowdfunding platforms are forced / motivated to operate in ‘grey’ areas of the law without the actual oversight by any regulator. This may potentially harm all parties involved; investors, targets, Crowdfunding platform operators as well as the NBS. There is a clear understanding from the Crowdfunding platform operators about the need for certain basic rules for Crowdfunding such as protection of the investors, transparent

information to be provided to the public or application of the AML laws – which they do not oppose. Their argument is that there needs to be certain regulation but less burdensome than the current one.

## 5 Lessons learned from Slovakia for a possible harmonized European Crowdfunding regulation

### 5.1 Role models (“dos”)

For a possible harmonised European regulation of the Crowdfunding the following aspects can serve as a role model:

- exception of Crowdfunding from most regulatory requirements (in particular prospectus requirements);
- replacement of the prospectus with much briefer / shorter fact sheets for investors;
- only lighter regulation of the Crowdfunding platform;
- unlimited investment amounts for ”professional” investors;
- transparent & easy rules regarding access to foreign markets both in terms of foreign investors and foreign companies/projects without the need to obtain foreign licences and without the need to establish corporate presence in more than one EU member state.

### 5.2 Aspects that should be avoided (“don’ts”)

Regulation of Crowdfunding under the Slovak law should not serve as a role model for a possible harmonised European regulation of Crowdfunding. In particular following aspects should be avoided:

- Any limitations in terms of number of investors;
- Any limitations in terms of amount of funds raised & time period within which such amount can be raised;
- Too harsh minimum registered capital requirements for Crowdfunding platforms – better to replace these with adequate minimum insurance requirements;
- Requirement for joint stock company legal form – any capital corporate form (limited liability company, simple joint stock company and joint stock company should be allowed).

## 6 Conclusion

In conclusion, currently both Slovak and EU regulation pose a barrier for Crowdfunding to evolve and positively impact the business environment in Slovakia. The main regulatory barriers stem from the Securities and Investment Services Act and the Collective Investment Act while the national regulator under both regimes, the NBS, does not have any practice or policy established in respect of Crowdfunding platforms. We agree that the increasing fragmentation of the European Crowdfunding regulation due to the introduction of national

Crowdfunding regulation may even aggravate the barriers for cross-border Crowdfunding. A need for a harmonized European Crowdfunding regulation is in our opinion justified.

## 7 Summary – Crowdfunding regulation

| Country   | Slovakia   |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• New corporate legal form – simple joint stock company;</li> <li>• Number of new Crowdfunding platforms in Slovakia.</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• The Securities and Investment Services Act – licence and prospectus requirements.</li> <li>• The Collective Investment Act – licence and sale prospectus requirements – possible exception of financing regular business activity with half of the funds being collected from own resources;</li> </ul>   |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for offering of securities or investment products;</li> <li>• General threshold: EUR 100,000 per issuer within 12 months;</li> <li>• No explicit exemption from prospectus for Crowdfunding.</li> </ul>  |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Depending on the particulars, both project companies and operating companies may constitute an AIF;</li> <li>• General exemption from AIFM for financing of the general business activities provided half of the funds collected from own resources;</li> <li>• General exemption for intra-group financing and financing of general business activities of municipalities.</li> </ul>  |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Licence required for money remittance and payment transactions, however, number of exemptions might be applicable;</li> <li>• Cooperation with payment institution or bank removes the risk of applicability of the Payment Services Act.</li> </ul>  |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Act No. 162/2014 Coll. on public collections, as amended</li> <li>• Act No. 455/1991 Coll., on trade licencing, as amended;</li> <li>• Act No. 297/2008 Coll., on protection against legalization of crime proceeds and against financing of terrorism, as amended (AML regulation);</li> <li>• Act No. 129/2010 Coll., on provision of consumer credit, as amended;</li> <li>• Act No. 483/2001 Coll., on banks, as amended;</li> <li>• Act No. 122/2013 Coll., on protection of personal data, as amended.</li> </ul> |
| <b>Regulatory barriers</b>                            |  |
| <b>Inbound</b>  | <b>Foreign Crowdfunding platform addresses Slovak investors</b>  |

|                        |  |
|------------------------|--|
|                        | <ul style="list-style-type: none"> <li>• Slovak regulatory law is applicable since Slovak investors are approached in Slovakia.</li> <li>• Three licence options are available for foreign Crowdfunding platform: Full Licence, Branch Licence or EU Passport.</li> <li>• The company/project has mainly prospectus obligations which can be met by approval of the prospectus by the NBS, by approval of the prospectus in its home member state or by approval of the prospectus outside EU with subsequent approval by the NBS subject to certain equivalency provisions.</li> </ul> <p><b>Foreign Crowdfunding platform addresses Slovak companies / projects</b></p> <ul style="list-style-type: none"> <li>• Slovak regulatory law may be applicable depending on whether the Slovak market is approached (Slovak language, physical presence, marketing focus on Slovakia).</li> <li>• Three licence options are available for foreign Crowdfunding platform: Full Licence, Branch Licence or EU Passport.</li> <li>• The company/project has mainly prospectus obligations which can be met by approval of the prospectus by the NBS, by approval of the prospectus in its home member state or by approval of the prospectus outside EU with subsequent approval by the NBS subject to certain equivalency provisions.</li> </ul>   |
| <p><b>Outbound</b></p> | <p><b>Slovak Crowdfunding platform addresses investors in other EU country</b></p> <ul style="list-style-type: none"> <li>• Primarily governed by the laws of that EU country.</li> <li>• Slovak regulatory law may be triggered if there is sufficient link to Slovak market in addition to links with other EU markets. If that is the case, Full Licence needs to be obtained in Slovakia.</li> <li>• If the Slovak Crowdfunding platform is already licenced in Slovakia, then – according to the Slovak law – it can either rely on EU Passport or establish a branch in that EU country subject to applicable laws of that country.</li> <li>• The company/project has mainly prospectus obligations which can be met by approval of the prospectus by the NBS, by approval of the prospectus in its home member state or by approval of the prospectus outside EU with subsequent approval by the NBS subject to certain equivalency provisions.</li> </ul> <p><b>Slovak Crowdfunding platform addresses company/projects in other EU country</b></p> <ul style="list-style-type: none"> <li>• Not explicitly recognised under the Slovak law.</li> <li>• General test of whether the Slovak law applies (link to Slovak market).</li> <li>• The company/project has mainly prospectus obligations which can be met by approval of the prospectus by the NBS, by approval of the</li> </ul> |

|                                |   |
|--------------------------------|---|
|                                | prospectus in its home member state or by approval of the prospectus outside EU with subsequent approval by the NBS subject to certain equivalency provisions.  |
| <b>Impact of EU regulation</b> |   |
| <b>Prospectus regulation</b>   | <ul style="list-style-type: none"> <li>• Since there are only two equity-based Crowdfunding platforms in Slovakia (to the best of our knowledge), the EU regulations have no great impact on the Crowdfunding in Slovakia.</li> <li>• However, for these two equity-based Crowdfunding platforms, the EU regulations (as implemented into Slovak law) pose a major regulatory barrier to their operation and/or establishment.</li> </ul> |
| <b>AIFM-Directive</b>          | The impact of AIFM-Directive as implemented into Slovak law is not yet fully clear since there is no enforcement standpoint of the main regulator – the NBS – on its applicability to Crowdfunding platforms.   |
| <b>MiFID / MiFID II</b>        | EU Passport possibility is the main impact.   |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• Depending on its cash flow model, licence requirements for mainly money remittance services may be triggered.</li> <li>• Certain licence exemptions available.</li> </ul>  |

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# Slovenia

## 1 Recent developments in the market of Crowdfunding in Slovenia

Crowdfunding is a relatively new concept in Slovenia, but has seen significant development and positive media coverage in the last years. Currently several public initiatives are working on developing an operational and legal framework for this new type of financing.

### 1.1 Equity

There have been no recent developments in the equity Crowdfunding market in Slovenia.

### 1.2 Lending

CONDA Slovenia, a lending based Crowdfunding platform, entered into the Slovenian market in May 2016. CONDA Crowdfunding is a cross border European crowdfundering platform currently operating in Austria, Germany, Slovenia, Slovakia and Poland. Investors can invest into Project Companies in the form of Subordinated Loans. Every investor is entitled to 4,5 – 5,5 % annual interest (if the Project Company has a positive EBITDA) for the duration of the loan, and after maturity they are entitled to special appreciation bonus which is calculated on the basis of pre-campaign valuation in respect to valuation of Project Company at the end of Loan Agreement. 2016 was a very successful year for Slovenia in respect to Crowdfunding and crowdfundering. Besides official start of platform CONDA Slovenia, two other donations based platforms launched.

### 1.3 Donations or rewards

The prevailing Crowdfunding model used by projects in Slovenia remains the donations and rewards model. The first Slovenian donations or rewards based Crowdfunding platform called Adrifund launched in April 2016. Adrifund is a Crowdfunding platform based on Iceland's Karolina fund and operates on donation model, offering various NGO, art, music and literature project to be funded by their supporters. Chariyo is a Slovenian platform for crowd charity with a very different model of fundraising. Funds for charity projects are provided by companies and supporters of the project are allocating them by performing various tasks such as viewing ads, participating in contests and so. However it is still common practice to use foreign platforms, mostly over the Internet, for funding projects. Social projects with charitable and humanitarian purposes are commonplace and raise funds under the Humanitarian Agencies Act (*Zakon o humanitarnih organizacijah*) through media campaigns and non-profit associations.

### 1.4 Real Estate / Renewable Crowdfunding

Crowdfunding in the Real Estate sector appears to be fully undeveloped. Real Estate project are still largely funded by in traditional ways, such as with financing obtained through commercial loans, while larger projects may be funded through public-private partnerships or with the help of subsidies.

Crowdfunding in the Renewables sector appears to be fully undeveloped as well and Slovenian Energy Agency as well as the Crowdfunding initiatives operating in Slovenia are unaware of any special Crowdfunding initiatives in this sector. This fact may be attributed to higher short-term costs of renewable energy sources compared to the traditional energy sources, which helps explaining why most Renewables projects are co-funded by public funds.

### 1.5 International approach

As the Slovenian Crowdfunding market is relatively undeveloped compared to other EU, we are unaware of any third country Crowdfunding platforms trying to enter the Slovenian market and planning to establish an international Crowdfunding platform in Slovenia. However, CONDA EU, the Crowdinvesting platform originating in Austria, is now offering investment opportunities for Slovenian investors for *inter alia* Slovenian projects as well.

## 2 Recent developments in the regarding Crowdfunding regulation in Slovenia

There is yet no Crowdfunding specific legal framework in place, however under applicable law the equity, lending as well as donations or rewards based models are possible. The AIFMD was implemented through the Act on alternative investment fund managers (*Zakon o upraviteljih alternativnih investicijskih skladov*) and an amendment to the Investment Trusts and Management Companies Act (*Zakon o investicijskih skladih in družbah za upravljanje*). The content of both Acts follow the AIFMD text. There have been no other significant recent developments in the Crowdfunding regulation in Slovenia.

## 3 Current Regulation of Crowdfunding in Slovenia

### 3.1 Licence under the Financial Instruments Market Act

#### 3.1.1.1 Equity Model

Under the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*), only banks, broker-dealers and investment enterprises that hold a licence issued by the Securities Market Agency may perform financial services and transactions. Financial services and transactions among others include brokerage and agency services involving financial instruments, operation of a multilateral trading facilities, investment consulting and trading of financial instruments on primary and secondary markets. Financial instruments include transferable securities, namely shares in joint-stock companies, Societas Europaea and limited partnerships with share capital, bonds, other debt securities and derivative financial instruments. However, membership units in limited liability companies and rights in limited and general partnerships formed under the Companies Act (*Zakon o gospodarskih družbah*) are not transferable securities and therefore do not fall under the regulation of the Financial Instruments Market Act. It must be noted that under the Companies Act a limited liability company may not have more than 50 members without a special approval of the Ministry of Economic Development and Technology. Therefore, where a Crowdfunding platform enables

the financial services and transactions with transferable securities a licence by the Securities Market Agency is required.

### 3.1.1.2 Lending Model

Trade and services related to offering of bonds and other debt securities qualify as provision of financial services and transactions under the Financial Instruments Market Act, which triggers the requirement for a licence by the Securities Market Agency.

Taking in of money from unsophisticated persons in the form of deposits or otherwise pursuant to a deposit or other agreement whereby the depositor has the right to request repayment in certain time periods is considered provision of banking services under the Banking Act (*Zakon o bančništvu*). Additionally, granting of credits and loans as a business activity is also provision of banking services under the Banking Act. Only banks holding a licence from the Bank of Slovenia are permitted to preform banking services.

Otherwise, private and personal lending of money in return for the repayment with interest is a non-regulated activity in Slovenia even if the lending occurs through online Crowdfunding platform. Therefore, the creditors would not require a licence, but the general civil and commercial rules regarding lending would still apply.

However, the performance of intermediary and agency services with respect to consumer credit and other loan agreements are considered supplementary financial services under the Banking Act and require a licence by the Bank of Slovenia or the Securities Market Agency.

Therefore, the key aspects to consider when adopting the lending model for the Crowdfunding platform are whether the platform will take deposits and/or perform financial services and how the relationship vis-a-vis the lenders and projects is set under the platform's terms.

Depending on the lending model of the Crowdfunding platform licences by the Securities Market Agency and/or the Bank of Slovenia may be required.

### 3.1.1.3 Donations or Rewards Model

Games of chance under the Gaming Act (*Zakon o igráh na srečo*) are games in which participants share the same likelihood of winning a price or reward and where the outcome of the game depends exclusively or predominantly on chance or on another uncertain event. For performance of games of chance a licence or concession granted by the Government of the Republic of Slovenia and of the Ministry of Finance is required.

Individual taxpayers in Slovenia may direct and give up to 0.5% of their personal income tax in a year to a designated recipient as a donation under the Personal Income Tax Act (*Zakon o dohodnini*). To qualify as a recipient of donations that may be paid under direction of a donor out of the donor's personal income tax the recipient must each year apply and qualify as a recipient before the Ministry competent for his business area. Further requirements for recipients are set forth under the Personal Income Tax Act and the Decree of the appropriation

of the personal income tax for donations (*Uredba o namenitvi dela dohodnine za donacije*). Other tax implications may apply to donations received through Crowdfunding.

Depending on how a Donations or Rewards model of the Crowdfunding platform is structured, it might trigger licensing requirement for games of chance and/or the Personal Income Tax Act. Otherwise, Donations and Rewards models are not subject to financial services regulation or licence requirements.

### 3.2 Prospectus requirements

#### (1) General rule

As a general rule nobody may offer securities in the Republic of Slovenia without publishing a prospectus that has been approved by the Securities Market Agency under the Financial Instruments Market Act. By offering of securities of third persons the Crowdfunding platform would likely fall under this requirement as the general rule applies to the same extent to any securities intermediaries. Same prospectus requirements would apply if bonds or other debt financial instruments would be used in a Crowdfunding financing model structure.

#### (2) Exceptions

The prospectus requirement does not apply to the following offering of securities, in the relevant part: (i) hedge funds units, (ii) securities with the guarantee of the state or local government, (iii) offering of securities to sophisticated investors only, (iv) offering of securities to up to 150 natural or legal persons, who are not sophisticated investors, (v) offering of securities with the purchase price above EUR 100.000 for each individual offer of securities in such offering, (vi) offering of securities with nominal value of at least EUR 100.000 for each offered security, or (vii) offering of securities where the aggregate purchase price in the European Union within 12 months does not exceed EUR 100.000. Each subsequent offer of securities purchased under an exception to the prospectus requirement is subject to the general rule under the Financial Instruments Market Act defined above. In other words, each subsequent offer of securities purchased under an exception must rely on an exception or satisfy the prospectus requirement. Prior to any trade of securities on a stock exchange a prospectus must be approved by the Securities Market Agency and published in accordance with the Financial Instruments Market Act.

A limited prospectus requirement applies where the offering price of securities does not exceed EUR 5.000.000 in the European Union within 12 months. In such case, the issuer may replace the prospectus with a simplified prospectus under the Financial Instruments Market Act.

### 3.3 Regulation of Crowdfunding under the AIFMD regime

The AIFMD has recently been implemented into the Slovenian law. The Act on alternative investment fund managers (*Zakon o upraviteljih alternativnih investicijskih skladov*) is a new

piece of legislation, implementing the AIFMD in Slovenia, which has been in force since 23 May 2015. AIFMD has also been implemented through an amendment to the Investment Trusts and Management Companies Act (*Zakon o investicijskih skladih in družbah za upravljanje*).

Entities within the meaning of a collective investment undertaking, which raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors, are currently regulated only by the Investment Trusts and Management Companies Act implementing the UCITS Directive 2009/65/EC. Such entities are investment funds, namely mutual and umbrella funds, defined as funds whose sole purpose is investment in transferable securities and other liquid financial assets on the principle of risk spreading, within the meaning of Article 1 of the UCITS, and investment companies within the meaning of Chapter V of the USTIC. The Non-UCITS open ended investment funds under the Investment Trusts and Management Companies Act are the so called “alternative funds”, defined as funds that do not qualify as hedge or umbrella funds, which underlay more relaxed set of rules for permitted investments (for example precious metal or units of other funds), but require a minimal first investment into the fund in the amount of EUR 100.000. Only investment funds management companies holding a licence by the Securities Market Agency may operate investment funds in Slovenia.

Under the Venture Capital Companies Act (*Zakon o družbah tvegane kapitala*), a venture capital fund may be registered in the form of a joint-stock company, limited liability company, dual company, limited partnership or limited partnerships with share capital, which are all legal entity forms under the Companies Act. A venture capital fund is managed and legally represented by another legal entity and must among other invest at least 50% of the fund's assets in small and medium sized enterprises. The minimal amount of capital investment in the venture capital fund is EUR 50.000. The status of a venture capital fund may only be granted by the Ministry of Economic Development and Technology after the requirements of the Venture Capital Companies Act have been met.

The European Securities and Market Authority (ESMA) in its Guidelines on key concepts of the AIFMD of 13 August 2013 explained that an ordinary company with a general commercial or industrial purpose (i.e. one that pursues a business strategy, which includes running predominantly a commercial activity, involving the purchase, sale, and/or exchange of goods or commodities and/or the supply of non-financial services, or an industrial activity, involving the production of goods or construction of properties, or a combination thereof), would generally not qualify as an alternative investment fund under AIFMD. It is expected that the Securities Market Agency will follow the ESMA Guidelines in applying the Slovenian implementing legislation of the AIFMD to projects financed through Crowdfunding platforms, most notably the Act on alternative investment fund managers (*Zakon o upraviteljih alternativnih investicijskih skladov*).

### **3.3.1 Operating company seeking funding**

An operating company seeking funding would likely not qualify as neither a UCITS or Non-UCITS investment fund nor as a venture capital fund under Slovenian law, if it did not issue fund units for money received or operate an investment fund.

The same could be concluded in relation to the mentioned ESMA Guidelines, namely an ordinary company, common start-ups or emerging companies with a general commercial or industrial purpose seeking funding through a Crowdfunding platform would not qualify as AIFs within the meaning of AIFMD.

### **3.3.2 Project Company seeking funding**

#### **3.3.2.1 Equity Model**

Depending on the equity financing structure of a company established to finance a single project such as for example a movie, a computer game, a wind farm or a solar park (project company), it cannot be excluded that such project company might constitute an AIF under the Investment Trusts and Management Companies Act. It depends on the equity financing structure of a company established to finance a single project such as for example a wind farm, a solar park, a movie or a computer game. The same could be concluded in relation to already mentioned guidelines on key concepts of the AIFMD issued by ESMA, if the Project Company seeking funding is raising capital with the view to investing it in accordance with a defined investment policy.

#### **3.3.2.2 Lending Model**

Depending on the debt financing structure of the project company it cannot be excluded that it might constitute an AIF under regulation that will be adopted for the implementation of the AIFMD. As noted above, performance of intermediary and agency services with respect to consumer credit and other loan agreements are considered supplementary financial services under the Banking Act and require a licence by the Bank of Slovenia or the Securities Market Agency.

#### **3.3.2.3 Donations or Rewards Model**

As noted above, in general donations or rewards based financing structures do not trigger licence requirements or other significant regulatory issues and would likely not constitute an AIF under the current law. However, tax, consumer protection and payment services laws may principally apply.

### **3.3.3 Crowdfunding Platform**

If the Crowdfunding platform through its operations did not seek or raise funds from investors on its own behalf or operate an investment fund it will likely not fall under the regulation implementing the AIFMD in Slovenia. Provision of intermediary and agency services with respect to consumer credit and other loan agreements by a Crowdfunding platform would require a licence by the Bank of Slovenia or the Securities Market Agency.

### 3.4 Licence under the Payment services and systems Act (*Payment Services Directive*)

In addition to any requirements set forth above, a transfer of funds through the Crowdfunding platform will most likely constitute a payment service under the Payment services and systems Act (*Zakon o plačilnih storitvah in sistemih*). Such transfer of funds would occur if the investor, creditor or donor paid and transferred the funds through the Crowdfunding platform to the entrepreneur whereby the Crowdfunding platform performed any of these activities: deposit or withdrawal of cash, payment services for debit or credit of a bank account, issuance or acquisition of payment instruments, remittance of cash payments or transfer of funds by an intermediary between a customer and a provider of goods and services. In Slovenia only banks, licenced electronic money institutions, payment institutions and cash remittance institutions may perform payment services if they were granted a payment services licence by the Bank of Slovenia.

A Crowdfunding platform might however be able to rely on the exemption for “technical service providers” under the Payment services and systems Act, if it outsourced the payment transactions so that it performed only technical services with respect to these payment transactions. Such technical services may include processing and storage of data, data safety and person identification services, IT and communication services, maintenance of payment services equipment and other similar technical services, as long as the provider of such technical services at any time does not have the power to freely dispose with the moneys that are being transferred.

### 3.5 Possible additional Regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Consumer Protection Act (*Zakon o varstvu potrošnikov*)
- Consumer Protection against Unfair Commercial Practices Act (*Zakon o varstvu potrošnikov pred nepoštenimi poslovnimi praksami*)
- Consumer Credit Act (*Zakon o potrošniških kreditih*);
- Prevention of Money Laundering and Terrorist Financing Act (*Zakon o preprečevanju pranja denarja in financiranja terorizma*)
- Book Entry Securities Act (*Zakon o nematerializiranih vrednostnih papirjih*)
- Personal Data Protection Act (*Zakon o varstvu osebnih podatkov*)
- Investment Trusts and Management Companies Act (*Zakon o investicijskih skladih in družbah za upravljanje*)
- Venture Capital Companies Act (*Zakon o družbah tveganega kapitala*)
- Supportive Environment for Entrepreneurship Act (*Zakon o podpornem okolju za podjetništvo*)
- Humanitarian Agencies Act (*Zakon o humanitarnih organizacijah*)

- Code of Obligations (*Obligacijski Zakonik*)
- Prevention of Restriction of Competition Act (*Zakon o preprečevanju omejevanja konkurence*)

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

Under the Slovenian conflict of laws rules, most notably the Private International Law and Procedure Act (*Zakon o mednarodnem zasebnem pravu in postopku*) and the Regulation (EC) No 593/2008 of 17 June 2008 on the law applicable to contractual obligations (Rome I), the seat of the Crowdfunding platform would generally determine the governing law for the contracts for the provision of its services to projects and investors, if the parties did not expressly agree on the governing law.

The Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) and the Banking Act (*Zakon o bančništvu*) regulate the conditions under which entities with seat in another EU member state may perform investment services in Slovenia and the conditions of Slovenian law under which entities with the seat in Slovenia may perform investment services in another EU member state.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addresses Slovenian investors

##### 4.2.1.1 Crowdfunding platform

An EU member state based Crowdfunding platform may provide investment services and activities within the meaning of the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) in Slovenia either through a branch or directly, if it is authorised to provide such services in such EU member state. Direct provision of such services may occur only after the Securities Market Agency received from the supervisory authority of the EU member state, in which the Crowdfunding platform concerned has a registered office, a notification. Such notification shall include a business plan with the description of the type and scope of the intended services and activities in Slovenia and an indication as to whether the Crowdfunding platform intended to use the services of tied agents in Slovenia. In addition to other applicable law, EU member state based Crowdfunding platforms would in Slovenia still be subject to Slovenian laws regulating consumer protection, money laundering prevention and other areas applicable to brokerage companies in the Republic of Slovenia with the aim of protecting public benefits.

Provision of investment services of a Crowdfunding platform from another EU member state through a branch office in Slovenia is also possible, after materially similar notification procedures as mentioned above would apply. Note that under the Companies Act (*Zakon o gospodarskih družbah*), a local branch in Slovenia would not be a legal person, but would be generally be allowed to carry out all operations, which the Crowdfunding platform may carry

out. The Crowdfunding platform from another EU member state would be liable with all its assets for the liabilities arising from the business conduct of its local branches in Slovenia.

#### **4.2.1.2 Company / project**

As a general rule nobody may offer transferrable securities in Slovenia without first publishing a prospectus that has been approved by the Securities Market Agency under the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) or without a prospectus being “passported” into Slovenia. This applies also to an issuer of the securities (i.e. foreign companies) which are presented on the Crowdfunding platforms in another EU member state. By offering of securities of third persons in Slovenia the Crowdfunding platform would likely fall under this requirement as the general rule applies to the same extent to any securities intermediaries. Same prospectus requirements would apply if bonds or other debt financial instruments would be used in a Crowdfunding financing model structure. The decisive factor is the offering of securities itself, namely as soon as the offering is made in Slovenia, then the local financial regulation applies and the prospectus requirement should be observed before the offering is made. The prospectus requirements do not apply in certain cases and there are several exemptions available as explained in more detail in section 3 above.

### **4.2.2 Foreign Crowdfunding platform addresses Slovenian companies**

#### **4.2.2.1 Crowdfunding platform**

In case of a Crowdfunding platform from another EU member state approaching the companies and projects in Slovenia to invite them to be included onto their platform, the sole action of merely approaching the Crowdfunding platform should not be an act regulated by the Slovenian prospectus rules from the prospectus regulation point of view. If the transferrable securities of the approached companies would be included onto the platform and thereby offering of transferrable securities would be made in Slovenia, the same prospectus regulatory rules explained above in the preceding paragraph would apply. Most common types of companies in Slovenia are a limited liability company with business shares. Such shares are not transferrable securities under the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) and the prospectus requirement is not applicable in case funding is made for such type of equity.

#### **4.2.2.2 Company / project**

See our conclusions under point 4.2.1.2 above.

## **4.3 Outbound**

### **4.3.1 Slovenian Crowdfunding platform addresses foreign (EU) investors**

In general we note that, the same requirements and conclusions of Slovenian law discussed in section 3 above would also apply to Crowdfunding crossing borders regardless of

whether the Slovenian Crowdfunding platform, whose operations would be governed under Slovenian law, addressed investors in Slovenia or in another EU country.

#### 4.3.1.1 Crowdfunding platform

A Slovenian Crowdfunding platform that wished to start directly providing investment services and activities within the meaning of the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) in another EU member state would first need to qualify as a brokerage company and would be obliged to notify the Securities Market Agency accordingly. It would also need to indicate the EU member state in which it planned to provide such services directly. A business plan with the description of the type and scope of the intended services and activities in such EU member state must be attached to the notification as well as an indication as to whether the Crowdfunding platform intended to use the services of tied agents in that EU member state. The Securities Market Agency would then submit the notification together with the enclosures to the supervisory authority of the EU member state, and would notify the Crowdfunding platform accordingly. The platform would be allowed to commence directly providing so notified investment services and activities in another EU member state on the day the supervisory authority of that member state received the notification of the Securities Market Agency.

Provision of investment services of a Slovenian Crowdfunding platform in another EU member state through a branch office in such member state is also possible and material similar notification procedures apply, but the Securities Market Agency may refuse to submit the respective notification to the supervisory authority of such other EU member state, if it established, taking into consideration the planned volume and type of operation the platform planned to perform through the branch, that reasonable doubt exists as to whether the organisation and management of the branch or the platform's financial standing are adequate.

#### 4.3.1.2 Company / project

If a Crowdfunding platform from Slovenia addressed only investors in another EU country and the offering would not take place in Slovenia, the Slovenian prospectus regulation would not apply. The Slovenian prospectus regulation would likewise not apply, if a Crowdfunding platform from Slovenia addressed only companies or projects in another EU country and the offering would not take place in Slovenia.

In most instances when a foreign investor generates revenue from investments in Slovenia, he must first obtain a tax identification number from the Slovenian Financial Administration, which is a formality that may generate administrative and compliance problems for a Crowdfunding platform. Namely, tax identification numbers are issued only upon application in person at the counter of the Slovenian Financial Administration or in writing sent through postal service. Acquisition of the tax identification numbers through a written power of attorney is possible. Considering the above, the acquisition may take some time and additional administration, because electronic filing of the application is not available.

### 4.3.2 Slovenian Crowdfunding platform addresses foreign companies / projects

#### 4.3.2.1 Crowdfunding platform

See our conclusions in section 4.3.1.1 above.

#### 4.3.2.2 Company / project

See our conclusions in section 4.3.1.2 above.

### 4.4 Impact of EU regulation

The EU Prospectus Directive and the MiFID (II) are implemented into the Slovenian rules governed under the Financial Instruments Market Act (*Zakon o trgu finančnih instrumentov*) and the Payment Services Directive is implemented into Slovenian legislation with the Payment services and systems Act (*Zakon o plačilnih storitvah in sistemih*). Furthermore, the AIFMD has recently been implemented into the Slovenian law, namely through the Act on alternative investment fund managers (*Zakon o upraviteljih alternativnih investicijskih skladov*) and an amendment to the Investment Trusts and Management Companies Act (*Zakon o investicijskih skladih in družbah za upravljanje*).

### 4.5 Summary

Due to harmonization of the EU financial regulation laws, as explained above in 4.4 (Impact of EU regulation), it is much easier for EU Crowdfunding platforms to enter the Slovenian market than it is for third country Crowdfunding platforms. The same is true for Slovenian Crowdfunding platforms trying to enter foreign markets.

While it is true that within the EU, the Crowdfunding platforms can take advantage of the EU passporting system and harmonized legislation, due to the lack of EU Crowdfunding specific legislation, significant entry barriers continue to exist for Crowdfunding platforms, both inbound and outbound.

## 5 Lessons learned from Slovenia's regulation for a possible harmonized European Crowdfunding regulation

### 5.1 Role model ("dos")

The possibility for taxpayers to give qualified non-state recipients a portion of their yearly personal income tax as a donation is widely perceived as a good practice.

Prospectus requirement exception, most notably the threshold for an offering of securities where the aggregate purchase price in the European Union within 12 months does not exceed EUR 100.000 is welcomed by many start-up raising money through Crowdfunding. Therefore, some organizations active in Crowdfunding are pushing for the increase of the threshold to EUR 500.000.

Most licencing requirements with respect to payment services and the activity of taking of deposits may be avoided when a Crowdfunding platform cooperates with a bank or another

appropriately licensed payment or credit institution which handles the payments instead of the Crowdfunding platform.

## 5.2 Aspects that should be avoided ('don'ts')

Applying certain administrative burdens, like the requirement of obtaining a tax identification number by the investors in another EU member state, which cannot be issued or administrated electronically, may delay or obstruct the cross-border functioning of a Crowdfunding platform.

## 6 Conclusion

Crowdfunding is not per se a heavily or specifically regulated business in Slovenia, but various regulatory and compliance issues might arise based on existing regulation of the financial instruments and markets, banking and payment services industries. In addition, the operation and investment through a Crowdfunding platform may have tax, consumer protection, game of chance and other legal implications that require attention.

## 7 Summary – Crowdfunding regulation

| Country   | Slovenia  |
|---|---|
| <b>Summary</b>  |   |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• AIFMD was implemented through the Act on Alternative Investment Fund Managers (<i>Zakon o upraviteljih alternativnih investicijskih skladov</i>), which entered into force on 23 May 2015, and an amendment to the Investment Trusts and Management Companies Act (<i>Zakon o investicijskih skladih in družbah za upravljanje</i>), which entered into force on 19 May 2015.</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |   |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• Financial services and transactions related to offerings of securities provided by a Crowdfunding platform trigger requirement for a licence by the Securities Market Agency</li> <li>• Intermediary services with respect to consumer credit and other loan agreements require a licence by the Bank of Slovenia or the Securities Market Agency</li> <li>• Donations and Reward Crowdfunding models would among others likely have tax, game of chance and consumer protection legal implications</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• Prospectus requirement for offer of <b>securities</b></li> <li>• Threshold: <b>EUR 100.000</b> in the European Union within 12 months</li> <li>• Other most relevant exceptions: (i) offering of securities to sophisticated investors only, or (ii) offering of securities to up to 150 natural or legal persons, who are not sophisticated investors</li> <li>• Simplified prospectus possible for offerings of securities below or equal to EUR 5.000.000 in the European Union within 12 months</li> </ul> |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• AIFMD has not yet been implemented in Slovenia</li> <li>• AIFs presently regulated by the Investment Trusts and Management Companies Act and the Venture Capital Companies Act</li> <li>• Crowdfunding platform might fall under the AIF regulation and future regulation implementing the AIFMD in Slovenia</li> </ul> <p>Intermediary services with respect to consumer credit and other loan agreements would require a licence by the Bank of Slovenia or the Securities Market Agency</p>                 |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• Remittance of cash payments or transfer of funds by an intermediary between a customer and a provider of goods and services constitutes provision of payment services, which requires a licence by the Bank of Slovenia.</li> <li>• A Crowdfunding platform might rely on the “technical service provider” exemption.</li> </ul>   |

|   |  |
|---|--|
| <p><b>Consumer credit regulation</b></p>                            | <ul style="list-style-type: none"> <li>• Consumer Credit Act (<i>Zakon o potrošniških kreditih</i>) regulating the content and offering of consumer credit applies only to credit and loan agreements entered into with natural persons who are acting as consumers, which means acting outside of their employment or gainful activity.</li> </ul>  |
| <p><b>Further possible requirements</b></p>                         | <ul style="list-style-type: none"> <li>• Consumer Protection Act (<i>Zakon o varstvu potrošnikov</i>)</li> <li>• Consumer Protection against Unfair Commercial Practices Act (<i>Zakon o varstvu potrošnikov pred nepoštenimi poslovnimi praksami</i>)</li> <li>• Prevention of Money Laundering and Terrorist Financing Act (<i>Zakon o preprečevanju pranja denarja in financiranja terorizma</i>)</li> <li>• Book Entry Securities Act (<i>Zakon o nematerializiranih vrednostnih papirjih</i>)</li> <li>• Personal Data Protection Act (<i>Zakon o varstvu osebnih podatkov</i>)</li> <li>• Investment Trusts and Management Companies Act (<i>Zakon o investicijskih skladih in družbah za upravljanje</i>)</li> <li>• Venture Capital Companies Act (<i>Zakon o družbah tveganega kapitala</i>)</li> <li>• Supportive Environment for Entrepreneurship Act (<i>Zakon o podpornem okolju za podjetništvo</i>)</li> <li>• Humanitarian Agencies Act (<i>Zakon o humanitarnih organizacijah</i>)</li> <li>• Code of Obligations (<i>Obligacijski Zakonik</i>)</li> <li>• Prevention of Restriction of Competition Act (<i>Zakon o preprečevanju omejevanja konkurence</i>)</li> </ul> |
| <p><b>Regulatory barriers for Crowdfunding crossing borders</b></p> |  |
| <p><b>General</b></p>   | <ul style="list-style-type: none"> <li>• The seat of the Crowdfunding platform would generally determine the governing law for the contracts for the provision of its services to projects and investors, if the parties did not expressly agree on the governing law</li> <li>• The same requirements and conclusions of Slovenian law discussed above would also apply to Crowdfunding crossing borders regardless of whether the Slovenian Crowdfunding platform, addressed investors in Slovenia or in another EU country</li> </ul>   |
| <p><b>Inbound</b></p>   | <ul style="list-style-type: none"> <li>• The Financial Instruments Market Act (<i>Zakon o trgu finančnih instrumentov</i>) and the Banking Act (<i>Zakon o bančništvu</i>) apply</li> <li>• A EU member state based Crowdfunding platform may provide investment services and activities in Slovenia either through a branch or directly</li> <li>• Notification and “passporting” procedures apply</li> <li>• The Crowdfunding platform would be liable with all its assets for the liabilities arising from the business conduct of its local branches in Slovenia</li> <li>• The prospectus requirements would apply in cases where securities (debt or equity) were offered in Slovenia, unless an exception detailed above applies</li> </ul>   |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>• A prospectus may be approved by the Securities Market Agency or it may be “passported” into Slovenia</li> </ul>   |
| <b>Outbound</b>                | <ul style="list-style-type: none"> <li>• The Financial Instruments Market Act (<i>Zakon o trgu finančnih instrumentov</i>) and the Banking Act (<i>Zakon o bančništvu</i>) apply</li> <li>• Notification and “passporting” procedures apply</li> <li>• The Securities Market Agency may refuse to submit the respective notification to the supervisory authority of another EU member state, if that reasonable doubt exists as to whether the organisation and management of the branch or the platform's financial standing are adequate</li> <li>• If a Crowdfunding platform from Slovenia addressed only investors and/or only companies and projects in another EU country and the offering would not take place in Slovenia, the Slovenian prospectus regulation would not apply.</li> </ul> |
| <b>Impact of EU regulation</b> |  |
| <b>Prospectus regulations</b>  | <ul style="list-style-type: none"> <li>• The EU Prospectus Directive is implemented into the Slovenian rules governed under the Financial Instruments Market Act (<i>Zakon o trgu finančnih instrumentov</i>).</li> </ul>  |
| <b>AIFM-Directive</b>          | <ul style="list-style-type: none"> <li>• The AIFMD has recently been implemented into the Slovenian law, namely through the Act on alternative investment fund managers (<i>Zakon o upraviteljih alternativnih investicijskih skladov</i>) and an amendment to the Investment Trusts and Management Companies Act (<i>Zakon o investicijskih skladih in družbah za upravljanje</i>).</li> </ul>  |
| <b>MiFID / MiFID II</b>        | <ul style="list-style-type: none"> <li>• The MiFID (II) is implemented into the Slovenian rules governed under the Financial Instruments Market Act (<i>Zakon o trgu finančnih instrumentov</i>).</li> </ul>   |
| <b>PSD / PSD II</b>            | <ul style="list-style-type: none"> <li>• The Payment Services Directive is implemented into Slovenian legislation with the Payment services and systems Act (<i>Zakon o plačilnih storitvah in sistemih</i>).</li> </ul>   |

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# Spain

## 1 Recent developments in the Crowdfunding market in Spain

Over recent years there have been the following significant developments in Spain regarding Crowdfunding:

### 1.1 The Equity Model / Lending Model

In 2016, Equity and Lending based Crowdfunding has had the biggest growth rate of all of the Crowdfunding sectors and a market share of more than 50%. In particular, 29% of Crowdfunding platforms operate under the Lending Model and 25% under the Equity Model.

Since the passing of the Promotion of Corporate Finance Act 5/2015 of 27 April (*Ley 5/2015, de 27 de abril, de fomento de la financiación empresarial*) ("**LFFE**"), the Spanish Stock Market Commission ("**CNMV**") has authorised and registered a total number of 8 equity Crowdfunding platforms, 8 lending Crowdfunding platforms and 3 mixed lending and equity Crowdfunding platforms.

Notwithstanding the foregoing, there are a few Crowdfunding platforms that are operating without the mandatory administrative authorisation due to their problems in meeting the high financial requirements established by the LFFE.

### 1.2 The Donations or Rewards Model

In Spain, the Rewards Model has a market share of 36%. This means that despite the exponential growth of Equity and Lending models in 2016, the most popular model of the Spanish Crowdfunding market is still the Rewards Model, with approximately 25 platforms currently operating in Spain. Under this traditional Rewards Model, individuals provide funds to a specific project (normally cultural) by means of contributions in cash, in exchange for a reward or consideration.

The Donations Model, which has a market share of 10%, is based on contributions from users, in the form of donations, to support specific projects of social aid managed by organisations (generally NGOs), associations or individuals as a non-profit organisation. No financial investment or return is involved.

### 1.3 Real Estate Crowdfunding / Renewable Crowdfunding

#### 1.3.1 Real Estate Crowdfunding

In Spain, Real Estate Crowdfunding platforms follow both Equity and Lending Models and are currently expanding their business rapidly. The Real Estate Crowdfunding business closed 2016 with approximately 4 Crowdfunding platforms operating in the alternative investment market and have made investments of more than EUR 3,500 million..

This type of Crowdfunding platform raises capital in order to buy houses for the purposes of renting them during a period of time and/or to invest in the refurbishment of houses for the

purposes of selling them to families. Under this Real Estate Crowdfunding model, investors receive their incomes through the rents paid by the lessees and/or through the future revaluation resulting from the selling of the house.

The problem in the Real Estate Crowdfunding market is that none of the operating platforms are registered and authorised by the CNMV due to the legal limbo in which they are living. Real Estate Crowdfunding platforms are in a conflict of interest situation caused by the problem of separating both the status of promoter and that of Crowdfunding platform. The CNMV, together with the Spanish Government, are expected to make changes to Crowdfunding legislation in this regard.

### 1.3.2 Renewable Crowdfunding

Most operations carried out in the Spanish renewable energy market involve the acquisition of PV power plants and wind farms. Since 2012, the Spanish government has passed a plan of action to modify the renewable energies regime, which also includes plans to cut the feed-in-tariffs for all kinds of renewable energy projects.

In this context, Spain must rethink the place that renewable energy and citizens occupy in the energy system. Despite having been a leader in investment and innovation, it may now be in the wilderness compared to its neighbours. However, due to the actions of the Spanish Government, the growth of renewable energy has almost ceased and Spain will not fulfill its binding national target of reaching 20% of renewable energy in the final gross energy demand by 2020, as stipulated in Directive 2009/28/EC (Renewable Energy Directive).

Despite the growth of renewables in Spain in the past decade, little was done regarding citizen or community involvement. However, citizen participation has increased lately??. Without a supportive framework, this nascent industry cannot reach its full potential.

Most of the funds are invested in renewable energy projects through different products and finance services such as Project Finance, private equity fund investments, venture capital, photovoltaic leasing, sale and leaseback and bridge equity.

Renewable Crowdfunding in Spain has not yet reached the highest levels of importance in financing RES Projects, although its importance is expected to continue to increase. Some of the Renewable Crowdfunding projects that use Crowdfunding platforms in Spain are:

- Project "Enertika and ECrowd" which target a set of energy efficient measures implemented in base stations of mobile telephony without electricity grid connection, distributed in different parts of Spain.
  - These actions allow an annual reduction of approximately 320,000 kg of CO2 emissions to the atmosphere, equivalent to the energy consumption of 111 homes of 90 m2 or the planting of 32,000 trees. The improvements were financed through investments made by the Lending based Crowdfunding platform "ECrowd!". In total, EUR 140,000 has been raised from 127 investors.

- Project "Mar de Fulles". This is a new ecotourism concept, which defines itself as a sustainable environmental management system network. This environmental management system consists in the bioclimatic construction of a tourist complex located next to the Natural Park of the Sierra de Espadán (Castellón) and Special Protection Area (SPA) of the Natura 2000 NET. It is an innovative and pioneering project in Spain that encompasses the concepts of ecology, sustainability and energy efficiency at the highest level. The construction is ecofriendly with the forest plots following the strictest landscape integration criteria.
  - The only source of electricity of "Mar de Fulles" will be obtained from photovoltaic solar panels with support batteries. The purpose of this project is precisely the financing of the solar energy collection facility and the battery support that will allow the total self-supply of electric energy. EUR 174,000 has been raised.
- Project "ELECTROLINERA". A project to create a new station for the sale and fast loading of electric vehicles, equipped with solar panels and 100% renewable sourced energy, in the town of La Granja (Segovia).
  - This first sustainable station is located next to the National Parador de La Granja, close to Segovia and is part of a network of fast electric recharge stations that will start off with 7 stations located in strategic points of the Segovia province. It is an ambitious expansion plan for up to 200 stations by the end of 2020.
  - During the solar energy production hours, electric vehicles will be charged directly from the energy captured by the solar panels, whereas for the rest of the hours or in the event of bad weather, the stations have a 100% renewable energy supply. EUR 82,400 has been raised.

#### 1.4 International approach

It is expected that equity Crowdfunding will consolidate in the Spanish market as one of the main financing options. The access to the Spanish market of a greater and more professionalised and international number of investors will permit the closing of higher financing rounds. The option to international rounds will offer new opportunities to potential Spanish entrepreneurs.

## 2 Recent developments regarding Crowdfunding regulations in Spain

There have been no developments regarding Crowdfunding regulations in Spain since the passing of the LFFE on 29 April 2015. However, as mentioned, changes to the LFFE are expected to be implemented due to the legal limbo that Real Estate Crowdfunding platforms are experiencing.

The LFFE regulates the legal framework of peer-to-peer lending and equity Crowdfunding platforms and excludes Rewards and Donations Models, sale of goods and services and interest-free loans from its scope of application.

Crowdfunding platforms can obtain the necessary financing for a business project through the convergence of supply and demand provided by them. Crowdfunding platforms are

authorised companies whose activity consists of contacting, in a professional manner and through websites or other electronic means, a multiplicity of individuals or legal entities who provide funding in exchange for a monetary return, so-called investors and promoters who apply on their own behalf for funding to be earmarked exclusively for a specific project which, as pointed out by the LFFE, can only be a business, education or consumer related project.

These financing projects could be implemented through:

- The issue or subscription of bonds, ordinary and preferential shares or other securities representing the capital, when it does not require prospectus in accordance with the Royal Legislative Decree 4/2015, 23 October, which approves the consolidated version of Act 24/1988 of 28 July, on the Securities Market (texto refundido de la Ley de Mercado de Valores) ("LMV").
- The issue or subscription of shares in limited liability companies.
- The application for loans, including subordinated profit-participating loans.

The Equity Model is based on the contribution of funds that is conducted by the issue or subscription of shares or other financial instruments representing the capital, either as part of a process of incorporation of a company or through a capital increase. In this Equity Model, the investor receives the economic and political rights inherent to the status of shareholder of a company that receives the funds in return for the funding provided. Under this Equity Model, the investor can also subscribe bonds issued, either by a public limited company or a limited liability company, as the LFFE has opened the possibility of issuing simple bonds (not convertible bonds) to these limited liability companies.

The Lending Model is the other form of Crowdfunding regulated under the LFFE. Under this Lending Model, platforms act as intermediaries (or match-makers) through which investors (i.e. the lenders) and promoters (i.e. the borrowers) can interact directly with each other in order to provide unsecured loans. They are not considered as actual intermediaries that raise repayable funds from the public because they do not grant the repayment of the loan under certain conditions. However, each project passes through a strict process of risk assessment in order to provide the investor with proof of the solvency of the promoter and the interest associated to it.

The LFFE permits a Crowdfunding platform to grant loans or credits only if it invests in a project published on its web site without exceeding 10% of the funding target.

The financing obtained for the development of a specific project through Equity and Lending Crowdfunding platforms shall, under no circumstances, be assigned to:

- Professional financing of third parties and, in particular, the granting of credits or loans.
- The subscription or acquisition of shares, bonds and other financial instruments admitted for trading on a regulated market, on a multilateral trading system or equivalent third country markets.

- The subscription or acquisition of stocks and shares of collective investment schemes or their management companies, venture capital entities, other collective investment entities of a closed-ended type and management companies of other collective investment entities of a closed-ended type.

### 3 Current Regulation of Crowdfunding in Spain

#### 3.1 Licence under the Promotion of Corporate Finance Act (Ley 5/2015, de 27 de abril, de fomento de la financiación empresarial)

##### 3.1.1 Equity Model / Lending Model

###### 3.1.1.1 General Rule

The CNMV is the competent body in Spain to authorise and register Crowdfunding platforms, following a mandatory and binding report by the Bank of Spain in the case of platforms that publish projects related to applications for loans, including subordinated profit-participating loans.

The LFFE sets forth a number of requirements for an entity to obtain and maintain authorisation as a Crowdfunding platform so that it can operate in the Spanish market, which are as follows:

- Have the exclusive corporate purpose for carrying out activities that are individual to Crowdfunding platforms and, where appropriate, the activities of a hybrid payment institution.
- Have its registered office and effective administration and management in the Spanish territory or in another Member State of the European Union.
- Adopt the form of a capital company for an indefinite period.
- That the platform managers are persons of recognized business and professional repute and possess appropriate knowledge and experience in the areas necessary for the exercise of their functions.
- Have a good administrative and accounting structure or adequate internal control procedures.
- Have adequate means to ensure the security, confidentiality and reliability to provide the service by electronic means.
- Have an internal code of conduct that addresses potential conflicts of interest and the terms of the participation of directors, officers, employees and representatives in funding applications that are implemented through the Crowdfunding platform.
- Provide mechanisms so that, in the case of cessation of its activity, it may continue providing all or part of the services which it undertook to provide to the Crowdfunding projects for which they obtained funding.

At the same time the LFFE points out the financial requirements to be met by these Crowdfunding platforms:

A. Those which must be provided at all times:

- A social capital fully paid in cash of at least EUR 60,000, or
- Professional liability insurance, a guarantee or other equivalent assurance that deals with responsibility for negligence in the exercise of their professional activity, with a minimum coverage of EUR 300,000 for each claim, and a total of EUR 400,000 per year for all claims, or
- A combination of initial capital and professional indemnity insurance, guarantee or other equivalent assurance which results in a coverage level equivalent to that indicated in the preceding two paragraphs.

B. When the amount of the financing obtained in the last 12 months for the projects published on the platform exceeds EUR 2 million, the Crowdfunding platforms must have at least EUR 120,000 of their own resources.

- Its total own resources will be increased depending on the total amount of the financing obtained in the last 12 months for projects published on the platform.

### 3.1.1.2 Exemptions from licensing requirement

No exemptions from licensing requirement are provided by the LFFE.

### 3.1.2 Donations or Rewards Model

As already stated, the Spanish framework only regulates cases in which the investors receive an economic remuneration in return for the funding provided, with the Donations and Rewards Models being excluded from the LFFE, therefore no license is required.

## 3.2 Prospectus requirements

### 3.2.1 Equity Model / Lending Model

In general, public stock, share and bond offerings through the Crowdfunding platforms are not subject to the national provisions of the LMV regarding issue of securities in the primary market, since the legislator limits the operational scope of Crowdfunding platforms for those issues in which the existing regulation on the primary market is not applied.

Thus, LFFE highlights that Crowdfunding projects can be implemented by means of issue or subscription of bonds, ordinary and preferential shares or other securities representing the capital, when it does not require prospectus in accordance with the LMV.

Under the LMV the obligation to publish a prospectus shall not apply to any of the following types of offering (which shall not be considered to be public offerings for the purposes of the LMV):

- A. An offering of securities exclusively addressed to qualified investors.
- B. An offering of securities addressed to less than 150 natural or legal persons per Member State, without including qualified investors.

- C. An offering of securities addressed to investors who acquire securities for a total consideration of at least EUR 100,000 each, per offering.
- D. An offering of securities whose unit nominal value amounts to at least EUR 100,000.
- E. An offering of securities amounting to a total of less than EUR 5 million in the European Union, which limit shall be calculated over a period of 12 months.

On the other hand, the LFFE sets a fixed limit of EUR 5 million as a maximum amount of funds that a Crowdfunding project can raise on a yearly basis, provided that it is exclusively targeted to accredited investors (if it is targeted to non-accredited investors this fixed limit will be set at EUR 2 million). This limit of EUR 5 million also corresponds to the maximum limit that, in accordance with the LMV, can allow securities offerings to be exempt from the obligation to publish the prospectus.

A defect affecting this regulation is that there is no adequate coordination between the LMV and the LFFE, given that the LMV establishes the limits on the raising of capital without the need for a prospectus in relation to a single offering, whereas the LFFE fixes the limits on raising capital in relation to a specific Crowdfunding project. Certainly, the LFFE prohibits a promoter from publishing simultaneously more than one project on one platform, but nothing prevents such a promoter from raising funds for various projects on different platforms and, hence, from acquiring substantial amounts of money in a short time.

### 3.2.2 Donations or Rewards Model

As mentioned above, in this model the publication of a prospectus is not mandatory regardless of whether it is excluded from the LFFE.

## 3.3 Regulation of Crowdfunding under the AIFMD regime

Prior to the approval and entry into force in Spain of the LFFE and Act 22/2014 of 12 November, which regulates venture capital entities, other collective investment entities of a closed-ended type and management companies of other collective investment entities of a closed-ended type ("Act 22/2014"), which transposes AIFMD, the possibility that Crowdfunding platforms could be considered as managers of alternative investment funds was an unclear issue. Unlike other jurisdictions, neither the CNMV nor Act 22/2014 have included a specific definition of Alternative Investment Fund, and what is more, Act 22/2014 defines collective investment entities in the same way as the AIFMD defines Alternative Investment Fund.

Faced with the normal functioning of public offerings for subscription under the LMV, the primary market generated by Spanish Crowdfunding presents a relevant singularity consisting of the necessary intermediation of a Crowdfunding platform. With the regulation of the platforms, the LFFE establishes a new intermediary category in the financing market, reserving the activity of contacting, in a professional manner, investors and promoters, through websites or other electronic means.

In particular, Crowdfunding platforms shall provide the following mandatory services:

- Receipt, selection and publication of Crowdfunding projects, and
- Development, establishment and operation of communication channels to facilitate the search for funding between investors and promoters.

Also, Crowdfunding platforms may provide, among others, the following ancillary services:

- Advice to promoters in relation to the publication of the project including the provision of services and advice in the information technology, marketing, advertisement and design fields.
- Project analysis, determination of the level of risk for investors, not being considered as financial advice the publication, classification and aggregation of such information in objective terms.
- Make available to the parties the templates of the contracts that are necessary to participate in the projects.
- The judicial or extrajudicial claim of the credit rights, acting on behalf of investors, or on their own behalf if investors assign such credit rights to them.

At the same time, the LFFE prohibits Crowdfunding platforms from publishing projects through which promoters assign the funds raised to the subscription or acquisition of stocks and shares of collective investment schemes or their management companies, venture capital entities, other collective investment entities of a closed-ended type and management companies of other collective investment entities of a closed-ended type.

Based on the aforementioned, setting such activities as the sole activities that Crowdfunding platforms can conduct while outlining activities that are expressly prohibited, the uncertainty about the possibility for the platforms to be considered as managers of AIFs has been clarified.

### 3.4 Regulation under the Payment Services Directive

The LFFE prohibits Crowdfunding platforms from exercising the activities reserved to payment institutions and, especially, from receiving funds in order to pay on behalf of investors or promoters, without the platform being authorised as a hybrid payment institution in accordance with the Payment Services Act 16/2009 of 13 November (*Ley 16/2009, de 13 de noviembre, de servicios de pago*).

In addition to the CNMV authorisation, the Spanish Payment Services Act states that to perform the services of a hybrid payment institution, the Crowdfunding platform must submit an application to the minister of Economy and Competitiveness to be authorised as a payment institution, after a consultation with the Bank of Spain and the Executive Service of the Commission for the Prevention of Money Laundering and Monetary Offences.

### 3.5 Possible additional regulations

Other common regulations to which the operator of a Crowdfunding platform may be subject include:

- Consumer contracting loans or mortgage and brokerage services for the conclusion of contracts of loan or credit Act 2/2009 of 31 March (*Ley 2/2009, de 31 de marzo, por la que se regula la contratación con los consumidores de préstamos o créditos hipotecarios y de servicios de intermediación para la celebración de contratos de préstamo o crédito*);
- Consumer credit contracts Act 16/2011 of 24 June (*Ley 16/2011, de 24 de junio, de contratos de crédito al consumo*);
- General Contracting Terms Act 7/1998 of 13 April (*Ley 7/1998, de 13 de abril, sobre condiciones generales de la contratación*);
- Protection of Consumers and Users Act 1/2007 of 16 November (*Real Decreto Legislativo 1/2007, de 16 de noviembre, por el que se aprueba el texto refundido de la Ley General para la Defensa de los Consumidores y Usuarios y otras leyes complementarias*);
- Money Laundering and Terrorist Financing Prevention Act 10/2010 of 28 April (*Ley 10/2010, de 28 de abril, de prevención del blanqueo de capitales y de la financiación del terrorismo*);
- Personal Data Protection Act 15/1999 of 13 December (*Ley Orgánica 15/1999, de 13 de diciembre, de Protección de Datos de Carácter Personal*).

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

LFFE follows a marketing focused approach.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addresses Spanish investors

LFFE can apply to foreign Crowdfunding platforms that announce, promote or attract investors or potential investors in Spain, and/or address its services specifically to investors residing in Spanish territory. Therefore, such foreign Crowdfunding platforms and the Spanish investors shall comply with the LFFE and CNMV regulations.

For the avoidance of doubt, the LFFE does not apply to investors residing in Spain that participate in foreign Crowdfunding platforms at their own initiative since it is considered that the services provided by such foreign Crowdfunding platforms are not provided in the Spanish territory. In this case, Spanish investors shall not have to comply with the LFFE and CNMV regulations.

##### 4.2.1.1 Foreign Crowdfunding platforms

As mentioned above, foreign Crowdfunding platforms shall have to apply to CNMV for authorization as a Crowdfunding platform and to register in CNMV's Registry.

The requirements for foreign Crowdfunding platforms to obtain and maintain authorisation as a Crowdfunding platform so that it can operate in the Spanish market are:

- Have the exclusive corporate purpose for carrying out activities that are individual to Crowdfunding platforms and, where appropriate, the activities of a hybrid payment institution.
- Have its registered office and effective administration and management in the Spanish territory or in another Member State of the European Union.
- Adopt the form of a capital company for an indefinite period.
- That the platform managers are persons of recognized business and professional repute and possess appropriate knowledge and experience in the areas necessary for the exercise of their functions.
- Have a good administrative and accounting structure or adequate internal control procedures.
- Have adequate means to ensure the security, confidentiality and reliability to provide the service by electronic means.
- Have an internal code of conduct that addresses potential conflicts of interest and the terms of the participation of directors, officers, employees and representatives in funding applications that are implemented through the Crowdfunding platform.
- Provide mechanisms so that, in the case of cessation of its activity, it may continue providing all or part of the services which it undertook to provide to the Crowdfunding projects for which they obtained funding.

At the same time the LFFE points out the financial requirements to be met by these foreign Crowdfunding platforms:

A. Those which must be provided at all times:

- A social capital fully paid in cash of at least EUR 60,000, or
- Professional liability insurance, a guarantee or other equivalent assurance that deals with responsibility for negligence in the exercise of their professional activity, with a minimum coverage of EUR 300,000 for each claim, and a total of EUR 400,000 per year for all claims, or
- A combination of initial capital and professional indemnity insurance, guarantee or other equivalent assurance which results in a coverage level equivalent to that indicated in the preceding two paragraphs.

B. When the amount of the financing obtained in the last 12 months for the projects published on the platform exceeds EUR 2 million, the Crowdfunding platforms must have at least EUR 120,000 of their own resources.

C. Its total own resources will be increased depending on the total amount of the financing obtained in the last 12 months for projects published on the platform.

#### 4.2.1.2 Foreign promoters seeking funding

- The LFFE prohibits a promoter from publishing simultaneously more than one project on one platform

- The LFFE sets a fixed limit of EUR 5 million as a maximum amount of funds that a Crowdfunding project can raise on a yearly basis, provided that it is exclusively targeted to accredited investors (if it is targeted to non-accredited investors this fixed limit will be set at EUR 2 million).
- LFFE establishes main information obligations regarding the loan or the issue (description of the essential features and risks associated to, form, rights and obligations of the parties...etc).

#### **4.2.2 Foreign Crowdfunding platform addresses Spanish promoters**

LFFE can apply to foreign Crowdfunding platforms that announce, promote or attract promoters or potential promoters in Spain, and/or address its services specifically to promoters residing in Spanish territory. Therefore, such foreign Crowdfunding platforms and the Spanish promoters shall comply with the LFFE and CNMV regulations.

For the avoidance of doubt, the LFFE does not apply to promoters residing in Spain that participate in foreign Crowdfunding platforms at their own initiative since it is considered that the services provided by such foreign Crowdfunding platforms are not provided in the Spanish territory. In this case, Spanish promoters shall not have to comply with the LFFE and CNMV regulations.

##### **4.2.2.1 Foreign Crowdfunding platforms**

As mentioned above, foreign Crowdfunding platforms shall have to apply to CNMV for authorization as a Crowdfunding platform and to register in CNMV's Registry.

The requirements for foreign Crowdfunding platforms to obtain and maintain authorisation as a Crowdfunding platform so that it can operate in the Spanish market are:

- Have the exclusive corporate purpose for carrying out activities that are individual to Crowdfunding platforms and, where appropriate, the activities of a hybrid payment institution.
- Have its registered office and effective administration and management in the Spanish territory or in another Member State of the European Union.
- Adopt the form of a capital company for an indefinite period.
- That the platform managers are persons of recognized business and professional repute and possess appropriate knowledge and experience in the areas necessary for the exercise of their functions.
- Have a good administrative and accounting structure or adequate internal control procedures.
- Have adequate means to ensure the security, confidentiality and reliability to provide the service by electronic means.
- Have an internal code of conduct that addresses potential conflicts of interest and the terms of the participation of directors, officers, employees and representatives in funding applications that are implemented through the Crowdfunding platform.

- Provide mechanisms so that, in the case of cessation of its activity, it may continue providing all or part of the services which it undertook to provide to the Crowdfunding projects for which they obtained funding.

At the same time the LFFE points out the financial requirements to be met by these foreign Crowdfunding platforms:

A. Those which must be provided at all times:

- A social capital fully paid in cash of at least EUR 60,000, or
- Professional liability insurance, a guarantee or other equivalent assurance that deals with responsibility for negligence in the exercise of their professional activity, with a minimum coverage of EUR 300,000 for each claim, and a total of EUR 400,000 per year for all claims, or
- A combination of initial capital and professional indemnity insurance, guarantee or other equivalent assurance which results in a coverage level equivalent to that indicated in the preceding two paragraphs.

B. When the amount of the financing obtained in the last 12 months for the projects published on the platform exceeds EUR 2 million, the Crowdfunding platforms must have at least EUR 120,000 of their own resources.

C. Its total own resources will be increased depending on the total amount of the financing obtained in the last 12 months for projects published on the platform.

#### 4.2.2.2 Promoters

- The LFFE requires promoters to be validly incorporated (or, in the case of an individual, to have its tax residence) in Spain or in any other EU member State.
- The LFFE prohibits a promoter from publishing simultaneously more than one project on one platform
- The LFFE sets a fixed limit of EUR 5 million as a maximum amount of funds that a Crowdfunding project can raise on a yearly basis, provided that it is exclusively targeted to accredited investors (if it is targeted to non-accredited investors this fixed limit will be set at EUR 2 million).
- LFFE establishes main information obligations regarding the loan or the issue (description of the essential features and risks associated to, form, rights and obligations of the parties...etc).

### 4.3 Outbound

#### 4.3.1 Spanish Crowdfunding platform addresses foreign (EU) investors

Spanish regulatory law is not clear in respect of which is the regime applicable to a Spanish Crowdfunding platform that enters EU markets and therefore addresses foreign investors.

LFFE expressly considers that (i) only Crowdfunding platforms that provide services in the Spanish territory and (ii) investors and promoters participating in the aforementioned

Crowdfunding platforms, will be under its scope of application. Also, LFFE clarifies that it won't be consider that a service is provided in the Spanish territory if a Spanish investor or promoter participates on its own initiative in a foreign Crowdfunding platform.

On the contrary, there is no Spanish regulation of which is the applicable law when a Spanish Crowdfunding platform addresses foreign investors or promoters.

However, in the case that not only foreign investors are addressed but also Spanish promoters, a restrictive interpretation of Spanish regulatory law should be applied. Therefore, in this case, Spanish Crowdfunding platform could provide services in the Spanish territory as it approaches Spanish promoters; therefore Spanish regulatory law is (likely) applicable.

In the case that a Spanish Crowdfunding platform publishes foreign projects that are addressed to foreign investors, Spanish regulatory law is (likely) not applicable since the Spanish Crowdfunding platform does not target the Spanish market.

#### **4.3.1.1 Spanish Crowdfunding platform**

As mentioned above, Spanish Crowdfunding platforms shall have to apply to CNMV for authorization as a Crowdfunding platform and to register in CNMV's Registry.

The requirements for Crowdfunding platforms to obtain and maintain authorisation as a Crowdfunding platform so that it can operate in the Spanish market are:

- Have the exclusive corporate purpose for carrying out activities that are individual to Crowdfunding platforms and, where appropriate, the activities of a hybrid payment institution.
- Have its registered office and effective administration and management in the Spanish territory or in another Member State of the European Union.
- Adopt the form of a capital company for an indefinite period.
- That the platform managers are persons of recognized business and professional repute and possess appropriate knowledge and experience in the areas necessary for the exercise of their functions.
- Have a good administrative and accounting structure or adequate internal control procedures.
- Have adequate means to ensure the security, confidentiality and reliability to provide the service by electronic means.
- Have an internal code of conduct that addresses potential conflicts of interest and the terms of the participation of directors, officers, employees and representatives in funding applications that are implemented through the Crowdfunding platform.
- Provide mechanisms so that, in the case of cessation of its activity, it may continue providing all or part of the services which it undertook to provide to the Crowdfunding projects for which they obtained funding.

At the same time the LFFE points out the financial requirements to be met by these Crowdfunding platforms:

- A. Those which must be provided at all times:
  - A social capital fully paid in cash of at least EUR 60,000, or
  - Professional liability insurance, a guarantee or other equivalent assurance that deals with responsibility for negligence in the exercise of their professional activity, with a minimum coverage of EUR 300,000 for each claim, and a total of EUR 400,000 per year for all claims, or
  - A combination of initial capital and professional indemnity insurance, guarantee or other equivalent assurance which results in a coverage level equivalent to that indicated in the preceding two paragraphs.
- B. When the amount of the financing obtained in the last 12 months for the projects published on the platform exceeds EUR 2 million, the Crowdfunding platforms must have at least EUR 120,000 of their own resources.
- C. Its total own resources will be increased depending on the total amount of the financing obtained in the last 12 months for projects published on the platform.

#### 4.3.1.2 Foreign and domestic promoters

In case that a Spanish Crowdfunding platform publishes a Spanish project:

- The LFFE requires promoters to be validly incorporated (or, in the case of an individual, to have its tax residence) in Spain or in any other EU member State.
- The LFFE prohibits a promoter from publishing simultaneously more than one project on one platform
- The LFFE sets a fixed limit of EUR 5 million as a maximum amount of funds that a Crowdfunding project can raise on a yearly basis, provided that it is exclusively targeted to accredited investors (if it is targeted to non-accredited investors this fixed limit will be set at EUR 2 million).
- LFFE establishes main information obligations regarding the loan or the issue (description of the essential features and risks associated to, form, rights and obligations of the parties...etc).

#### 4.3.2 Spanish Crowdfunding platform addresses Spanish investors and presents foreign projects

As mentioned above, there is no specific regulation of which is the applicable law when a Spanish Crowdfunding platform addresses foreign promoters. However, since in this case Spanish investors are approached, CNMV will come to the conclusion that Spanish regulatory law will be applicable.

#### 4.3.2.1 Crowdfunding platform

Spanish Crowdfunding platforms shall have to apply to CNMV for authorisation as a Crowdfunding platform and to register in CNMV's Registry.

The requirements for Crowdfunding platforms to obtain and maintain authorisation so that it can operate in the Spanish market are:

- Have the exclusive corporate purpose for carrying out activities that are individual to Crowdfunding platforms and, where appropriate, the activities of a hybrid payment institution.
- Have its registered office and effective administration and management in the Spanish territory or in another Member State of the European Union.
- Adopt the form of a capital company for an indefinite period.
- That the platform managers are persons of recognized business and professional repute and possess appropriate knowledge and experience in the areas necessary for the exercise of their functions.
- Have a good administrative and accounting structure or adequate internal control procedures.
- Have adequate means to ensure the security, confidentiality and reliability to provide the service by electronic means.
- Have an internal code of conduct that addresses potential conflicts of interest and the terms of the participation of directors, officers, employees and representatives in funding applications that are implemented through the Crowdfunding platform.
- Provide mechanisms so that, in the case of cessation of its activity, it may continue providing all or part of the services which it undertook to provide to the Crowdfunding projects for which they obtained funding.

At the same time the LFFE points out the financial requirements to be met by these Crowdfunding platforms:

- A. Those which must be provided at all times:
  - A social capital fully paid in cash of at least EUR 60,000, or
  - Professional liability insurance, a guarantee or other equivalent assurance that deals with responsibility for negligence in the exercise of their professional activity, with a minimum coverage of EUR 300,000 for each claim, and a total of EUR 400,000 per year for all claims, or
  - A combination of initial capital and professional indemnity insurance, guarantee or other equivalent assurance which results in a coverage level equivalent to that indicated in the preceding two paragraphs.
- B. When the amount of the financing obtained in the last 12 months for the projects published on the platform exceeds EUR 2 million, the Crowdfunding platforms must have at least EUR 120,000 of their own resources.

- C. Its total own resources will be increased depending on the total amount of the financing obtained in the last 12 months for projects published on the platform.

#### 4.3.2.2 Promoters

- The LFFE prohibits a promoter from publishing simultaneously more than one project on one platform
- The LFFE sets a fixed limit of EUR 5 million as a maximum amount of funds that a Crowdfunding project can raise on a yearly basis, provided that it is exclusively targeted to Spanish accredited investors (if it is targeted to Spanish non-accredited investors this fixed limit will be set at EUR 2 million).
- LFFE establishes main information obligations regarding the loan or the issue (description of the essential features and risks associated to, form, rights and obligations of the parties...etc).

### 4.4 Impact of EU regulations

#### 4.4.1 Prospectus rule / regimes

In Spain, the MIFID was implemented in the Royal Legislative Decree 4/2015, 23 October, which approves the consolidated version of Act 24/1988 of 28 July, on the Securities Market (*texto refundido de la Ley de Mercado de Valores*) ("LMV") and its developing regulation. The scope of LMV includes the following financial instruments:

- A. Transferable securities issued by public or private persons or entities and grouped in issues. A transferable security will be defined as any patrimonial right, regardless of its name, which, because of its own legal configuration and system of transfer, is eligible for generalised and impersonal trading on a financial market.
- B. Options, futures, swaps, forward rate agreements and any other derivative contract relating to securities, currencies, interest rates or yields, or other derivative financial instruments, financial indices or financial measures which may be settled in kind or in cash.
- C. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event).
- D. Options, futures, swaps, and any other derivative contract relating to commodities that can be settled in kind provided that they are traded on a regulated market and/or a multilateral trading facility (MTF).
- E. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to commodities that can be settled by physical delivery not otherwise mentioned before and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard, inter alia, to whether they are cleared and settled through recognised clearing houses or are subject to regular margin calls.
- F. Derivative financial instruments for the transfer of credit risk.

- G. Financial contracts for differences.
- H. Options, futures, swaps, forward rate agreements and any other derivative contracts relating to, among other factors, climatic variables, emission licences or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event), etc.

As mentioned above, equity Crowdfunding regulated under the LFFE is based on the issue or subscription of bonds, ordinary and preferential shares or other securities representing the capital, when it does not require prospectus in accordance with the LMV.

Hence, European prospectus regulation does not impact on Spanish regulations for Crowdfunding platforms since they do not fall under the scope of the LMV and the LFFE expressly prohibits them from exercising the activities reserved to investment firms and credit institutions such as (i) the reception, transmission and execution of orders of clients in relation to bonds, ordinary and preferential shares or other securities representing the capital, (ii) receiving funds on behalf of investors or promoters unless such funds are received for the sole purpose of executing payments and the Crowdfunding platform is authorised as a hybrid payment institution in accordance with the Payment Services Act 16/2009 of 13 November, and (iii) receiving assets of the promoters on their behalf to guarantee compliance of the promoters' obligations with the investors.

Also, according to the LFFE, Crowdfunding platforms are not allowed to provide the following services:

- Discretionary and individualised management of investments made through Crowdfunding projects.
- Provision of personal recommendations to an investor in respect of Crowdfunding projects.
- The provision of loans and credit to investors and promoters except when the amount of the loan or credit does not exceed 10% of the funding target of each Crowdfunding project and such amount does not allow the Crowdfunding platform to hold, directly or indirectly, control over the company. According to the Spanish Code of Commerce, control shall be considered to be, among others, when the Crowdfunding platform (i) holds the majority of the voting rights, (ii), has the power to appoint or dismiss the majority of the members of the governing body, or (iii) may dispose, by virtue of agreements entered into with third parties, of the majority of the voting rights, etc.
- Underwriting the fundraising to promoters.
- Provide automatic investment mechanisms which allow non-accredited investors to make automatic investment decisions, whether such mechanisms are based on criteria predetermined by the investor.

#### 4.4.2 AIFM-Directive

As mentioned above, the AIFM-Directive and the implementing Spanish Act 22/2014 do not affect Crowdfunding platforms. They affect renewable energy projects.

#### 4.4.3 MiFID / MiFID II

Since MiFID and MiFID II i. a. are restricted to transferable securities (and equal financial instruments) the scope of application on the Spanish Crowdfunding market does not exist.

Since Spanish Crowdfunding platforms facilitate (i) the issue or subscription of bonds, ordinary and preferential shares or other securities representing the capital, when it does not require prospectus in accordance with MiFID / MiFID II, (ii) the issue or subscription of shares in limited liability companies and (iii) the application for loans, including subordinated profit-participating loans, which are not covered by MiFID / MiFID II they are not impacted by MiFID / MiFID II.

#### 4.4.4 PSD / PSD II

The Payment Services Directive was partially implemented by the Payment Services Act 16/2009 of 13 November (*Ley 16/2009, de 13 de noviembre, de servicios de pago*). The Payment Services Directive II (entered into force in 2016) must be implemented until January 2018.

The LFFE prohibits Crowdfunding platforms from exercising the activities reserved to payment institutions and, especially, from receiving funds in order to pay on behalf of investors or promoters, without the platform being authorised as a hybrid payment institution in accordance with the said Payment Services Act 16/2009 of 13 November.

In addition to the CNMV authorisation, the Spanish Payment Services Act states that to perform the services of a hybrid payment institution, the Crowdfunding platform must submit an application to the minister of Economy and Competitiveness to be authorised as a payment institution, after a consultation with the Bank of Spain and the Executive Service of the Commission for the Prevention of Money Laundering and Monetary Offences.

### 4.5 Summary

The LFFE is not clear regarding the scope of territorial application since it only regulates in detail the regime of provision of services in the Spanish territory, including those services offered by Crowdfunding platforms registered outside the Spanish territory to Spanish investors and promoters.

However, on the contrary, there is no mention as to what happens when investors and promoters registered outside the Spanish territory have access to services provided by a Spanish Crowdfunding platform. In certain cases, this lack of legislation has caused this possibility to be interpreted in a restrictive manner.

## 5 Lessons learned from Spanish regulations for a possible harmonized European Crowdfunding regulation

### 5.1 Role model ("dos")

- Regulation of a specific legal framework of peer-to-peer lending and equity Crowdfunding platforms for the first time in Spain.
- Exception of Crowdfunding platforms from prospectus requirements.
- Transparency and investors' protection obligations.

### 5.2 Aspects that should be avoided ("don'ts")

- Same requirements applicable to Equity based Crowdfunding platforms and Lending based Crowdfunding platforms considering that both types of platforms provide different activities and, hence, the risks inherent to them vary.
- No specific regime regarding foreign investors participating in a Spanish Crowdfunding platform is regulated under LFFE.

## 6 Conclusion

Under Spanish regulations the Crowdfunding platform is not a broker or agent of the promoter (issuer or borrower), but simply a mediator between promoters and investors seeking to facilitate transactions. The role of the operator of the platform is the management and operation of a primary market for small and medium-sized enterprises from a position of neutrality. The platform selects and publishes the projects, and can advise promoters regarding their advertising and marketing, but they are prohibited from making personalised recommendations to investors on specific projects, as well as managing financing projects discreetly and individually.

Given that the platform is intended to create a market enabling a meeting point between supply and demand of capital where Crowdfunding projects are not required to be authorised and, thus, are not reviewed by the Spanish authorities, the control exercised by the CNMV over the platform is very limited in comparison to the control exercised over entities subject to financial services regulations. Notwithstanding the foregoing, we can say that this vulnerability of investors, that is a result of less control being exercised by the CNMV, is compensated by the limitation to non-accredited investors of the maximum EUR 10,000 in investments made over a period of 12 months.

## 7 Summary – Crowdfunding regulation

| Country   | Spain   |
|---|---|
| <b>Summary</b>  |   |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>• There are different investing models in Spain: Equity, Lending and Donation or Rewards models.</li> <li>• Crowdfunding platforms operating the Equity model and the Lending model are regulated for the first time by the Promotion of Corporate Finance Act 5/2015 of 27 April</li> </ul>   |
| <b>Current Crowdfunding regulation</b>                |   |
| <b>General regulation</b>                             | <ul style="list-style-type: none"> <li>• CNMV authorisation required for Equity and Lending Models.</li> <li>• Donations and Rewards Models are not subject to the LFFE and therefore, no licence is required.</li> <li>• The LFFE points out the financial and general requirements for an entity to obtain authorisation as a Crowdfunding platform.</li> <li>• No exemptions from authorisation requirement are provided by the LFFE.</li> </ul> |
| <b>Prospectus requirement</b>                         | <ul style="list-style-type: none"> <li>• The publication of a prospectus is not mandatory.</li> <li>• Crowdfunding platforms shall include on their homepage background information for the client.</li> </ul>  |
| <b>AIFMD-regulation</b>                               | <ul style="list-style-type: none"> <li>• Crowdfunding platforms are not considered as managers of AIFs.</li> </ul>  |
| <b>Payment service regulation</b>                     | <ul style="list-style-type: none"> <li>• If platforms wish to receive funds in order to pay on behalf of investors or promoters, Minister for the Economy and Competitiveness authorisation is required.</li> </ul>   |
| <b>Further possible requirements</b>                  | <ul style="list-style-type: none"> <li>• Consumer contracting loans or mortgage and brokerage services for the Conclusion of Contracts of Loan or Credit Act.</li> <li>• Consumer Credit Contracts Act.</li> <li>• General Contracting Terms Act.</li> <li>• Protection of Consumers and Users Act.</li> <li>• Money Laundering and Terrorist Financing Prevention Act.</li> <li>• Personal Data Protection Act.</li> </ul>                         |
| <b>Regulatory barriers</b>                            |   |
| <b>Inbound</b>  | <ul style="list-style-type: none"> <li>• Spanish regulatory law is applicable to foreign Crowdfunding platforms that announce, promote or attract clients or potential investors and promoters in Spain, and/or address its services specifically to investors and promoters residing in Spanish territory.</li> </ul>  |

|   |  |
|---|--|
| <b>Outbound</b>   | <ul style="list-style-type: none"> <li>Spanish regulatory law is not clear in respect of which is the regime applicable to a Spanish Crowdfunding platform that enters EU markets and therefore addresses foreign investors.</li> <li>However, since not only foreign investors are addressed but also Spanish promoters, a restrictive interpretation of Spanish regulatory law should be applied. Therefore, in this case, Spanish Crowdfunding platform could provide services in the Spanish territory as it approaches Spanish promoters; therefore Spanish regulatory law is (likely) applicable.</li> </ul> |
| <ul style="list-style-type: none"> <li>Impact of EU regulation</li> </ul> |  |
| <b>Prospectus regulations</b>   | <ul style="list-style-type: none"> <li>Due to the fact that equity Crowdfunding regulated under the LFFE is based on the issue or subscription of bonds, ordinary and preferential shares or other securities representing the capital, when it does not require prospectus in accordance with the LMV, these EU regulations have no impact to Crowdfunding in Spain.</li> </ul>   |
| <b>AIFM-Directive</b>   | <ul style="list-style-type: none"> <li>Since Crowdfunding platforms are not considered as managers of AIFs, AIFM-Directive and its implementation in Spanish law have no impact to Crowdfunding in Spain.</li> </ul>   |
| <b>MiFID / MiFID II</b>   | <ul style="list-style-type: none"> <li>Since LFFE expressly prohibits Crowdfunding platforms from exercising the activities reserved to investment firms and credit institutions under the Securities Market Act (LMV), provisions of MiFID and MiFID II have no impact to Crowdfunding in Spain.</li> </ul>   |
| <b>PSD / PSD II</b>   | <ul style="list-style-type: none"> <li>If platforms wish to receive funds in order to pay on behalf of investors or promoters, Minister for the Economy and Competitiveness authorisation is required.</li> </ul>  |

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# Sweden

## 1 Recent developments in the market of Crowdfunding in Sweden

During the last years there were the following significant developments in Sweden regarding Crowdfunding:

### 1.1 The Equity Model

Equity Crowdfunding platforms are by far the most popular Crowdfunding model in Sweden. There are around 15-20 Swedish and international crowdequity platforms active in Sweden and the number is increasing.

From a regulatory point of view, there have not been any significant developments in Crowdfunding. The way equity based Crowdfunding is however mainly operated today is in non-compliance with Swedish company law, due to the violation of the spreading and advertisement prohibition for private liability companies (detailed below in Section 3.5.1).<sup>1</sup> The insecurity and risk has therefore increased and many equity platforms are now seeking to find other ways to operate a more compliant operation e.g. by using public investment models.

The Government is currently undertaking an investigation and will publish a report on the matter by December 2017 that may include a legislative proposal regarding crowd equity (Section 3.5.1).

## 2 The Lending Model

The Lending Model has emerged the last years in Sweden. The lending platforms offer peer-to-business, business-to-business, business-to-peer and peer-to-peer lending.

The last couple of years, at least one crowdlending platform has lost its permit due to default in handling the funds and violation of statutory rules. In October 2015, the S-FSA withdrew the permit of a company due to serious misconduct of lender's funds, which affected 3 500 lenders and SEK 300 million.

The PSD II might affect the licence requirements for the lending platforms. The S-FSA has not any guidelines or official statements on how the platforms are assessed and how the current legislation is applied when assessing lending platforms. It is therefore challenging to evaluate how this might change in relation with PSD II.

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<sup>1</sup> Companies Act (2005:551), Ch. 1 § 7.

## 2.1 The Donations or Rewards Model

This Crowdfunding model has the lowest investment risks since no financial investment or return is offered. The model is mainly used for social or charity projects.

Many platforms that previously offered equity, lending and donations/rewards, have now started to remove the donation/reward part, due to the low activity and low return for the platform in that spectrum. There are however a couple of platforms that has specialized in only this type of projects.

## 2.2 Real Estate Crowdfunding and Renewable Crowdfunding

There are today at least two platforms that offer Real Estate Crowdfunding in Sweden and it is an emerging model that has received huge publicity in media. Real estate is an intense market in the urban areas of Sweden, with increasing property values. The Crowdfunding method has opened up the investment market for many natural persons but also generated business opportunities for companies that are in need of project funding. The investments are mainly made in limited liability companies, which is associated with some uncertainty with respect of the spreading prohibition in the Companies Act.

There is still not a platform that is only focused on Renewable Crowdfunding. However, the existing platforms have, from time to time, renewable energy funding campaigns.

## 2.3 International approach in your country

Due to the lack of permit/licence requirement to Equity Crowdfunding, Sweden is a rather easy market to enter. However, the lack of legislation also creates a grey zone that also entails a higher risk for foreign platforms to enter the market.

Nevertheless, Sweden is has a great entrepreneurial landscape and an ecosystem that encourage business and innovation. Sweden has over the years produced a great number of innovative companies that put Sweden on the start-up map internationally.

A number of European and North American platforms are active or are trying to establish an activity on the Swedish market. We will most likely see an increase in this aspect when the legal aspect is more certain regarding equity Crowdfunding.

## 3 Recent developments regarding Crowdfunding regulation in Sweden

There have not been any specific regulatory developments regarding Crowdfunding regulation in Sweden since December 2015.

The S-FSA published a report overviewing the Crowdfunding landscape in Sweden and the related regulatory issues. The report stated that there was a grey zone from a legal perspective that needed to be further reviewed by the Government.

In general, the Swedish legislator has a positive attitude towards Crowdfunding as an alternative source of funding for small and medium-sized companies and wants to ensure high

consumer and investor protection in order to promote a reliable development of Crowdfunding platforms.

### 3.1 The government's investigation on Crowdfunding legislation

The government has in Directive 2016:70 (published on 28 July 2016), listed regulatory issues related with Crowdfunding that are subject to the government's review and investigation. The investigation will be published on 29 December 2017 and shall focus on equity and loan based Crowdfunding. It will further include the following items:

- A. outline the market for platforms used in Crowdfunding,
- B. clarify the role, function, status, and incentive structure of the platforms from a commercial law perspective, especially with regard to crowdlending,
- C. analyse which rules apply to equity based and loan based Crowdfunding and if these are appropriate,
- D. analyse how Crowdfunding of private limited companies relates to the spreading and advertisement prohibition in the Companies Act and clarify if there is any obstacle that prevents private limited companies that wish to use Crowdfunding from becoming public,
- E. propose legislative amendments necessary to promote Crowdfunding and strengthen legal protection for investors and other involved parties,
- F. analyse whether the scope of current commercial legislation can be amended or, if a new regulation of Crowdfunding shall be adopted, and, if necessary, elaborate the necessary legislative proposals, and
- G. analyse the need for sanctions and, if necessary, submit legislative proposals that also include sanctions.

The government has noted that a special issue to be considered is the relationship between donation-based Crowdfunding and the rules of anti-money laundering and terrorist financing.

## 4 Current regulation of Crowdfunding in Sweden

### 4.1 Banking / Financial Service licence requirements – MiFID (I and II)

#### 4.1.1 Equity Model - Securities Market Act (2007:528)

##### (1) Key Definitions

The Swedish Securities Market Act regulates financial trading of securities, including investment brokering, financial advising and prospectus rules. Licence to conduct financial services is required for regulated marketplaces and is issued by the S-FSA.

A regulated market (*Sw. reglerad marknad*) is defined as a multilateral system within EEA that brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments in a way that results in a contract. Financial instruments (*Sw. finansiella instrument*) mean transferable securities, money market

instruments, UCITS, and financial derivative instruments. Relevant in this case is transferrable securities (*Sw. överlåtbara värdepapper*).

Transferable securities are defined<sup>2</sup> as securities, with the exception of instruments of payment, which are traded on the capital market, such as:

- A. shares in companies and comparable ownership rights in other types of undertakings, and depositary receipts in respect of shares;
- B. bonds and other forms of debt instruments, including depositary receipts in respect of such securities; and
- C. other securities granting the right to transfer or acquire such transferable securities as referred to in a and b, or giving rise to a cash settlement calculated based on prices of transferable securities, currencies, interest rates or yields, commodities or other indices or measures.

According to the Swedish government's referral to the Council on Legislation (*Sw. lagrådsremiss*) and the Government Bill (*Sw. proposition*) of the implementation of MiFID II<sup>3</sup>, the definition of transferrable securities in Securities Market Act will remain unchanged in relation to MiFID I when implementing MiFID II in Sweden.<sup>4</sup>

Other amendments in local law with respect to MiFID II shall enter into force on 1 August 2017 and 3 January 2018.

## **(2) Applicability to Crowdfunding**

According to the definition of transferrable securities, securities held in both public and private limited liability companies that are not traded on the capital market falls outside the scope of the directive. The capital market is defined as a securities market, meaning trading on the stock exchange or other organized marketplace.<sup>5</sup>

According to the legislator, shares in private limited liability companies may not be spread to the public and traded on a Swedish or/and foreign regulated marketplace. Such shares do therefore not constitute transferrable securities. Public companies must be registered as a central securities depository (CSD) company in order to be traded on a stock exchange/regulated/capital market.<sup>6</sup> Provided that the public companies that are seeking funding on Crowdfunding platforms are not CSD companies, the securities cannot be transferrable in accordance with the stipulated definition. None listed public companies have

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<sup>2</sup> Chapter 1, section 4.

<sup>3</sup> Respectively published on 20 January 2017 and 5 April 2017.

<sup>4</sup> <http://www.regeringen.se/48f3fd/contentassets/96124c8c82b64d10a526a34f26284243/nya-regler-om-marknader-for-finansiella-instrument-mifid-ii-och-mifir>, referral to the Council on Legislation (*Sw. lagrådsremiss*), p. 244.

<sup>5</sup> Prop. 2006/07:115, p. 282.

<sup>6</sup> Companies Act.

been found on any Crowdfunding platforms, both in our review and according to the S-FSA's report.

With this background, a Crowdfunding platform does normally not constitute a platform where transferrable securities are traded. The Crowdfunding platforms mainly serve as an active or passive intermediary of the share transfer of private and/or public limited liability companies. Therefore, the Crowdfunding platforms shall not fall within the scope of the act and does not need to register or apply for a licence to offer its services in Sweden.

However, this can create difficulties if a Swedish platform wishes to enter another EU country and if such country requires Crowdfunding platforms to hold an EU passport in order to offer Crowdfunding services on the specific market. The S-FSA cannot issue a licence under MiFID for Crowdfunding platforms according to the current legislation and the licence can therefore not be passported to other countries.

MiFID II is therefore not applicable to Crowdfunding platforms in Sweden and no licence or authorization is necessary under the regime.

## 4.2 Prospectus requirements – MiFID (I and II)

### 4.2.1 Equity Model - Financial Instruments Trading Act

The Financial Instruments Trading Act contains provisions regarding the prospectus requirements for trade with transferrable securities and the exemptions for such requirements.

The obligation to prepare a prospectus for transferrable securities is stated in the Swedish Financial Instruments Trading Act (1991:980)<sup>7</sup>, chapter 2 sections 2-7. According to the act, a prospectus shall be prepared when transferable securities are offered to the general public or admitted for trading on a regulated marketplace. In order to facilitate the funding process for smaller companies, the act includes exemptions of the prospectus duty for offerings of transferrable securities below EUR 2,500,000 within a period of twelve months. There is no other information requirement applicable under the act.

“Transferrable securities” under this act has the same definition as the Securities Market Act (see Section 3.1). Equity Crowdfunding is not subject to any prospectus requirement under this act and are not subject to any supervision of the S-FSA, because securities that are offered on Crowdfunding platforms (both public and private limited liability companies) do not fall within the definition of transferrable securities.

The platforms act as intermediaries that do not trade transferrable securities according to the stipulated definition.

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<sup>7</sup> *Sw. lag om handel med finansiella instrument.*

## 4.3 Regulation of Crowdfunding under the AIFMD regime

### 4.3.1 Equity Model - Alternative Investment Fund Managers Act (2013:561)

The AIFMD is implemented in Swedish legislation with e.g. the Alternative Investment Fund Managers Act<sup>8</sup>. The act regulates licence and registration requirements for AIF and AIFMs as well as the supervision of funds and managers. Alternative Investment Fund (“AIF”) (*Sw. alternativ investeringsfond*) is defined as a collective investment undertaking that raises capital from a number of investors in accordance with a defined investment policy for the benefit of those investors. AIF-manager (“AIFM”) (*Sw. AIF-förvaltare*) is defined as legal persons whose regular business is managing one or more AIFs.

A Swedish AIFM whose total assets do not exceed the threshold of EUR 100 000 000, and an AIFM who only manages unleveraged AIFs and that do not grant investors redemption rights during a period of five years with a cumulative value of the AIFs below a threshold of EUR 500 million, are exempted from the licence requirement and can instead apply for registration with the S-FSA. A registered AIFM may not, as a main rule, manage funds directed towards retail investors and it can only be marketed and managed nationally.

The current platforms do not fall within the stipulated definition of AIFs/AIFMs. However it is possible that future Crowdfunding platforms act in a way that would make the business model fall within the scope of the AIFMD. Such service has not yet been launched in Sweden.

## 4.4 Regulation under the Payment Services Directive

The Lending Model is regulated under a number of acts. If the platforms offer payment services or credit intermediation, the platform needs a licence or registration under the Banking and Financing Business Act (2004:297), the Act regarding Certain Activities with Consumer Credit (2014:275) (“LVK”) and the Payment Services Act (2010:751). If the platform's activities are not covered by any of these acts, it may instead require registration under the Certain Financial Operations (Reporting Duty) Act (1996:1006).

### 4.4.1 Lending Model - LVK

LVK contains provisions on certain professional activities that provide and mediate consumer credits (peer-to-peer and businesses-consumers). Such platforms need to apply for a licence under the act. The licence requirement can also be applicable for platforms that only mediate without actually receiving the funds. The platforms under this act are under the supervision of the S-FSA.

#### (1) *The S-FSA’s assessment of application*

Platforms that conduct activities under this act are required to run the business in a sound way. The soundness requirement means that the company, among other things, must have

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<sup>8</sup> *Sw. Lag om förvaltare av alternativ investeringsfonder.*

internal routines and procedures on how credits are granted and intermediated as well as how the funds are handled.

The act also imposes specific requirements on owners and the management of the platform - every owner and representative needs to be assessed and approved by the S-FSA. Anyone who conducts activities under the act must also comply with the rules of the Consumer Credit Act (2010: 1846).

The act does not apply to consumer credit providers that are under a registration or licence requirement according to e.g. the Payment Service Act (see below).

### ***(1) Violations of the act***

If a platform or a board member of such platform violates or breaches a provision of the act, the S-FSA may issue an injunction restricting the activities, or take any other action to remedy the situation. If the violation is serious, the licence may be revoked, or notice a warning if it is deemed sufficient. Sanction fine between SEK 5000 and SEK 50 000 000 can be decided in case of such breach. An injunction may also be combined with a penalty fee.<sup>9</sup>

The act does not contain any liability provisions, but a platform that is in violation of the act shall according to the provisions be liable for any incurred damages due to such violation.

### **4.4.2 Lending Model – The Payment Service Act (2010:751)**

The Payment Services Act<sup>10</sup> is one of the acts that implements of the Payment Services Directive 1<sup>11</sup>. Payment service (*Sw. betaltjänst*) is defined as, among other things, services that make it possible to make cash deposits and withdrawals, execution of payment transactions and money transfers (Ch. 1 Section 2).

Actors that fall under the definition of a payment service provider are subject to a licence requirement. The licence is issued by the S-FSA, who is also the supervising authority. A Swedish payment service provider must be a Swedish limited liability company or economic association to be granted licence.

### ***(1) Exemptions***

An actor may apply to be exempted from the licence requirement. Exceptions may be provided if the total amount of payment transactions during the last 12 months do not exceed an amount equivalent to EUR 3 000 000 per month (average the latest 12 months). Those exempt from the licence requirement will instead be registered with the S-FSA (registered payment service provider, *Sw. registrerad betaltjänstleverantör*).

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<sup>9</sup> LVK, Sections 20-32.

<sup>10</sup> *Sw. Lag om betaltjänster*.

<sup>11</sup> Directive 2007/64/EC.

Also, if the platform only mediates between the parties without possessing and/or controlling any funds, authorisation as a consumer credit institution according to LVK is most likely sufficient. The S-FSA is however very limited in giving general statements on how the requirements are assessed due to the huge differences in platform solutions.

### ***(2) The S-FSA's assessment of the application***

The S-FSA conducts an individual assessment on each platform and decides whether the licence or authorization requirement is applicable based on the funding model and setup of the platform. Any transfer of funds through the crowdlending platform operator, e.g. the platform operator accepts funds from one party in order to forward loans to another party, would most likely constitute a service regulated by the Payment Services Act, which would require a licence to become an active payment service provider.

Similar to the LVK, owners and individuals in the management/board of the payment service provider must be reviewed and approved by the S-FSA. Any change of ownership or management must be reported to the S-FSA.

The F-SA must ensure that the company has procedures to keep customers' funds separate from the company's funds and that it has procedures to reduce the risk of money laundering and financing of terrorism. The company must also have satisfactory routines for handling the clients' funds separate from the platform's funds, as well as granting and intermediating credits.

### ***(1) Violation of the act***

If a platform is in violation of the provisions of the act, the S-FSA may issue an injunction restricting the activities, or take any other action to remedy the situation. If the violation is serious, the licence may be revoked, or notice a warning if it is deemed sufficient.<sup>12</sup> Sanction fine between SEK 5000 and SEK 50 000 000 can be decided in case of such breach. An injunction may also be combined with a penalty fee.<sup>13</sup>

## **4.5 Possible additional regulations**

### **4.5.1 The Companies Act – Equity Model**

Under the Swedish Companies, limited liability companies can be registered as either public or private companies. Private companies must have a registered share capital of minimum SEK 50.000, while public companies must have at least SEK 500,000 due to investor protection reasons. Public companies may, by advertisement or in other way, offer their shares to the public (more than 200 persons). Private limited liability companies can raise capital by issuing new shares, but there are limitations in place that restrict the scope of the share offers in private companies.

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<sup>12</sup> Payment Services Act, Ch. 8 Section 8.

<sup>13</sup> Payment Services Act, Ch. 8 Section 15.

According to the Companies Act<sup>14</sup>, a private liability company or a shareholder in such company is not allowed to;

- A. offer securities or subscription rights to the public by advertisement, or
- B. in other ways offer or attempt to offer securities to more than 200 investors, as it constitutes a “public” offering,
- C. Such offering as stipulated in b) above may however occur in case the offer is directed solely to a group of persons who have previously given notice of interest in such offers and where no more than 200 trading units are offered.

Violation against the spreading and advertising prohibition is sanctioned both under civil and criminal law. Note that even failed campaigns are in violation of the provision since even attempting to spread the shares is prohibited.

Despite the prohibition, many crowdequity platforms are still hosting funding campaigns for private limited liability companies. Yet, there have not been any lawsuits or rulings against any such campaigns and/or companies. This creates a grey zone and high insecurity for the involved parties. From a legislation point of view, the spreading prohibition is the most crucial aspect that needs to be reviewed and clarified by the legislator in respect to Crowdfunding.

The Swedish government has been quite passive and has the last years observed the development of the crowdequity market, both locally and globally. The government wants to increase the investor protection in order to encourage the development of a reliable form of funding. The government is currently investigating the legislation that affects Crowdfunding (see Section 2.1).

#### 4.5.2 The Marketing Practices Act (2008:486)<sup>15</sup>

The purpose of the Marketing Practices Act is to promote the interests of consumers, trade and industry in connection with the marketing of goods and to counteract marketing practices that are unfair to consumers and companies.

The act is applicable to Crowdfunding platforms because the platforms actively advertise the funding campaigns but also market the products and services of the fund seeking projects/companies.

According to the act, all marketing must be based on generally accepted marketing practices (*Sw. god marknadsföringssed*)<sup>16</sup>, which means generally-accepted business practices or other accepted norms, the purpose of which are to protect consumers and traders in the context of the marketing of products.

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<sup>14</sup> Companies Act, Ch. 1, Section 7.

<sup>15</sup> *Sw. marknadsföringslag, implementing Directive 2006/114/EC Concerning misleading and comparative advertising.*

<sup>16</sup> Marketing Practices Act, Section 5.

The act prohibits misleading marketing practices. A trader may not use inaccurate claims or other presentations in the marketing which are misleading with respect to the commercial operations of the trader or a third party. Nor may a trader omit material information in the marketing of its own or a third party's commercial operations. Misleading omission also refers to such cases where the material information is given in an unclear, incomprehensible, ambiguous or other inappropriate manner.<sup>17</sup>

In case of a purchase offer, the marketing practice is misleading where, in a presentation, the trader offers consumers a specified product with a statement of price but does not include the following material information:

- the product's defining characteristics;
- price and comparison price;
- the trader's identity and physical address;
- terms and conditions for payment, delivery, performance and handling of complaints where these differ from those standard for the industry or product in question; and
- information which must be provided to the consumer pursuant to law regarding the right of withdrawal or right to rescind a purchase.<sup>18</sup>

#### ***(1) Injunctions, orders and damages***

A trader whose marketing practices are unfair may be forbidden from continuing the practice or from adopting any other similar practice.<sup>19</sup> A trader who, in the course of its marketing, fails to provide material information may be ordered to provide such information, which may include a duty to provide information in advertisement, through labelling or in another certain form requested by a consumer.

Material information refers to e.g. such information that must be provided under specific legislation, information about warranties and information in connection with a purchase offer (see above). Such injunction shall be issued in conjunction with a conditional fine unless special reasons render such unnecessary.<sup>20</sup>

A trader who intentionally or negligently breaches an injunction or order shall compensate any consumer or trader for any damage suffered thereby.

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<sup>17</sup> Marketing Practices Act, Section 10.

<sup>18</sup> Marketing Practices Act, Section 12.

<sup>19</sup> Marketing Practices Act, Section 23.

<sup>20</sup> Marketing Practices Act, Section 26.

### 4.5.3 Off-Premises Contract Act (2005:59)<sup>21</sup>

Agreements signed by electronic means falls within the scope of the Distance and Off-Premises Contracts Act (2005:59). In Crowdfunding, the parties enter different types of contracts by distance (e.g. share subscription agreements, shareholders' agreement).

The act contains consumer friendly conditions and a minimum protection level for consumers in conjunction with distance contracts, such as i.e. information duty and cancellation right. Any contracts containing less favourable terms than what is stated in the act shall be invalid and unenforceable against the consumer. The act also provides a higher protection in terms of damages due to unfair marketing practices.

The consumer shall be entitled to withdraw from the contract by submitting or sending notice thereof to the trader within 14 days of the contract date. However, the provisions concerning the right of cancellation shall not apply where both parties, at the consumer's request, have performed their obligations under the contract.<sup>22</sup> Furthermore, the cancellation right is not applicable to contracts concerning:

- A. financial services or transfers of financial instruments where the price depends on fluctuations on the financial markets beyond the trader's control and which may occur during the withdrawal period;
- B. participation in share issues or another similar activity, where the price for the right to which the activity relates will, following the expiration of the subscription period, depend on such fluctuations on the financial markets; or
- C. credit associated with real estate mortgages, site leaseholds, or tenant-owners' association rights, or similar rights, or in connection with comparable rights in buildings which do not belong to the property.

The consumers who subscribe shares in crowdequity platforms do therefore not have a right of withdrawal in accordance with b) above.

### 4.5.4 Other Possible Regulations

- Money Laundering and Terrorist Financing (Prevention) Act (2009:62),
- Contracts Act (1915:218),
- Tort Liability Act (1972:207),
- Act concerning qualified electronic signatures (2000:832),
- Consumer Contracts Act (1994:1512),
- Consumer Sales Act (1990:932)

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<sup>21</sup> *Sw. lag om distansavtal och avtal utanför affärslokaler*, implementing - Distance Marketing of Financial Services Directive (Directive) 2002/65/EC).

<sup>22</sup> Off-Premises Contracts Act, Ch. 2 Section 10 and Ch. 3 Section 2.

## 5 Regulatory barriers for Crowdfunding crossing borders

As previously stated, the regulatory aspects of Sweden's Crowdfunding market are still in a grey zone. The following are the major regulatory obstacles for cross-border business in Sweden.

### 5.1 Applicable law

The local Swedish financial regulations apply when a foreign platform markets its services to the Swedish market and Swedish investors are approached by foreign actors. The S-FSA thus applies a marketing focused approach. In addition to this, the financial rules also apply when a foreign actor has a seat or a registered office in Sweden.

### 5.2 Inbound

The question is if the Crowdfunding platform addresses Swedish investors or wants to present Swedish companies/projects on its platform.

#### 5.2.1 Foreign Crowdfunding platform addresses Swedish investors and companies:

Swedish regulatory law can apply to the

- Crowdfunding platforms (mainly licence for lending, information and compliance obligations) and,
- foreign companies/projects seeking funding (information and compliance obligations)

##### 5.2.1.1 Crowdfunding platforms

#### (1) Licence obligations

##### *MiFID – Equity*

Since MiFID is not applicable to crowdequity platforms according to Swedish law, there is no requirement for foreign Crowdfunding platform to have an EU passport in order to offer its crowdequity services on the Swedish market.

##### *PSD – Lending*

Swedish crowdlending platforms are obliged to hold a PSD-licence or to obtain registration with the S-FSA in accordance with LVK or the Payment Service Provider Act (see Section 3.4.1 and 3.4.2) in order to offer lending services in Sweden. Foreign actors must however hold a licence in the home state in order to offer its services in Sweden – a registration with the national financial supervisory authority is not sufficient. Crowdlending platforms (categorized as payment providers) domiciled in an EEA country wishing to start operating in Sweden shall report this to the competent authority of the EEA country in which the company is authorized. It is then the home state regulatory authority that approves the cross border and informs the S-FSA.

For foreign actors, the Crowdfunding platform can be operated either through a branch, agent or entities to which the platform's activities have been outsourced.

## **(2) Other financial/compliance regulations**

### ***Money Laundering and Terrorist Financing (Prevention) Act***

This act shall apply to natural and legal persons who conduct crowdlending and crowdquity e.g. operations providing payment services in its capacity as a payment institution pursuant to the Payment Services Act but also without being a payment institution, operations involving consumer credit pursuant to LVK as well as assisting with the planning or execution of transactions on behalf of a client in conjunction with the buying and selling of real property or a company.<sup>23</sup> The provisions regarding basic due diligence measures and ongoing follow-up of business relationships do not apply to the referred platforms if they are domiciled within the EEA because the state has equivalent provisions regarding measures against money laundering.

#### **5.2.1.2 Company/Project**

##### **(1) Licence obligations**

There is no prospectus requirement for companies that offer non-transferrable securities under Swedish law.

##### **(2) Other regulations**

The Companies Act is only applicable to Swedish limited liability companies. The foreign companies/projects will therefore not be affected by the spreading prohibition.

The companies/project must comply with the information requirements under the Marketing Practices Act.

Swedish anti-money laundering regulation is not applicable to the EEA fund seeking companies / projects – since they or any branches are not based in Sweden and are covered by the anti-money laundering provisions in their home state.

## **5.3 Outbound**

In this situation a Swedish Crowdfunding platform enters foreign (European) markets and therefore addresses foreign investors.

Again, two different alternatives must be considered:

- Swedish Crowdfunding platform approaches foreign (EU) investors and companies/projects (mainly licence requirement for lending platforms) and,

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<sup>23</sup> Money Laundering and Terrorist Financing (Prevention) Act, Chapter 1, Section 2 p. 17, 18 and 20, Section 3 p. 2.a.

- Swedish Crowdfunding platform approaches Swedish investors and presents a company/project from another EU member state on its platform

### **5.3.1 Swedish Crowdfunding platform addresses foreign (EU) investors**

#### **5.3.1.1 Crowdfunding platforms**

##### **(1) PSD-licence**

Activities in an EEA country may, after notification to the S-FSA, be operated either by employing a representative or setting up a branch in that country or conducting other cross-border activities in the country. A company that is going to change any of the conditions specified in the company's notification to the S-FSA after the cross-border activity has been initiated, must notify the S-FSA in writing before the change is made.

In order for a Swedish company to be able to operate in a non-EEA country, it is necessary for the company to set up a branch there and that the S-FSA provides permission for branch establishment. If the company subsequently intends to change any of the conditions specified in the company's licence application, FI must be informed before the change is made.

##### **(2) Other regulations**

###### ***Anti-money laundering***

Crowdfunding platforms must comply with the Swedish anti-money laundry provisions in order to be compliant in other EEA countries as well (see above). However, since the platform's liability for e.g. lending is often unclear, the incentives for the platforms to control borrowers in certain cases may be low, which increase the risk of the platform being used for money laundering and for financing terrorism.

#### **5.3.1.2 Company/project**

###### ***Anti-money laundering***

Same as above.

## **5.4 Impact of EU regulation**

### **5.4.1 MiFID I and II and prospectus rules**

The different interpretations and implementations of certain elements in MiFID I and II have created a quite non-harmonized regulatory framework regarding licence requirements for Crowdfunding platforms. As Crowdfunding platforms are covered by the scope of the local legislation in some countries, due to the definition of e.g. transferrable securities, other countries have the opposite approach, which lead to licence requirements in some countries but not in other. Sweden does not have a MiFID-licence requirement for equity platforms. The Swedish crowdequity platforms can therefore not enter a market that requires a passportable MiFID licence since the S-FSA cannot issue such licence for crowdequity platforms.

The same applies to the prospectus requirements in EU that have emerged due to the different interpretations of the directive. Such differences create entry barriers for cross border platforms.

#### 5.4.2 PSD I and II

The Payment Service Directive II will be implemented in Sweden by 13 January 2018.

In Sweden, the most crucial provision would be the money remittance provision, where the Crowdfunding platforms would be considered as payment service providers if they receive funds from the payer for the purpose of transferring the amount to a recipient or to another payment service provider acting on the recipient's behalf. Here, the platforms must be cautious on how the business model is set up and to outsource the payment and money transfer service to a licenced payment service provider.

As well as the roll of a marketplace is interesting as such intermediating party can be considered a payment service provider if it acts on behalf of both the payer and the payee and also is in control or possession of any client funds. However this is stipulated in the consideration (p. 11) and is thus not binding.

### 5.5 Summary

Sweden does not have a Crowdfunding act and no other acts have been amended with regard to Crowdfunding yet. This is similar to other European countries that have interpreted and implemented the EU-directives differently. For instance, different licence requirements in the EEA states make it more difficult for platforms to conduct cross border activity. A clear example is that a Swedish platform that cannot obtain a MiFID-licence for a crowdequity platform cannot enter a market that requires such licence, for example Finland.

A harmonized Crowdfunding regulation on the EU-level would allow more cross border activity and a more secure funding environment since many countries would have clear directions to relate to.

## 6 Lessons learned from Sweden's regulation for a possible harmonised European Crowdfunding regulation

### 6.1 Role model ("dos")

- Maintain the investor and consumer protection perspective,
- Restrict the definition of transferrable securities to only include securities that can be traded on a capital market, in order to remove the MiFID-licence requirement and the prospectus duty (too extensive), and
- Maintain the information obligation (Marketing Practices Act).

### 6.2 Aspects that should be avoided ("don'ts")

- A spreading prohibition that creates a grey zone for this type of funding threatens the expansion of the Crowdfunding market. Although the spreading prohibition is

an essential provision for private limited liability companies, a clarification is needed from the legislator on how to interpret its applicability to Crowdfunding. It must however be adapted in order to be harmonized with other EU-countries.

- The S-FSA is very timid in its guidelines on how to interpret and apply the EU-regulations on the different Crowdfunding models (in comparison to the BaFin). The national supervisory authorities should publish guidelines or statements that assist in the understanding of how the S-FSA applies the rules.

## 7 Conclusion

The activity of Crowdfunding is increasing in Sweden, but it lacks satisfactory legislation. Equity Crowdfunding platforms are not subject to a financial licence and are not under the S-FSA's supervision. However, the spreading and advertisement prohibition in the Companies Act for private limited liability companies creates a grey zone regarding equity based Crowdfunding. Although it is prohibited and sanctioned under civil and criminal law, there are no rulings on the matter yet. The donation and reward based models are not subject to any licence or registration. However, the crowdlending platforms, depending on how the funds are managed, need to register their business with the S-FSA or apply for a licence as a payment service provider. The latter licence is also a required for cross border activities of such crowdlending platform.

Due to the individual Crowdfunding regulations in the EU-states, the platforms and companies/project that wish to pursue cross border activities, are recommended to thoroughly review the legislative framework for each state and evaluate which jurisdiction that is most suitable and favourable from a legal, cost and time efficient perspective.

The importance of the investors' and the platform's due diligence before investing or hosting a campaign shall be emphasized in order to reduce the risk of liquidity risk of a funded company, fraud and money-laundry. Especially for donation based Crowdfunding, the lack of rules lead to high risk for fraud, money-laundry and terrorist financing.

The Swedish government has expressed interest in Crowdfunding as an alternative investment form. The government will publish an investigation by 29 December 2017 that aims to outline the Crowdfunding landscape in Sweden and, if deemed necessary, propose relevant legislation, which hopefully will lead to a more secure Crowdfunding market.

## 8 Summary – Crowdfunding Regulation

| Country   | Sweden   |
|---|--|
| <b>Summary</b>  |  |
| <b>Recent developments in Crowdfunding regulation</b> | <ul style="list-style-type: none"> <li>•</li> <li>•</li> </ul>   |
| <b>Current / planned Crowdfunding regulation</b>      |  |
| <b>General regulation</b>                             | <p>The government will investigate regulatory issues related with Crowdfunding (Dir. 2016:70):</p> <ol style="list-style-type: none"> <li>a) outline the market for platforms used in Crowdfunding,</li> <li>b) clarify the role, function, status, and incentive structure of the platforms from a commercial law perspective, especially with regard to crowdlending,</li> <li>c) analyse which rules apply to equity based and loan based Crowdfunding and if these are appropriate,</li> <li>d) analyse how Crowdfunding of private limited companies relates to the spreading and advertisement prohibition in the Companies Act and clarify if there is any obstacle that prevents private limited companies that wish to use Crowdfunding from becoming public,</li> <li>e) propose legislative amendments necessary to promote Crowdfunding and strengthen legal protection for investors and other involved parties,</li> <li>f) analyse whether the scope of current commercial legislation can be amended or, if a new regulation of Crowdfunding shall be adopted, and, if necessary, elaborate the necessary legislative proposals, and</li> <li>g) analyse the need for sanctions and, if necessary, submit legislative proposals that also include sanctions</li> </ol> |
| <b>MiFID and Prospectus requirement</b>               | <p><b>MiFID-licence</b></p> <ul style="list-style-type: none"> <li>• Transferable securities are defined in the Securities Market Act as securities, with the exception of instruments of payment, which are traded on the capital market, such as:             <ol style="list-style-type: none"> <li>a) shares in companies and comparable ownership rights in other types of undertakings, and depositary receipts in respect of shares;</li> <li>b) bonds and other forms of debt instruments, including depositary receipts in respect of such securities; and</li> <li>c) other securities granting the right to transfer or acquire such transferable securities as referred to in a and b, or giving rise to</li> </ol> </li> </ul>  |

|   |   |
|---|---|
|   | <p>a cash settlement calculated based on prices of transferable securities, currencies, interest rates or yields, commodities or other indices or measures.</p> <ul style="list-style-type: none"> <li>• Securities held in both public and private limited liability companies that are not traded on the capital market fall outside the scope of the directive.</li> <li>• The capital market is defined as a securities market, meaning trading on the stock exchange or other organized marketplace.<br/>→ No MiFID licence required for crowdequity platforms</li> </ul> <p><b>Prospectus requirement</b></p> <ul style="list-style-type: none"> <li>• The Financial Instruments Trading Act contains provisions regarding the prospectus requirements for trade with transferrable securities.</li> <li>• Prospectus shall be prepared when transferable securities are offered to the general public or admitted for trading on a regulated marketplace.</li> <li>• Transferrable securities in the Financial Instruments Trading Act have the same definition as in Securities Market Act.<br/>→ No prospectus required for crowdequity platforms</li> </ul> |
| <p><b>AIFMD-regulation</b></p>              | <ul style="list-style-type: none"> <li>• Alternative Investment Fund Managers Act regulates licence and registration requirements for AIF and AIFMs as well as the supervision of funds and managers.</li> <li>• The business models of the current platforms do not fall within the stipulated definition of AIFs/AIFMs.</li> <li>• Possible that future Crowdfunding platforms to fall within the scope of the AIFMD.<br/>→ The AIFMD is not applicable to the current Crowdfunding platforms.</li> </ul>   |
| <p><b>Payment service regulation</b></p>    | <p>The Lending Model is regulated under the following acts:</p> <ul style="list-style-type: none"> <li>• If the platforms offer payment services or credit intermediation, the platform needs a licence or a registration under <ul style="list-style-type: none"> <li>– The Banking and Financing Business Act (2004:297),</li> <li>– The Act regarding Certain Activities with Consumer Credit (2014:275) (“LVK”), and</li> <li>– The Payment Services Act (2010:751).</li> </ul> </li> <li>• If the platform's activities are not covered by any of the above acts, it may instead require registration under the Certain Financial Operations (Reporting Duty) Act (1996:1006).</li> </ul>  |
| <p><b>Further possible Requirements</b></p> | <ul style="list-style-type: none"> <li>• The Companies Act (2005:551)</li> <li>• The Marketing Practices Act (2008:486)</li> <li>• Off-Premises Contract Act (2005:59)</li> </ul>   |

|                            |   |
|----------------------------|---|
|                            | <ul style="list-style-type: none"> <li>• Money Laundering and Terrorist Financing (Prevention) Act (2009:62),</li> <li>• Contracts Act (1915:218),</li> <li>• Tort Liability Act (1972:207),</li> <li>• Act concerning qualified electronic signatures (2000:832),</li> <li>• Consumer Contracts Act (1994:1512),</li> <li>• Consumer Sales Act (1990:932)</li> </ul>   |
| <b>Regulatory barriers</b> |   |
| <b>Inbound</b>             | <p><b>Foreign Crowdfunding platform addresses Swedish investors and companies</b></p> <p>The S-FSA applies a marketing focused approach - Swedish regulatory law applies when the market is approached.</p> <p><i>PLATFORMS</i></p> <ul style="list-style-type: none"> <li>• <b>Licence obligations</b> <ul style="list-style-type: none"> <li>- Equity: MiFID-licence not required since MiFID is not applicable to crowdequity platforms according to Swedish law.</li> <li>- There is no requirement for foreign Crowdfunding platform to have an EU passport in order to approach and offer its crowdequity services on the Swedish market.</li> <li>- Lending: PSD-licence is required. Foreign platforms must have a EU-passport and report cross-board activity to the competent authority of the home state in which the company is authorized.</li> <li>- Foreign Crowdfunding platform can be operated either through a branch, agent or entities to which the platform's activities have been outsourced.</li> </ul> </li> <li>• <b>Other financial/compliance regulations</b> <ul style="list-style-type: none"> <li>- Money Laundering and Terrorist Financing (Prevention) Act</li> <li>- The provisions regarding basic due diligence measures and ongoing follow-up of business relationships do not apply to the foreign platforms if they are domiciled within the EEA because the state has equivalent provisions regarding measures against money laundering.</li> </ul> </li> </ul> <p><i>COMPANY / PROJECT</i></p> <ul style="list-style-type: none"> <li>• <b>Licence obligations</b> <ul style="list-style-type: none"> <li>- No prospectus requirement for companies that offer non-transferrable securities.</li> </ul> </li> <li>• <b>Other regulations</b> <ul style="list-style-type: none"> <li>- The Companies Act is only applicable to Swedish limited liability companies. The foreign companies/projects will therefore not be affected by the spreading prohibition.</li> </ul> </li> </ul> |

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|   | <ul style="list-style-type: none"> <li>- Must comply with the information requirements under the Marketing Practices Act.</li> <li>- Swedish anti-money laundering regulation is not applicable to the EEA fund seeking companies/projects – if not based in Sweden, they are covered by the anti-money laundering provisions in their home state.</li> </ul>  |
| <b>Outbound</b>                         | <p><b>Swedish Crowdfunding platform addresses foreign investors</b></p> <p><i>PLATFORMS</i></p> <ul style="list-style-type: none"> <li>• <b>Licence obligations</b> <ul style="list-style-type: none"> <li>- Activities in an EEA country may, after notification to the S-FSA, be operated either by employing a representative or setting up a branch in that country or conducting other cross-border activities in the country.</li> <li>- A company that is going to change any of the conditions specified in the company's notification to the S-FSA after the cross-border activity has been initiated, must notify the S-FSA in writing before the change is made.</li> </ul> </li> <li>• <b>Other regulations</b> <ul style="list-style-type: none"> <li>- Anti-money laundering: platforms must comply with the Swedish anti-money laundry provisions in order to be compliant in other EEA countries.</li> </ul> </li> </ul> |
| <b>Impact of EU-regulation</b>          |  |
| <b>MiFID and Prospectus regulations</b> | <ul style="list-style-type: none"> <li>• The different interpretations and implementations of certain elements in MiFID I and II have created a quite non-harmonized regulatory framework regarding licence requirements for Crowdfunding platforms.</li> <li>• MiFID-licence and prospectus requirements in some countries but not in other.</li> </ul>   |
| <b>PSD I / II</b>                       | <ul style="list-style-type: none"> <li>• High risk for Crowdfunding services to be considered payment service providers (money remittance) if they receive and transferring funds between the parties.</li> <li>• Must use third party licenced payment service providers.</li> <li>• PSD II will most likely lead to increased harmonisation.</li> </ul>  |

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# Switzerland

## 1 Recent developments in the market of Crowdfunding in Switzerland

Overall, the Swiss Crowdfunding market remains rather small in comparison with the USA, Germany, the UK or other European countries. Nevertheless, it is growing strongly and gaining momentum. In 2016, CHF 128.2 million, were collected through Crowdfunding in Switzerland, an increase of 362% compared to the CHF 27.3 million collected in 2015 (CHF 15.8 million in 2014 and CHF 11.6 million in 2013). More than 100,000 people supported 3,098 campaigns.<sup>1</sup> If this accelerated growth trajectory continues, Swiss Crowdfunding platforms could collect as much as CHF 300 – 400 million in 2017.<sup>2</sup> As of the end of April 2017, approximately 50 platforms were maintaining a physical presence in Switzerland (compared to 50 in 2016). Several nondomestic platforms without a physical presence in Switzerland were also active in the Swiss market.<sup>3</sup> In 2016, for the first time more funds were collected in Switzerland under the Equity and Lending Models than under the Reward and Donation Models. In the same year, a platform offering firms the possibility to sell their receivables to investors at a discount achieved the same volume as all platforms operating under the Reward and Donation Model together.<sup>4</sup>

### 1.1 The Equity Model (individuals make investments in return for a share in the profits or revenue generated by the company/project)

Only few platforms use the Equity Platform in Switzerland and offer investments in start-ups or Swiss and non-Swiss real estate. In the Equity model, investors normally acquire shares in a company limited by shares or, in case of real-estate, a co-ownership interest in a real estate. The volume of investments in real estate is about 4.5 times higher than investments in companies.

In 2016, the Equity Model raised CHF 39.2 million for 25 projects compared to CHF 7.1 million for 17 projects in 2015 (up 453%).<sup>5</sup> The growth was clearly driven by real estate Crowdfunding, which raised CHF 32.4 in 2016, only a year after first emerging on the Crowdfunding market in Switzerland.<sup>6</sup>

### 1.2 The Lending Model (individuals lend money to a company or project in return for repayment of the loan and interest on their investment)

In the Lending Model, the crowd lends funds to small and medium enterprises and to individuals, including, more recently, firms and individuals seeking mortgages. In 2016, the

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<sup>1</sup> See DIETRICH, ANDREAS/AMREIN, SIMON, The Crowdfunding Monitoring Switzerland 2017, available under <https://blog.hslu.ch/retailbanking/Crowdfunding/>, p. 44 (cited: DIETRICH/ AMREIN, Monitoring 2017).

<sup>2</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 44.

<sup>3</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 6.

<sup>4</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 8.

<sup>5</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 8.

<sup>6</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 14.

Lending Model involved a volume of CHF 55.1 million compared to CHF 7.9 million in 2015 (up 597%) and various new platforms were launched in 2015 and 2016.<sup>7</sup>

The increase of volume was mainly driven by the trend to provide loans to small and medium enterprises which picked up in 2015 and 2016. The average loan granted to small and medium enterprises in 2016 was CHF 18'000 while loans averaging CHF 4'000 were granted to consumers.<sup>8</sup>

### **1.3 The Donations or Rewards Model (individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

In Switzerland, the Donation or Reward Model is split into to a so-called crowdsupporting (or reward-based) and a crowddonating model, where the donator does not get any direct and measurable consideration.

The growth in Crowdfunding via the Donations or Rewards Model slowed considerably between 2015 and 2016. Funds in the amount of CHF 17.0 million were raised in 2016, compared to CHF 12.3 million in 2015 (up 37%).<sup>9</sup> In all, 1'338 campaigns were successful, raising an average of CHF 12'672 in 2016, compared to CHF 11'660 in 2015.<sup>10</sup>

The Donation and Rewards Model was popular mainly in the areas of technology, music, sports and social projects.<sup>11</sup>

### **1.4 Real estate Crowdfunding**

As mentioned in connection with the Equity Model, there are various platforms, which facilitate the Crowdfunding of real estate projects in Switzerland and abroad, some of them on an exclu-sive basis.

Investors investing in Swiss real estate projects normally acquire co-ownership in the real estate and are registered in the land register as legal owners of the respective co-ownership.

### **1.5 Receivables Trading**

A new development in the industry is a receivable trading platform, which allows firms to pre-finance or sell receivables at a discount to investors, who can thereby directly fund the working capital. This platform started in 2016 and for that year attracted funds in the same amount as all platforms operating under the Reward and Donation Model.<sup>12</sup>

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<sup>7</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 16.

<sup>8</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 16.

<sup>9</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 8.

<sup>10</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 9.

<sup>11</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 9.

<sup>12</sup> See DIETRICH/AMREIN, Monitoring 2017, p. 8.

## 1.6 International approach

In addition, international Crowdfunding platforms are active in Switzerland (including platforms from Austria and Germany) and in 2017 one Swiss platform teamed up with a European platform. Offering Crowdfunding services into Switzerland from abroad requires a careful legal analysis as various Swiss regulations apply also to platforms with no physical presence in Switzerland.<sup>13</sup>

## 2 Recent developments regarding Crowdfunding regulation in Switzerland

### 2.1 Developments in politics and authorities regarding Crowdfunding regulation

#### 2.1.1 In General

By international standards, Crowdfunding did not attract major attention in Switzerland until two years ago.<sup>14</sup> Since then, it received media coverage and increased attention from lawmakers and regulators. Although no specific rules were enacted yet, the issue is getting more and more attention – especially from the Swiss Financial Market Supervisory Authority (FINMA) but also from the Swiss State Secretariat for Economic Affairs (SECO), the Federal Office of Culture (FOC) and more recently the Swiss Federal Council, the Swiss government, which initiated a law-reform process to relax the regulatory framework for innovative financial technologies (FinTech)<sup>15</sup>, which would also benefit Crowdfunding platforms.<sup>16</sup>

#### 2.1.2 The Swiss Financial Market Supervisory Authority (FINMA)

Until 2015, FINMA has expressed a reserved view on Crowdfunding and commented in passing on Crowdfunding in a report called "How investors can protect themselves against unauthorized financial market providers".<sup>17</sup> In this report, FINMA noticed that more and more individuals seeking finance (borrowers) and investors are looking for alternatives to banks. However, since there is a huge variety of Crowdfunding platforms, no general answer to the question of whether such platforms require some form of license exists. Therefore, FINMA must review each business model on a case-by-case basis.<sup>18</sup>

Although FINMA did not take a general view on Crowdfunding, some general information on FINMA's approach of Crowdfunding can be found in a short fact sheet FINMA published on 1 December 2014.<sup>19</sup> This being said, according to newspaper articles, FINMA has issued

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<sup>13</sup> See below, section 4.

<sup>14</sup> See KUNZ, PETER V., Crowdfunding, in: Jusletter of 25 August 2014, para 1 (cited: KUNZ, Crowdfunding).

<sup>15</sup> See <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-64356.html> and <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-65476.html>.

<sup>16</sup> See below, sections 2.2 and 3.1.3.

<sup>17</sup> This FINMA report can be downloaded under <https://www.finma.ch/en/documentation/finma-publications/reports/supervisory-reports/>. (cited: FINMA report).

<sup>18</sup> See FINMA report, p. 11.

<sup>19</sup> See <https://www.finma.ch/en/documentation/finma-publications/fact-sheets/#Hidden%20Filter=%7B3A570A4C-0D04-4628-83CE-7AED5968E9F8%7D&Order=4>.

rulings on at least three different platforms so far deciding that none of them is subject to the supervision of FINMA.<sup>20</sup>

Since then the trend changed. In a speech in September 2015 about technological change and innovation in the financial sector, Mark Branson, the Chief Executive Officer of FINMA suggested introducing a new licensing category for financial innovators and a license exempt area (sandbox).<sup>21</sup> FINMA focuses amongst other things on reducing obstacles to FinTech, which will also benefit Crowdfunding platforms in Switzerland.<sup>22</sup> This proposal was then picked up and pursued by the Swiss Federal Council.<sup>23</sup> Furthermore, to remove technical barriers to FinTech firms, FINMA has amended existing regulations. In particular, it enabled the use of on-line and video identification for money laundering prevention purposes to make the process more technology-friendly.<sup>24</sup>

### 2.1.3 Swiss State Secretariat for Economic Affairs (SECO)

In December 2013, SECO has published a discussion paper called "Diskussionspapier Risiko-kapital in der Schweiz".<sup>25</sup> This document gives an overview over the forms of Crowdfunding, the platforms in Switzerland and the current regulation in Switzerland and some other countries. Moreover, the authors of the document formulated some recommendations in terms of the necessity to intervene in this area. They especially recommend that FINMA issue a policy paper stating its view on various issues in relation to Crowdfunding. Furthermore, the report recommends amending various legislations to clarify the scope and applicability to Crowdfunding.<sup>26</sup> However, this document caused neither wide discussions nor actions in Switzerland.<sup>27</sup>

In October 2015, SECO has published another opinion called "Crowdfunding – neue Möglichkeiten für Publikumsfinanzierungen"<sup>28</sup>. The document reflects on the opportunities and challenges of Crowdfunding in Swiss tourism and how the Swiss Confederation might encourage financing tourism investments through Crowdfunding.

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<sup>20</sup> See e.g. <http://www.tagesanzeiger.ch/schweiz/standard/Die-Fallstricke-des-CrowdfundingBooms/story/27666437>.

<sup>21</sup> This speech can be downloaded under <https://www.finma.ch/en/documentation/finma-publications/addresses-and-specialist-articles/#Order=4>; for details see below section 3.1.2.

<sup>22</sup> See <https://www.finma.ch/en/news/2016/03/20160317-mm-fintech/>.

<sup>23</sup> See below, sections 2.2 and 3.1.3.

<sup>24</sup> See <https://www.finma.ch/en/news/2015/12/20151221-mm-videoidentifizierung/>.

<sup>25</sup> The opinion can be downloaded under [https://www.seco.admin.ch/dam/seco/de/dokumente/Standortfoerderung/KMU-Politik/Finanzierung%20der%20KMU/Studie%20Diskussionspapier%20Risikokapital%20in%20der%20Schweiz.pdf.download.pdf/Studie\\_Diskussionspapier\\_Risikokapital\\_in\\_der\\_Schweiz.pdf](https://www.seco.admin.ch/dam/seco/de/dokumente/Standortfoerderung/KMU-Politik/Finanzierung%20der%20KMU/Studie%20Diskussionspapier%20Risikokapital%20in%20der%20Schweiz.pdf.download.pdf/Studie_Diskussionspapier_Risikokapital_in_der_Schweiz.pdf) (cited: SECO, Diskussionspapier 2013).

<sup>26</sup> On the whole SECO, Diskussionspapier 2013, p. 7 et seq.

<sup>27</sup> See KUNZ, Crowdfunding, para 52.

<sup>28</sup> See

[https://www.seco.admin.ch/seco/de/home/Standortfoerderung/Tourismuspolitik/Tourismus\\_Forum\\_Schweiz/Viertes\\_Tourismus\\_Forum\\_Schweiz.html](https://www.seco.admin.ch/seco/de/home/Standortfoerderung/Tourismuspolitik/Tourismus_Forum_Schweiz/Viertes_Tourismus_Forum_Schweiz.html) (cited: SECO, Diskussionspapier 2015).

### 2.1.4 Federal Office of Culture (FOC).

In March 2016 the Federal Office of Culture and Pro Helvetia published a study called "Crowd-funding im Kulturbereich".<sup>29</sup> The study showed that 216 Crowdfunding projects in the cultural sector raised CHF 4.5 million in 2014. Projects ranged from concerts and festivals to the launch of games and software with 98.8 % of all projects being realized. Crowdfunding from the private sector ensures a cultural diversity, which could not be achieved through government subsidies for culture alone. It is therefore expected that Crowdfunding will become more and more important in the culture sector.

## 2.2 FinTech Reforms

On 2 November 2016, the Swiss Federal Council proposed to ease the Swiss regulatory framework for FinTech-providers by amending Federal Act on Banks and Saving Banks of 8 November 1934 (Banking Act, BankA, SR 952.0) and its implementing ordinance, the Ordinance on Banks and Saving Banks of 30 April 2014 (Banking Ordinance, BankO, SR 952.02).<sup>30</sup> These proposal was followed by a formal consultation proceeding that was opened on 1 February 2016 and lasted until 8 May 2017<sup>31</sup>. The amendments are likely to enter into force at the earliest in 2018.

In a nutshell, the proposal consists in two exemptions and a special regime for FinTech firms, which will allow firms to accept funds without being subject to the requirements applicable to fully fledged bank.<sup>32</sup> This reform if accepted will reduce the barriers to entry for Crowdfunding platforms and other FinTechs and increase the overall competitiveness of the financial center.

The draft amendments to the Banking Act and Banking Ordinance proposed by the Federal Council to encourage FinTechs will not extend to anti-money laundering regulations. Therefore, FinTechs will continue to be subject to the AMLA. However, FINMA has implemented certain enhancements to existing regulations to make it more technology-friendly, like enabling video identification for money laundering prevention purposes.<sup>33</sup>

## 2.3 Financial Market Infrastructure Act, future Financial Services and Markets Act and future Financial Institutions Act

In addition to FinTech and crowding related developments, Switzerland is in the process of restructuring its financial market regulation. However, neither the newly implemented FMIA, the future FinSA nor the future FinIA address Crowdfunding directly.<sup>34</sup> Nevertheless, especially the FinSA and FMIA might have some impact on Crowdfunding platforms. The

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<sup>29</sup> See [https://prohelvetia.ch/app/uploads/2016/06/03-Crowdfunding\\_im\\_Kulturbereich\\_final\\_digital.pdf](https://prohelvetia.ch/app/uploads/2016/06/03-Crowdfunding_im_Kulturbereich_final_digital.pdf).

<sup>30</sup> See <https://www.admin.ch/gov/en/start/documentation/media-releases/media-releases-federal-council.msg-id-64356.html>.

<sup>31</sup> See <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-65476.html>.

<sup>32</sup> See below, section 3.1.3.

<sup>33</sup> See <https://www.finma.ch/en/news/2015/12/20151221-mm-videoidentifizierung/>.

<sup>34</sup> See KUNZ, Crowdfunding, para 63.

FMIA can be relevant to platforms if they qualify as a stock exchange or a trading system.<sup>35</sup> The FinSA can bear some consequences for the Equity Model since it aims to introduce a comprehensive prospectus regime for equity offerings. Moreover, platforms may be subject to rules of conducts if they, for instance, buy and sell securities, receive and transmit orders in connection with securities or if they hold assets for the account of a client.

### 3 Current regulation of Crowdfunding in Switzerland

Although Crowdfunding is not subject to specific regulations, Crowdfunding platforms, depending on the particular Model, can be subject to a number of laws and regulations governing the financial intermediaries.

When a Crowdfunding platform accepts funds from investors and transfers them to the target companies, the Banking Act and its implementing ordinances are likely to apply. By contrast, if the Crowdfunding platform acts as a securities dealer by trading in securities on behalf of clients and either taking custody of the securities or holding them with a third party on behalf of clients, the Federal Act on Stock Exchanges and Securities Trading of 24 March 1995 (Securities Trading Act, SESTA, SR 954.1) may apply. Although the SESTA is focused on the secondary market, this also can be the case when a platform subscribes securities and places them with investors on the primary market. If, instead, the Crowdfunding platform allows investors to pool their investments or distributes interests in a vehicle used to pool investments, the Federal Act on Collective Investment Schemes of 23 June 2006 (Collective Investment Schemes Act, CISA, SR 951.31). Furthermore, if the Crowdfunding platform acts as trading platform, the Federal Act on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading of 19 June 2015 (Financial Market Infrastructure Act, FMIA, SR 958.1) should be considered. The same also applies if the platform constitutes a central counterparty, a central securities depository or a payment system. Finally, in all cases, where the Crowdfunding platform has the power to dispose over financial assets of investors, it is likely to be within the scope of the Federal Act on Combating Money Laundering and Terrorist Financing of 10 October 1997 (Anti-Money Laundering Act, AMLA, SR 955.0).

Furthermore, public offerings of shares and bonds are subject to prospectus requirements. Finally, the Federal Act on Consumer Credit of 23 March 2001 (Consumer Credit Act, CCA; SR 221.214.1) can come to apply to loans granted to consumers through a Crowdfunding platform.

#### 3.1 License under the Banking Act

##### 3.1.1 General rule

Under the Banking Act and the Banking Ordinance, natural persons and/or legal entities (collectively persons, each a person) mainly active in the financial sector intending to either (a) accept deposits from the public on a professional basis, or (b) finance an undetermined

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<sup>35</sup> See below, section 3.4.

number of persons or companies (with which they do not form an economic unit of their own) by refinancing themselves from five or more banks, to require a banking license from FINMA. This licensing requirement also applies to persons who solicit deposits from the public (in advertisements, prospectuses, circular letters, electronic media or similar publication media).

The Banking Ordinance provides for a broad definition of deposits including all liabilities owed to clients. It does, however, contain a list of exemptions for funds not qualifying as deposits. According to this list, inter alia, the acceptance of (i) funds provided in consideration for a transfer of property or the rendering of a service under a contract or as collateral for the performance of an obligation or (ii) funds accepted on interest-free accounts for the purpose of settlement of client transactions of securities dealers, precious metal traders, asset managers and similar firms are not considered as deposits.

A person is considered to act on a professional basis in case it accepts on an ongoing basis more than 20 deposits from the public.

### 3.1.2 Legal consequences for the Crowdfunding platforms in Switzerland

Crowdfunding platforms generally seek to avoid the onerous requirements of obtaining a banking license. To do so, they should ensure that they do not accept public deposits as part of the financing of a financing campaign or the administration of an investment. Under the current regulations this is best done by ensuring that the platform does not collect funds from investors on its own account or maintain accounts in the name of the investors, e.g. to accept funds from investors for the purchase of shares or for loans to be granted to the funded companies or to accept payments (interest, principal, or dividends) from the companies in the name and for the account of such investors.<sup>36</sup>

Moreover, under the current Swiss legislation, the financing third parties may also qualify as financing under the Banking Act. Crowdfunding platforms should therefore generally be cautious when providing such services (e.g. to grant loans to the companies in the name and for the account of the investors).

### 3.1.3 Proposed Amendments

The licensing requirements under the Banking Act are cumbersome and, arguably, impose an undue burden on Crowdfunding platforms and other FinTechs. The Federal Council therefore has initiated a reform process to introduce two new exemptions from the licensing requirements and a new regulatory regime, which could benefit various Crowdfunding platforms.

The first exemption would allow Crowdfunding platforms to hold funds for settlement purposes for an extended period of time of up to 60 days. Under the Banking Ordinance, funds held on interest-free settlement accounts of securities dealers, precious metals traders, asset

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<sup>36</sup> See BGE 2C\_352/2016 of 9 December 2016; REICHMUTH/VON DER CRONE: Crowdlending als bewilligungspflichtige Entgegennahme von Publikumseinlagen, in: SZW/RSDA 2/2017.

managers and other similar firms do not qualify as deposits. FINMA currently considers that funds can be held on such settlement accounts for at most seven days. Fundraising for Crowdfunding projects typically takes longer than that, thus limiting the practical relevance of this exemption. The Swiss Federal Council is therefore proposing the period to 60 days. This would allow Crowd-funding platforms to collect funds from the crowd on accounts in its own name and to hold on to them for 60 days without requiring a banking license, as long as no interest is paid on such funds and that the funds are used for settlement purposes.

Similarly, under the current regulation, a person collecting more than 20 deposits or holding themselves out as accepting deposits from the public (even if this results in fewer than 20 deposits) is deemed to act "on a commercial basis" and is thus subject to licensing requirements. Crowdfunding platforms typically try to attract as many clients as possible and will therefore quickly exceed the threshold of 20 deposits. At the suggestion of Mark Branson, CEO of FINMA, the Swiss Federal Council proposed to amend the Banking Ordinance to introduce a "sandbox" in terms of an innovation area, which is exempted from a licensing requirement. Under this proposal, providers will be able to accept public funds up to a total value of CHF 1 million before having to apply for a banking license. However, providers operating under the sandbox exemption would be required to inform their clients that they do not hold a FINMA license and therefore do not enjoy the protection of the deposit guarantee scheme. This exemption may interest for platforms which may seek to hold funds for an extended period of time or for an indeterminate purpose, and which will, therefore, not be able to enjoy the settlement exemption. The quantitative restriction, however, will limit the practical interest of this exemption to fairly small platforms and will be most likely to be of interest for early-stage platforms which are still seeking to establish a proof-of-concept.

The Federal Council intends, however, to create a new license type for larger entities, which accept public deposits but do not engage in commercial banking. This regime will allow platforms to accept to a maximum of CHF 100 million of public deposits, provided that they (i) do not pay any interest to depositors and (b) do not invest the deposits. The regulatory requirements for this type of license will be significantly reduced. Notably, the license will trigger substantially lower and simpler capital adequacy requirements than an ordinary banking license (probably five percent of the accepted public funds, but no less than CHF 300,000)<sup>37</sup>. This will allow platforms to maintain accounts for investors and offer various administrative services for investors, such as collecting dividends or interest payments and transfer them to investors, rather than merely brokering deals and forwarding instructions without actually managing the payments.

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<sup>37</sup> See Federal Department of Finance, Änderung des Bankengesetzes und der Bankenverordnung (FinTech): Erläuternder Bericht zur Vernehmlassungsvorlage, 1 February 2017, p. 31.

## 3.2 License under SESTA

### 3.2.1 General rule

Pursuant to SESTA, all persons qualifying as securities dealers are required to obtain an authorization from FINMA. A securities dealer is defined as a person or partnership who, in its professional capacity, (a) buys and sells securities on the secondary market, either (i) for its own account with the intent of reselling them within a short period of time or (ii) for the account of third parties, (b) publicly underwrites securities on the primary market, or (c) creates derivatives and offers them to the public.

Securities dealers include in particular own-account dealers (dealers who, in their professional capacity, trade in securities for their own account on a short-term basis), client dealers (dealers who, in their professional capacity, trade in securities in their own name for the account of clients) and issuing houses (securities dealers who, in their professional capacity, underwrite securities issued by third parties on a firm basis or against commission and offer them to the public on the primary market).

### 3.2.2 Legal consequences for Crowdfunding platforms in Switzerland

In the light of the foregoing, Crowdfunding platforms should, inter alia, refrain from the following business activities in order not to be considered a securities dealer:

- A. Trading of securities, including shares (or similar participation rights) and bonds, in companies presented on the platform in the name and for the account of the investors and, in particular, not (i) maintain any accounts for the settlement of transactions for such investors by itself or with third parties, and/or (ii) hold any securities, including shares (or similar participation rights) and bonds, on behalf of the investors in safe custody with itself or with third parties but in its own name; and
- B. Underwriting any kind of securities (in particular shares or bonds) newly issued by companies presented on the platform on a firm basis or against commission and subsequently publicly offer such securities to investors.

These restrictions apply mainly to the Equity Model. The Lending Model is not subject to these rules, unless the loan is deemed to be a bond. Furthermore, these requirements do not apply to the Donation/Rewards Models as well as direct investments in real estates or receivables.

## 3.3 License under the Federal Act on Collective Investment Schemes (CISA)

### 3.3.1 General rule

According to CISA, all persons responsible for the management of collective investment schemes, the safekeeping of assets held in such schemes as well as the distribution of such schemes to retail (i.e. non-qualified) investors are required to obtain an authorization from FINMA.

Collective investment schemes are defined as assets raised from several investors for the purpose of collective investment, and which are pooled and collectively managed for the account of such investors.

Distribution is generally defined as any offering of and advertising for collective investment schemes and covers any kind of activity which is aimed at investors acquiring collective investment schemes.

An exemption from the above authorization obligation applies if (i) the funds are solely invested in one operating company which is active in a manufacturing, trade or service business and generates its revenues and profits with such business (and not solely by way of committing funds), or if (ii) the investment decisions are primarily made by the investors and not by the management of the investment scheme.

Loans granted to a collective investment scheme should in principle also be outside the scope of the CISA. However, each case needs to be assessed globally, i.e. taken as a whole it must in a specific case be excluded that a loan (due to its risk profile or repayment schedule) can be characterized as an investment in a collective investment scheme.

### 3.3.2 Equity Model

To be outside the scope of the collective investment scheme regulation, an equity based Crowdfunding platform should be set up in a way that it is able to primarily profit from the exemption applicable with regard to investments into operating companies. Therefore, it should introduce possible investors to operating companies only and should refrain from any activities which could result in the platform pooling or managing funds received from the investors for the account of such investors by investing them collectively into a company via the platform itself. In other words, the platform should only act as an intermediary for purposes of information exchange (e.g. names, phone numbers and other contact details) with regard to possible direct investments into specific operating companies and not directly or indirectly transfer any funds from investors to companies.

### 3.3.3 Lending Model

A debt based Crowdfunding platform should generally avoid holding itself out as a collective investment scheme, i.e. an institution for the collective management of third party funds. Therefore and in order not to be subject to regulation by FINMA, such platforms should avoid (i) accepting funds from investors, (ii) pooling such investments from investors in the name of the platform in a way that the investments cannot be personalized anymore, and (iii) subsequently granting such investments as loans granted by the platform to a company advertising on the platform.

Basically the situation is the same as described above with regard to Equity Models; i.e. loans granted directly to operating companies or to private persons only (and in particular not to the operator of the platform for further on-lending) should fall outside the scope of the CISA. Even if loans were to be granted by an investor to a collective investment scheme presented

on the platform (but operated by a party other than the operator of the lending platform), the operator of the platform should still not be subject to the CISA, because granting a loan to a collective investment scheme should not be qualified as distributing a collective investment scheme.

Further, the investment decision to grant any funds to a specific company should always remain with and be made by the investor itself and not by the platform. Therefore, contractual arrangements appearing as third party management of funds should generally be carefully examined.

### 3.3.4 Donations or Rewards Model

Normally, these platforms are structured in a way that the contributions are not investments related to a direct return, if any, and therefore such platforms do not fall under the collective investment schemes regulations.

## 3.4 Financial Market Infrastructure Act (FMIA)

### 3.4.1 General rule

Under the FMIA, trading venues, such as stock exchanges and multilateral trading facilities (MTF), are subject to licensing requirements. The main difference between these two is that a stock exchange can list securities whereas an MTF does not. Therefore, both stock exchanges and multilateral trading facilities are subject to a large extent to the same regulatory regime regarding pre- and post-trade transparency and are separated only by the regulatory requirements applicable to listing securities and admitting them to trading.

Organized trading facilities are also regulated under the FMIA. However, they are subject to a significantly less strict regulatory regime than trading venues.<sup>38</sup> They are defined as (a) trading facilities set up for multilateral trading but fall short of the definition of a multilateral trading facility, (i) because they are not based on non-discretionary rules but rely on discretionary rules or (ii) because, although they provide for non-discretionary rules, they do not allow for the trade securities, defined under the FMIA as certificated and uncertificated securities, derivatives and intermediated securities which are suitable for mass trading (article 2 (b) FMIA), but other financial instruments or (b) bilateral trading systems whose purpose is the exchange of bids.

Organized trading facilities, unlike stock exchanges and multilateral trading facilities, are not subject to a specific licensing regime but must be either operated by a bank, a securities dealer or a trading venue or as a subsidiary of a financial group controlled directly by a financial market infrastructure and be subject to consolidated supervision by FINMA (article 43 FMIA).

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<sup>38</sup> See FINMA Circular 2018/1, Organised trading facilities, Duties of operators of organised trading facilities, published on 25 January 2017 and entering into force on 1 January 2018, N 23.

Furthermore, the FMIA sets out licensing requirements for central counterparties, central securities depositories and payments systems. The latter being subject to licensing and supervision only if they are systemically relevant.

### 3.4.2 Legal consequences for Crowdfunding platforms in Switzerland

A Crowdfunding platform should generally be careful not to qualify as a stock exchange, multi-lateral trading facility or an organized trading facility, if they offer services which should facilitate trading in securities (e.g. services other than providing information on possible secondary trading opportunities). Normally, Crowdfunding platforms operating under the Equity Model should not qualify as a stock exchange, multilateral trading facilities or organized trading facility because they present direct investment into newly issued securities and thus facilitate primary market transactions. However, an analysis on a case-by-case basis is recommended.

In particular, Crowdfunding platforms under the Equity Model, which aim to facilitate the interaction between investors and entrepreneurs by presenting the offering in a structured does not aim constitute a trading venue or an organized trading facility, if they do not offer the simultaneous exchange of bids or if the conclusion of the contracts occurs outside of the Crowdfunding platform rather than between the investor and the Crowdfunding platform itself.<sup>39</sup> However, a more careful analysis is warranted if the Crowdfunding platform allows for interaction among investors or allows entrepreneurs to sell existing shares.

Similarly, if a Crowdfunding platform seeks to act as central counterparty or a central securities depository, it will be subject to regulation under the FMIA. Due to the limitation of the rules on payment systems to systemically important systems, it is unlikely that a Crowdfunding platform will be subject to these rules.

Moreover, other Crowdfunding models are not concerned by the licensing requirements under the FMIA. This applies in particular to the Lending model (as long as the investors act as borrowers under loan agreements as opposed to investors in bonds), direct investments in real estate or receivables, which both do not constitute financial instruments and, generally, the Donation and Rewards Model.

## 3.5 Anti-Money Laundering Act (AML)

### 3.5.1 General rule

Pursuant to the AMLA, persons providing services as financial intermediaries must be affiliated with a recognized self-regulatory organization or need to obtain a license from FINMA for their professional business activities. In addition, financial intermediaries must comply with the statutory provisions and procedures of the AMLA, e.g. verification duties

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<sup>39</sup> See CLEMENTSON/TRIBOLET, Switzerland's approach to regulating Crowdfunding, February 2016.

regarding the identity of the customer (and the beneficial owner), duties to clarify and to keep records, and certain organizational measures.

Financial intermediaries are in particular persons who, in their professional capacity, accept or keep third party funds or who assist in the investment or transfer of such funds, such as persons carrying out credit transactions, providing services for payment transactions or assets, or securities managers and persons making actual investments in their capacity as investment advisors. However, persons solely providing investment advisory services (including platforms who act as intermediary without assisting in any kind in the transfer or flow of funds) are not considered as financial intermediaries.

### **3.5.2 Legal consequences for Crowdfunding platforms in Switzerland**

Whether an operator of a Crowdfunding platform (irrespective of the model operated) falls under the money laundering regulation very much depends on whether it limits its services to (i) providing information on possible investments, (ii) acting as intermediary with regard to possible transaction and/or (iii) provides solely advisory services (in all three cases without assisting in the transfer or flow of funds), in which cases the money laundering regulation should theoretically not apply.

Other services offered in connection with investments presented on a platform, such as (i) services facilitating the execution of a transaction (e.g. assisting investors and/or companies or borrowers in the investment or transfer of funds), (ii) accepting or keeping funds of investors and/or companies or borrowers, (iii) the platform making investments on behalf of investors, or (iv) the platform enabling the operator of the platform to dispose of funds or financial assets (even on the basis of specific instructions only), need to be carefully analyzed.

In particular, services provided by the operator of the platform in connection with (i) the flow of funds, (ii) keeping securities, or (iii) keeping accounts of investors will most likely bring a platform operator within the scope of the money laundering regulations as it will be considered a financial intermediary subject to the AMLA.

As a practical matter, whenever the platform has control over the funds, either by accepting them and forwarding them from and to the investors, the platform is very likely to be subject to anti-money laundering regulations.

## **3.6 Prospectus requirements**

In case equity securities or bonds are publicly offered for subscription, the issuing company needs to establish and issue an issue prospectus containing certain information regarding, inter alia, the company and its business activities. Generally speaking, any invitation to subscribe for equity securities which is not addressed solely to a limited number of persons is considered as a public offer. As a matter of Swiss law, the issuance prospectus does not need to be approved or filed with a governmental authority.

To our knowledge, Crowdfunding platforms in Switzerland do not make public offers for their own equity or debt securities, but merely assist the issuer in placing its securities. Therefore, they are generally not directly subject to the prospectus requirements under Swiss law. If in a particular case, an issue prospectus were required, the company itself would be the one obligated to produce, issue and publicly distribute such prospectus to the investors.

Despite the obligation to produce an issue prospectus lying with the companies offering their equity or debt securities publicly, one needs to keep in mind that anyone who, upon the issuance of equity or debt securities, intentionally or negligently contributed to an issue prospectus (or similar distribution material) containing incorrect, misleading or incomplete information, is liable to the acquirers of such newly issued and publicly sold shares for any damage caused in connection with the public offer of such shares. Accordingly, operators of platforms should put adequate measures in place to limit the risk of such prospectus liability.

The planned FinSA regulations will introduce a new and comprehensive Swiss prospectus regime for equity offerings, which will be largely modeled after the EU prospectus framework and might have an impact on the Equity Model. Under the new regulations offering prospectuses would have to be approved by a new regulatory body, subject to exemptions or partial or complete relief from the prospectus requirements. The prospectus and approval requirement will apply to all public offerings in Switzerland and to all securities that are to be admitted on a trading platform in Switzerland.

### **3.7 Consumer Credit Act (CCA)**

#### **3.7.1 General rule**

According to the Swiss Consumer Credit Act (Konsumkreditgesetz, CCA), a person regularly acting as a consumer credit broker is required to obtain an authorization from its canton of residence for the provision of such services.

A consumer credit agreement is defined as an agreement according to which a person who regularly grants credits in the course of its business (creditors) grants or promises to grant a credit to a consumer in the form of a deferred payment, a loan or a similar financial accommodation. Credit agreements entered into by creditors who do not regularly grant loans are not considered to be consumer credit agreements. Furthermore, certain consumer credit agreements are excluded from the scope of the CCA, in particular those with an amount of less than CHF 500 or exceeding CHF 80,000 or those with a duration of less than three months.

Besides the authorization requirement for consumer credit brokers mentioned above, the CCA requires that consumer credit agreements comply with certain material and formal requirements and that the consumers shall not be obliged to pay any compensation to a credit broker.

### 3.7.2 Legal consequences for Crowdfunding platforms in Switzerland

Crowdfunding platforms (including debt-based platforms) do normally not grant credits falling under the definition of a consumer credit mainly because the lenders normally are not persons who regularly grant credits in the course of their business. However, under the Lending Model, unless the Crowdfunding platform can rule out their lenders qualify as persons who regularly grant credit, they are at risk of falling under the scope of the CCA. Indeed, should the credit agreements offered on the platforms qualify as consumer credit agreements, the operators of such platforms are likely qualify as consumer credit brokers and thus require authorizations from their canton of residence. To avoid such qualification, operators of lending platforms should either exclude lenders who regularly grant credits in their professional capacity or obtain an authorization from its canton of residence for the provision of a consumer credit broker services.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable Law

As a matter of principle, the Swiss regulatory regime is fundamentally open to inbound offerings on a pure-cross border basis. Thus, the Banking Act and SESTA as well as the AMLA do not apply, in principle, to foreign entities that offer their services on a cross-border basis without a permanent physical presence in Switzerland. Therefore, it is generally open to Crowdfunding platforms based in other jurisdictions. Two exceptions should be however noted: the FMIA requires foreign trading venues, but not organized trading facilities, to be recognized by FINMA, if they allow Swiss securities dealers to participate directly to their system. More importantly, the CISA applies for the distribution of foreign collective investment schemes in or from Switzerland, thus also capturing cross-border offerings into Switzerland.

By contrast, Swiss law generally does not treat outbound offerings differently from domestic ones and thus the general regime applies to a platform regardless whether it addresses domestic investors or foreign ones.

The main challenge results from the complexity of the prospectus rules and the conflict of law rules determining the applicability of the CCA.

Overall, these issues are mainly applicable to the Equity Model and to a lesser extent the Lending Model.

### 4.2 Inbound

#### 4.2.1 Foreign Crowdfunding platform addresses Swiss investors

##### 4.2.1.1 Crowdfunding platform

###### (1) Licence obligations under the Banking Act and SESTA

Under certain conditions, foreign banks and securities dealers are required to obtain authorization from FINMA. Thus, Foreign Crowdfunding platforms might be subject to license requirements if they qualify as foreign securities dealers or banks.

Under Swiss law, a foreign bank or securities dealer is a company organized according to foreign law that:

- maintains a securities dealer/banking license in a foreign country;
- uses the term "securities dealer"/"bank" or "banker" or terms of similar meaning in the company name, the company purpose or its business documents; or
- performs securities trading (in the meaning of article 2 lit. d SESTA) /banking activities (in the meaning of article 2 Banking Ordinance) (see article 38 (1) Ordinance on Stock Exchanges and Securities Trading ("SESTO") and article 1 (1) FINMA-Ordinance on Foreign Banks ("FBO-FINMA")).

Foreign securities dealers and banks are required to obtain authorization from FINMA if they engage people in Switzerland who, on a permanent and commercial basis in or from Switzerland:

- enter into transactions/trade in securities, maintain client accounts or legally bind the foreign securities dealer/bank (i.e. branch); or
- operate in another way, in particular by passing on client orders to the foreign securities dealer/bank or by representing it for marketing or other purposes (i.e. representative of-fice) (see article 2 (1) FBO-FINMA and article 39 (1)(a) SESTO).

Therefore, if a foreign bank or securities dealer has a permanent physical presence in Switzerland, including through a representative office, a branch or, even, in some circumstances an introducing broker, it is likely to require a license in Switzerland. This conclusion also holds, as a matter of principle, even if no business that would trigger a licensing requirement is carried out in Switzerland.

By contrast, no banking or securities dealer license requirements are triggered, if a Crowdfunding platform which qualifies as a foreign securities dealer or bank does not have any physical presence in Switzerland, as pure cross-border banking or securities dealer activities from abroad into Switzerland are not regulated by Swiss law. FINMA has, however, from time to time, taken a consolidated view to business carried out through affiliates in Switzerland, typically, when a Swiss entity carries out a part of the business (e.g. marketing or financing) and a foreign entity another part (e.g. accepting deposits) and considered the business as a whole.

## **(2) Licence obligations under the FMIA**

The FMIA has a cross-border reach. Under Swiss law, stock exchanges and multilateral trading facilities organized under foreign law must obtain recognition from FINMA if they want to grant Swiss securities dealers access to their trading facilities (article 41 FMIA).

Therefore, should a foreign Crowdfunding platform qualify as a stock exchange or multilateral trading facility under the FMIA, it would need to obtain the recognition of FINMA before giving access to Swiss securities dealers access to their platform.

Should the foreign Crowdfunding platform, however, qualify as an operator of a foreign organized trading facility under the FMIA, it would not be subject to recognition requirements. Operators are, however, at liberty to undergo a recognition process for Switzerland.<sup>40</sup>

### **(3) Federal Act on Collective Investment Schemes (CISA)**

The CISA has a cross-border reach. It applies in particular to (i) foreign collective investment schemes which are distributed in Switzerland, (ii) to persons who manage foreign collective investment schemes in or from Switzerland, (iii) to persons who distribute, from Switzerland, foreign collective investment schemes which are not exclusively reserved for qualified investors or subject to equivalent foreign law and (iv) to persons who represent foreign collective investment schemes in Switzerland (article 2 (1) (b-f) CISA). Qualified investors under the CISA include inter alia regulated financial intermediaries such as banks, securities traders, fund management companies and asset managers of collective investment schemes, as well as central banks, regulated insurance institutions, public entities and retirement benefit institutions with professional treasury operations and companies with professional treasury operations (article 10 (3) CISA).

However, a case-by-case basis analysis is necessary to determine whether the CISA applies to the target company or the Crowdfunding platform<sup>41</sup>. If the target is deemed to constitute a foreign collective investment scheme, the distribution to non-qualified investors in Switzerland will be conditioned on the prior approval of FINMA. Even the distribution to qualified investors is conditioned on several requirements, including appropriate supervision in Switzerland or in the country of domicile of the distributor.

### **(4) Anti-Money Laundering Act (AMLA)**

The Swiss anti-money laundering regulations do not apply to Crowdfunding platforms that are domiciled abroad and offer their services into Switzerland on a pure cross-border basis, namely without employing persons permanently on the ground in Switzerland and without establishing a branch or representative office or any other form of relevant physical presence in Switzerland.<sup>42</sup>

### **(5) Prospectus requirements**

As a matter of Swiss conflict of law rules, the prospectus requirements of the law of the state of incorporation of the issuer or alternatively the law of the state where the public

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<sup>40</sup> See FINMA Guidance 01/2016: Financial Market Infrastructure Act: FINMA's next steps, published on 6 July 2016.

<sup>41</sup> See above, section 3.3.

<sup>42</sup> See HSU/FLÜHMANN, European FinTech Special Focus Switzerland, Regulating innovation, in: International Financial Law Review, p. 42.

offering was made applies. Therefore, if a foreign Crowdfunding platforms addresses Swiss investors, a number of laws may apply: the law of the state of incorporation of the company or the project, the law of the states where the public offering was made, including Swiss law when an offer is addressed to Swiss investors, thus meaning that multiple laws may apply to the same cross-border offering.

#### **(6) Consumer Credit Act (CCA)**

The CCA applies to a cross-border consumer credit agreement with Swiss consumers if as a matter of Swiss private international law, Swiss law applies to the consumer credit agreement. Therefore, should the credit agreements offered on the platforms be qualified as consumer credit agreements under CCA, a foreign Crowdfunding platform addressing Swiss investors might qualify as consumer credit brokers and thus require authorization.<sup>43</sup>

##### **4.2.1.2 Company / project**

#### **(1) Licensing Requirements**

Generally speaking the company/project is not regulated because it relies on Crowdfunding, unless it constitutes a collective investment scheme (or its business is otherwise a regulated).

#### **(2) Prospectus regulation**

As a matter of Swiss conflict of law rules, the prospectus requirements of the law of the state of incorporation of the issuer or alternatively the law of the state where the public offering was made applies. Therefore, if a foreign Crowdfunding platforms addresses Swiss investors, a number of laws may apply: the law of the state of incorporation of the company or the project, the law of the states where the public offering was made, including Swiss law when an offer is addressed to Swiss investors, thus meaning that multiple laws may apply to the same cross-border offering.

#### **4.2.2 Foreign Crowdfunding platform addresses Swiss companies/projects**

Swiss regulatory law does in principle not distinguish whether foreign Crowdfunding platforms offers its services to Swiss companies or Swiss investors. Therefore, in general, the above mentioned rules for foreign Crowdfunding platforms addressing Swiss investors<sup>44</sup> also apply to foreign Crowdfunding platforms addressing Swiss companies.

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<sup>43</sup> See above, section 3.7.2.

<sup>44</sup> See above, section 4.1.1.

## 4.3 Outbound

### 4.3.1 Swiss Crowdfunding platforms addresses foreign (EU) investors

#### 4.3.1.1 Crowdfunding platform

As a matter of Swiss law, the same licence requirements apply for Swiss Crowdfunding platforms regardless whether they address domestic (Swiss) investors or foreign (EU) investors. The general considerations in Section 3, above, therefore apply to Swiss Crowdfunding platforms addressing foreign (EU) investors.

#### 4.3.1.2 Company / Project

##### (1) Collective Investment Schemes

If a Swiss Crowdfunding platform addresses foreign investors, the CISA may apply to the company or the project, if it is deemed to constitute a collective investment scheme. This regime is, however, not different from a purely domestic distribution of Swiss or foreign collective investment schemes in Switzerland.

##### (2) Prospectus regulation

As a matter of Swiss conflict of law rules, the prospectus requirements of the law of the state of incorporation of the issuer or alternatively the law of the state where the public offering was made applies. Therefore, if a Swiss Crowdfunding platform addresses foreign (EU) investors, a number of laws may apply: the law of the state of incorporation of the company or the project, the law of the states where the public offering was made, thus meaning that multiple laws may apply to the same cross-border offering.

### 4.3.2 Swiss Crowdfunding platform addresses foreign companies / projects

#### 4.3.2.1 Crowdfunding platform

##### (1) Licence obligation

Swiss regulatory law does in principle not make a difference between Swiss Crowdfunding platforms addressing companies or investors. Therefore, in general, the above mentioned rules for Swiss Crowdfunding platforms addressing foreign investors<sup>45</sup> also apply to Swiss Crowdfunding platforms addressing foreign companies.

With regard to the Lending Model, should the credit agreements offered on the platform be qualified as consumer credit agreements, the operators of such platform might qualify as consumer credit broker and thus require authorization from its canton of residence.<sup>46</sup>

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<sup>45</sup> See above, section 4.2.1.

<sup>46</sup> See above, section 3.7.2.

#### 4.4 Impact of EU regulation

Switzerland is not a member of the European Union. Therefore EU regulation does not apply in Switzerland. However, the Swiss rules are often largely modelled after EU regulation.

However, the EU regulations can apply to outbound offerings by Swiss platforms into the European Union and can thus restrict the access to these markets for Swiss platforms and, indirectly, deprive EU investors from investing in this market.

#### 4.5 Summary

Switzerland has not implemented specific Crowdfunding regulation yet. However, the following barriers hinder cross-border activities of Crowdfunding platforms from a Swiss perspective:

- Depending on the services offered by the Crowdfunding platform in question, the operator of the platform would be subject to possible license or recognition requirements under the Swiss Banking Act, Sesta, FMIA, CISA, AMLA and/or CCA. However, most of these regulations do not apply to Crowdfunding platforms that are domiciled abroad and offer their services into Switzerland on a pure cross-border basis that is without employing persons permanently on the ground in Switzerland and without establishing a branch or representative office or any other form of relevant physical presence in Switzerland. Thus, making inbound offers fairly easy on a pure cross-border basis.
- Two exceptions should be however noted: the FMIA requires foreign trading venues, but not organized trading facilities to be recognized by FINMA, if they allow Swiss securities dealers to participate directly to their system. More importantly, the CISA applies for the distribution of foreign collective investment schemes in or from Switzerland, thus also capturing cross-border offerings into Switzerland
- Foreign companies / projects might face different local prospectus regimes in case they approach Swiss investors.
- Switzerland is not a member of the European Union and therefore the EU regulation does not apply in Switzerland. Either the operator of the Crowdfunding platform or the companies / projects might face additional local financial regulation requirements when participating in cross-border Crowdfunding.

However, the amendment of the Banking Act and Banking Ordinance in favour of FinTechs as well as the bill for a FinSA and FinIA will have effects on Crowdfunding platforms.

## 5 Lessons learned from Switzerland's regulation for a possible harmonized Euro-pean Crowdfunding regulation

### 5.1 Role model ("dos")

Currently, the Swiss prospectus requirements are limited (no pre-approval for non-listed securi-ties), which allows companies to raise funds at relatively low cost.

Another positive aspect regarding the Swiss regulation is the flexibility it gives. It is advisable also in view of a possible harmonized European Crowdfunding regulation to retain some flexibility on how to regulate Crowdfunding platforms. This allows the regulation to be tailored to the size and business model of Crowdfunding platforms.

This flexibility is supported by a constructive attitude of regulators, who are open to a dialogue to ensure that Crowdfunding platform are implemented in compliance with applicable laws.

### 5.2 Aspects that should be avoided ("don'ts")

We can learn from the Swiss system that the flexibility of the regulatory framework has a down-side: the case-by-case approach leads to legal uncertainty and higher costs for platforms, be-cause the authorities as well as the Crowdfunding platform's operators need more time and resources to evaluate the requirements and legality of the operator's activities because there is no standardized procedure.

Moreover, the overall uncertainty and the lack of de minimis exemptions or specific exemptions for Crowdfunding prevents further growth in this area.<sup>47</sup> However, the proposed amendments of the Banking Act and the Banking Ordinance will provide for exemptions and special regulation for FinTech companies which would also benefit Crowdfunding platforms.

## 6 Conclusion

In 2016, CHF 128.2 million were collected through Crowdfunding in Switzerland compared to CHF 27.3 million in 2015 and CHF 15.8 million in 2014. Nevertheless, the Swiss Crowdfunding market remains rather small in comparison with the USA, the UK and other European countries.

There is currently no specific legislation or regulation in Switzerland explicitly addressing Crowdfunding platforms in Switzerland. However, Switzerland is in the process of restructuring the regulatory framework regarding its financial market and the issue is getting more and more attention from different sides of government. Already today, there are several laws and regula-tions, which may, under certain circumstances, be applicable to Crowdfunding platforms. De-pending on the services provided and on the specific business model, Crowdfunding platforms (irrespective of whether they operate an Equity or Lending

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<sup>47</sup> See SECO, Diskussionspapier 2013, p. 14; HETTICH, PETER, Finanzierungsquellen für KMU im Zeitalter von Crowdfunding, GesKR 2013, 386 et seqq., p. 396.

Model) may require in particular a banking license, a license as securities dealer, a license as a multilateral trading facility and/or a license under the CISA.

Nevertheless, Crowdfunding platforms can be structured with minimal regulatory constraints and some platforms obtained a no-action letters from FINMA, confirming that the platforms as operated do not fall under the scope of application of either the Swiss Federal Act on Banks and Savings Banks, the Federal Act on Stock Exchange and Securities Trading, the Federal Act on Collective Investment Schemes or the Swiss Anti-Money Laundering Act.

The Swiss regulation contains some positive aspects such as the granting of flexibility to authorities and the Crowdfunding platforms as well as limited prospectus requirements. However, it also bears some negative aspects such as the assessment on a case-by-case basis, which causes higher costs and legal uncertainty. The lack of Crowdfunding exemptions is also a downside, which the legislator is planning to address in its amended Banking Act and Banking Ordinance. These negative aspects should be handled differently in a possible harmonized European Crowdfunding regulation.

## 7 Summary – Crowdfunding regulation

| Country  | Switzerland  |
|--|--|
| <p><b>Summary</b></p> <p><b>Recent developments in Crowdfunding regulation</b></p> | <ul style="list-style-type: none"> <li>• Proposed amendment of the Banking Act and Banking Ordinance to ease the Swiss regulatory framework for FinTech providers</li> <li>• FINMA report "How investors can protect themselves against unauthorized financial market providers"</li> <li>• SECO publication "Diskussionspapier Risikokapital in der Schweiz"</li> <li>• SECO publication "Crowdfunding – neue Möglichkeiten für Publikumsfinanzierung"</li> <li>• FOC publication "Crowdfunding im Kulturbereich"</li> <li>• Future Financial Services and Markets Act, Financial Market Infrastructure Act and Financial Institutions Act</li> </ul>   |
| <p><b>Current / planned Crowdfunding regulation</b></p>                            |  |
| <p><b>General regulation</b></p>   | <p><b>Banking Act:</b></p> <ul style="list-style-type: none"> <li>• Collection of funds, keeping of accounts in the name of investors or acceptance of deposits from investors might bring operator within activities covered by Banking Act<br/>→ FINMA license required</li> </ul> <p><b>CISA:</b></p> <ul style="list-style-type: none"> <li>• Pooling and subsequent collective investment of funds into a company might bring operator within scope of CISA<br/>→ FINMA license required</li> <li>• Exemptions for direct investments into an operating company or in case investment decision remains with the investor</li> </ul> <p><b>SESTA:</b></p> <ul style="list-style-type: none"> <li>• Trading of securities, keeping of accounts or underwriting of securities could result in the platform operator being a securities dealer<br/>→ FINMA authorization required</li> </ul> <p><b>FMIA:</b></p> <ul style="list-style-type: none"> <li>• A platform allowing investors to exchange orders to buy and sell securities or financial instruments on the secondary market could qualify as a multilateral trading or organized trading facility<br/>→ Limitation of purpose of the platform to exchange of information (e.g. price, names) and no simultaneous exchange of offers, conclusion of contracts or settlement of contracts</li> </ul> |

|                                      |  |
|--------------------------------------|--|
| <b>Prospectus requirement</b>        | <ul style="list-style-type: none"> <li>• Prospectus requirement for public offer for subscription of equity securities or bonds for companies advertising on the platform; not the platform itself</li> <li>• Platform may be liable for incorrect, misleading or incomplete information in issuing prospectuses or similar offering material</li> </ul>   |
| <b>AIFMD-regulation</b>              | <p><b>CISA:</b></p> <ul style="list-style-type: none"> <li>• Asset management services for collective investment schemes might bring operator within scope of CISA<br/>→ FINMA license required</li> </ul>   |
| <b>Payment service regulation</b>    | N/A  |
| <b>Further possible requirements</b> | <ul style="list-style-type: none"> <li>• Consumer credit regulation</li> <li>• Anti-Money Laundering Act <ul style="list-style-type: none"> <li>- Services regarding flow of funds, keeping of securities or of accounts for investors<br/>→ Operator of platform to be affiliated to a recognized self-regulatory organization or to obtain a license from FINMA</li> </ul> </li> <li>• Data Protection Act (Datenschutzgesetz)</li> </ul>  |
| <b>Regulatory barriers</b>           |  |
| <b>Inbound</b>                       | <p><b>Foreign Crowdfunding platform addresses Swiss investors or companies</b></p> <ul style="list-style-type: none"> <li>• Possible licence requirements for the operator of the platform under the Banking Act, SESTA and/or the AMLA regulations.</li> <li>• However, Banking Act, SESTA and/or the AMLA generally do not apply to Crowdfunding platforms that are domiciled abroad and offer their services into Switzerland on a pure cross-border basis.</li> <li>• Recognition requirements may apply under the FMIA to foreign Crowdfunding platforms qualifying as a trading venue, if they allow Swiss securities dealers to access the platform.</li> <li>• CISA may apply to Crowdfunding platforms addressing Swiss investors, if they distribute collective investment schemes into Switzerland</li> <li>• Possibly different local prospectus regimes applicable for foreign companies / projects when approaching Swiss investors</li> </ul> |
| <b>Outbound</b>                      | <p><b>Swiss Crowdfunding platform addresses foreign investors or companies</b></p> <ul style="list-style-type: none"> <li>• Same licence requirements for Swiss Crowdfunding platforms addressing foreign (EU) investors when addressing Swiss investors</li> <li>• CISA may apply to Crowdfunding platforms addressing Swiss investors, if they distribute collective investment schemes into Switzerland</li> </ul>  |

|                                |  |
|--------------------------------|--|
|                                | <ul style="list-style-type: none"> <li>Swiss Prospectus requirements for Swiss companies apply/ possibly different local prospectus regimes applicable for foreign companies / projects when approaching foreign in-vestors</li> </ul> |
| <b>Impact of EU Regulation</b> |  |
| <b>Prospectus regulation</b>   | <i>EU regulation does not apply in Switzerland</i>   |
| <b>AIFM-Directive</b>          | <i>EU regulation does not apply in Switzerland</i>   |
| <b>MiFID / MiFID II</b>        | <i>EU regulation does not apply in Switzerland</i>   |
| <b>PSD / PSD II</b>            | <i>EU regulation does not apply in Switzerland</i>   |

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# United Kingdom

## 1 Recent developments in the market of Crowdfunding in the UK

It is clear that the Crowdfunding market has grown rapidly from 2014. While an estimated GBP 500m was invested on regulated Crowdfunding platforms over the course of 2013, an estimated GBP 2.7bn was invested over the course of 2015. Whilst at the time of writing there are no reliable published figures for 2016, the consensus is that the industry will have continued to grow in the UK in line with previous years. There are over 100 platforms in the market or seeking authorisation. In July 2016, the UK Financial Conduct Authority (FCA) stated that 9 firms are fully authorised to offer loan-based Crowdfunding platforms and that it was currently considering 88 applications from firms. Additionally, 23 FCA-authorized firms and 11 appointed representatives operate investment-based Crowdfunding platforms

According to the 2015 UK Alternative Finance Industry Report, by the Cambridge Centre for Alternative Finance and Nesta, the loan-based Crowdfunding market has grown rapidly in recent years. The equity-based Crowdfunding market has also grown rapidly, but is still relatively small compared to the GBP 16.7bn in retail sales of investment funds over the course of 2015. The 2015 Alternative Finance Industry Report also shows growth in the market for debt securities (regulated investment products such as bonds or debentures) on Crowdfunding platforms, but that this market remains small in relation to the total volume of lending through such platforms.

The sections below provide an overview of each type of model.

### 1.1 Securities model (investors receive an equity or debt security)

In the UK, the financial services regulatory regimes for corporate finance business and investment funds both tend to shape the structure of investment-based Crowdfunding platforms. The FCA's approach was to acknowledge the permissibility of investment-based Crowdfunding as a valid business model operating under the existing investment-based regime, with minor amendments, as opposed to the creation of a new regulatory regime designed specifically for investment-based Crowdfunding. As a result of this approach, the regulation of platforms offering debt-based securities (such as bonds or debentures) is closer to the regime for equities platforms than it is to non-securities-based lending (known as P2P lending). For example, the FCA clarified its expectations of firms wishing to promote "non-readily realisable securities", covering most unlisted shares and debentures: such investments can be sold on a non-advised basis provided firms ensure the investors have the requisite level of understanding. The FCA has also signalled its disapproval of platform operators making use of exemptions in order to avoid becoming subject to regulation, although the legal loopholes that Crowdfunding firms had been using to operate outside the scope of regulation still exist.

## 1.2 Lending model (investors lend money to a company or project in return for repayment of the loan and interest on their investment)

Crowdlending is commonly referred to as peer-to-peer lending or P2P, although when individuals lend to businesses, many refer to it as P2B (or, increasingly, marketplace lending). The making of non-consumer loans was generally not treated as a regulated activity and so the Crowdfunding Lending Model developed quickly as an alternative to bank lending. However, from 1 April 2014, the new regulated activity of "operating an electronic platform in relation to lending" was introduced to the Regulated Activities Order. The activity only applies to loans where either:

- the lender is an individual; or
- the borrower is an individual and either:
  - the loan is GBP 25,000 or less; or
  - the individual is not borrowing for business reasons.

In this context, "individual" includes a partnership with 2 or 3 partners.

As most P2P platforms target individual lenders, the status of the borrower does not affect the requirement for the platform to be authorised. However, the nature of the lending does affect the regulatory regime that will apply to the platform, as more extensive rules apply to P2P platforms that facilitate consumer credit.

Firms operating P2P platforms before April 2014 were required to apply to the FCA for interim permissions to continue carrying on the activity. The FCA allotted a time window (usually 1 August to 1 November 2015) to each platform with interim permissions during which they were required to apply for full permission or lose their authorised status. Going forward, as the interim permission regime has now ended, firms wishing to operate P2P platforms will need to submit either a new authorisation application to the FCA (for firms which are unregulated and often newly established) or a variation of permission application (for firms who are currently authorised but do not hold the requisite P2P lending permissions). It is generally accepted that the regulatory regime for P2P platforms constitutes "light touch" regulation, which is in-keeping with the UK's ambitions to encourage increased responsible SME business lending and make the UK an international hub for Crowdfunding.

As discussed above, investors can also acquire debt-securities through Crowdfunding platforms: this falls into the MiFID regime for the distribution of securities, rather than the recently-created P2P regime.

A number of platforms also use a "receivables purchase" model, whereby the platform makes loans to borrowers directly, and then sells "receivables" (i.e. the right to receive amounts equal to the capital and interest payable by the borrower under the underlying loan) to investors. Provided that the borrowers are corporate entities and not consumers (which is generally the case), the receivables purchase model is currently unregulated.

### **1.3 Donations or Rewards Model (Individuals provide money to a company or project for benevolent reasons or for a non-monetary reward)**

The Donations or Rewards Model does not involve any form of financial investment or return and so it falls outside the scope of UK securities regulation.

### **1.4 Real Estate Crowdfunding / Renewables Crowdfunding**

According to the FCA's call for evidence, a recent development that was noted in the 2015 Alternative Finance Industry Report is the increasing use of Crowdfunding platforms to finance real estate. "Of the GBP 1,490m invested in business loans in 2015, GBP 609m, around 41%, was used to finance real estate lending (such as loans to purchase buy-to-let properties or bridging finance). Additionally, of the GBP 332m raised on investment-based Crowdfunding platforms in 2015, some GBP 85.7m was invested in real estate companies (which allow investors to acquire ownership of a property-asset via the purchasing of shares of a single property or a number of properties) as opposed to commercial businesses. This suggests a trend towards using both loan and investment-based Crowdfunding platforms for more fund-like investments, where businesses are set up as pooled investment vehicles rather than as trading enterprises."

### **1.5 International approach in the UK**

In their call for input, the FCA acknowledges the different approaches to the regulation of Crowdfunding that are being taken in other jurisdictions (for example, as identified in the IOSCO Crowdfunding 2015 survey responses report). The regulator confirms that whilst market context varies from country to country, it is keen to learn from other experiences to ensure that UK regulation provides appropriate levels of consumer protection. Despite that level of protection, the FCA considers their regime to provide a proportional approach which will still enable the market to develop. The FCA is actively engaged with European Authorities tasked with looking at the regulation of Crowdfunding and they intend to continue to engage in all international work streams that may have an impact on the regulation of Crowdfunding in the UK.

## **2 Recent developments regarding Crowdfunding regulation in the UK**

### **2.1 Post-implementation review of the FCA's Crowdfunding rules**

Crowdfunding investments are increasingly being afforded the same status as other, more conventional types of investments. The initial popularity of Crowdfunding as an alternative to more traditional bank financing has increased consumer awareness and understanding, and with it, the perception that Crowdfunding can be just as viable an investment option to add to existing portfolios.

Shortly after inception, the FCA recognised that Crowdfunding was a growing industry and an increasingly important source of alternative finance. In April 2014, the regulator introduced rules to regulate Crowdfunding and has been monitoring the appropriateness of

the regulatory regime, including through a review of the regime in February 2015 and most recently through the kick-off a post-implementation review which commenced in July 2016 with the FCA putting out a call for input. The regulator acknowledges that the UK market is now more established and that Crowdfunding has become a more accepted form of raising capital – as a result, it is the appropriate time to consider whether the rules need to be changed to reflect the current scale, status and risk to investors, or whether the current regime is adequate.

In December 2016, following industry feedback, the FCA published a Feedback Statement (FS16/13) providing interim feedback following its call for input. In the regulator's view, there is evidence of potential investor detriment and it intends to publish a consultation paper in the first quarter of 2017 proposing new rules. The FCA's focus will be on the loan-based market although it has concerns across both loan-based and investment-based sectors.

In relation to loan-based Crowdfunding, the FCA will consult on:

- additional rules to strengthen investor protections where there is a platform failure;
- additional requirements or restrictions on cross-investment; and
- extending the MCOB lending standards to P2P platforms where the investor/lender is not acting by way of business.

In relation to both loan and investment-based Crowdfunding, the regulator remains concerned about the quality of communications with potential investors and as a result, will consult on more prescriptive rules on the content and timing of disclosures it expects to see.

The FCA also intends to report in mid-2017 with the final conclusions of the full (rather than just interim) post-implementation review which is likely to result in additional suggested changes for the regime in the future.

## **2.2 Client money rule changes for Crowdfunding platform operators and the new P2P advice regulated activity**

On 21 March 2016, the FCA published a policy statement on changes to the FCA Handbook relating, amongst other provisions, to the segregation of client money on loan-based Crowdfunding platforms and the new regulated activity of advising on P2P agreements. The new and amended rules and guidance came into force on 21 March 2016 in relation to the client money provisions and 6 April 2016 in relation to the advice activity.

Firstly, the revised rules simplified the client money requirements for firms that operate electronic systems in relation to lending and hold money in relation to both regulated and unregulated P2P. As a result of the changes, firms that hold money in relation to both P2P and business-to-business (B2B) agreements, are entitled to elect to hold all lenders' monies in relation to this business under the FCA's client money rules if they wish to do so. Firms may then hold P2P and B2B monies together, but segregated from the firm's money, without

breaching the client money rules. The FCA decided to provide a transitional provision in relation to the requirement to submit a client money and assets return in certain specific circumstances.

Secondly, under the revised rules, the FCA applied its suitability rules to firms making personal recommendations about P2P agreements and banned commission for advice on P2P agreements given as a personal recommendation. The regulator did not apply the appropriateness test to P2P agreements sold on a non-advised basis, although the FCA reserved their position to revisit this in future. When the UK government revised the legislation to make the provision of advice to investors on loans made via P2P platforms a regulated activity, it did not require firms that already held FCA authorisation to advise on investments to have to seek additional authorisation in order to advise on P2P loans. Instead the government ensured that all firms already authorised to advise on investments were eligible to elect to have authorisation to advise on P2P loans automatically conferred upon them.

### **2.3 Operating collective investment schemes**

A key facet of loan-based Crowdfunding is the matching of multiple lenders to a single borrower with many lenders making small (micro) loans to meet a borrower's (macro) borrowing requirement. Those lenders effectively share in the risk if the borrower is unable to repay its loan. However, platforms are also increasingly developing models that provide for pooling of such risk across the lenders on a platform as a whole, meaning that each investor on the platform has some indirect exposure to the risk of other loans on the platform in which they may not themselves be invested.

This pooling and other factors may mean that some firms operating loan-based Crowdfunding platforms are also operating collective investment schemes. In January 2016, the Treasury amended secondary legislation so that firms carrying on the activity of operating an electronic system in relation to lending are not regarded as operating collective investment schemes (though they may still be Alternative Investment Funds ("AIFs") under the Alternative Investment Fund Managers Directive ("AIFMD")).

### **2.4 Revised prospectus requirements**

Although not a UK-specific development, the on-going negotiation as regards the EU Commission's proposed changes to the Prospectus Directive (2015/0268) may well have a strong effect on cross-border fund raises even if the European Parliament is successful in amending the Commission's proposal. The Commission's proposal permits Member States to impose an exemption from the requirement to produce a prospectus for domestic offers of up to EUR 10m (which was a welcome development from the current EUR 5m threshold). However, for non-domestic offers, there is a maximum raise of EUR 500k.

On 15 September 2016, the European Parliament adopted amendments which suggests that the exemption from the obligation to publish a prospectus should be revised back to the

original EUR 5m threshold with the reference to the requirements for the offer to be made in that Member State being deleted. It will be important to follow the text of this regulation as it progresses through the negotiation process to determine the like impact for the Crowdfunding industry.

## 2.5 Brexit

On 29 March 2017, the UK government triggered the process for exiting the EU. The ramifications for the cross-border development of Crowdfunding into and out of the UK will largely depend on the basis of any transitional arrangements following Brexit as well as the outcome of the negotiations on the UK/EU relationship which will determine what arrangements apply in relation to EU legislation in future once the UK has left.

A snap UK election has been called for 8 June 2017 which means that negotiations with the EU will not begin until later that month at the earliest. If there is a change of UK government, perhaps the incoming administration would want to push that date back whilst it gathers its thoughts. The European Commission currently expects that the negotiations themselves will last approximately 18 months (early June 2017 – October/November 2018). There are currently disagreements on the structure of the negotiations: the EU will only commence talks on the future overall framework of the relationship once the withdrawal agreement has been finalised whereas the UK would prefer to negotiate both in tandem given the curtailed timing.

When analysing the potential impact of Brexit on the financial services market, the following scenarios are the ones commonly discussed:

- A. full equivalence and passporting: the UK would obtain full equivalence and passporting across the full scope of the single market directives where such equivalence and passporting rights are currently available;
- B. equivalence where the provision already exists but no additional access rights are granted: the UK would become a “third country” and would obtain equivalence across the single market directives and regulations where equivalence is already established. No new access arrangements would be negotiated to compensate for the loss of passporting rights;
- C. third country agreement: the UK would become a “third country” but would not obtain equivalence across the core single market directives. No new access arrangements would be negotiated on a bilateral basis; and
- D. Bilateral agreement – these are negotiated with individual Member States to retain access where possible.

In reality, focus has centred on the second and third options – back in January, Prime Minister Theresa May made clear that the UK would not remain a member of the single market after Brexit – as a result, passporting rights will no longer be available. As regards the fourth option, in April, the European Parliament warned that any bilateral arrangement between one or several remaining member states and the UK, in the areas of EU competence,

which has not been agreed by the EU27, relating to issues included in the scope of the withdrawal agreement or impinging on the future relationship of the EU with the UK, would be in contradiction with the Treaties. This would especially be the case for any bilateral agreement or regulatory or supervisory practice (or both) that would relate, for example, to any privileged access to the internal market for UK-based financial institutions at the expense of the EU's regulatory framework.

Although it may be possible for some UK firms to continue to access EU markets under scenario 2, firms are neither relying on equivalence determinations being made nor assuming that equivalence would provide a sufficiently certain basis upon which to build a business plan. Firms are putting in place contingency plans and structuring solutions on the assumption that scenario 3 will apply. In both scenarios, the activities of UK (and possibly EU) firms will be disrupted – the extent of the disruption will depend on the way that individual businesses are structured. Clearly, given the uncertainty around equivalence determinations, firms would prefer arrangements to be negotiated that enable EU and UK firms to access each other's markets on the basis that their respective regimes are broadly consistent.

### 3 Current Regulation of Crowdfunding in the UK

#### 3.1 Regulation under the Financial Promotion Regime

The offer of shares, bonds or other securities and the provision of Crowdfunding services relating to securities and P2P loans will generally constitute a financial promotion, namely an invitation or inducement to engage in investment activity.

Much of the Crowdfunding website's contents will comprise an element of financial promotion. Accordingly, assuming the operator is FCA-authorized (or is the tied agent or appointed representative of an authorised firm), the contents of the website's financial promotions need to comply with the requirements of chapter 4 of the FCA's Conduct of Business Sourcebook to ensure that they are clear, fair and not misleading.

The FCA has also kept a close eye on the financial promotions made by Crowdfunding firms, particularly in the context of social media, on which it published specific guidance in March 2015. This guidance recognised the importance of this channel of promotion for firms, although highlighted the importance of "standalone compliance" in any communication (particularly relevant for financial promotions made through Facebook or Twitter) and the need to highlight potential risks to investors or lenders.

A financial promotion relating to non-readily realisable securities (which does not include P2P loans or listed securities) cannot be made to a retail investment audience unless the recipients of the promotion fall within certain categories (high net worth investors, sophisticated investors, advised investors or investors who will not invest more than 10% of their net worth in non-readily realisable securities). For this reason, P2P platforms have a less attritional investor membership process than securities platforms.

If the Crowdfunding entails investing in an unregulated collective investment scheme (similar to the European notion of an alternative investment fund), there is a more restrictive financial promotion regime that is often incompatible with "crowd" investing. For this reason, Crowdfunding platforms do not generally offer investments that would constitute units in an unregulated collective investment scheme.

As mentioned above, this is an area that is likely to be the subject of change during 2017 as the FCA consult following their post-implementation review.

### **3.2 Regulation of Securities Model under the Financial Services and Markets Act 2000 (FSMA)**

FSMA requires platform operators to become authorised by the FCA in order to conduct regulated activities. Conducting a regulated activity without authorisation is a criminal offence. Regulated activities associated with the Crowdfunding of securities transactions may include:

- bringing about transactions in investments issued by the party seeking funding;
- making arrangements with a view to transactions in investments (which captures referral arrangements even where a specific issuer or investment is not identified); and
- safeguarding and administering investments (custody);
- agreeing to carry on a regulated activity.

Less commonly, the platform operator could become involved in advising on securities, managing securities or dealing in securities, depending on the business proposition. Where the party seeking funding is not a trading company, platform operators may also need to consider whether they are carrying on the regulated activity of operating a collective investment scheme or managing an alternative investment fund (see below).

Seeking authorisation is a costly and time-consuming process and many platform operators are established as appointed representatives and/or tied agents of authorised firms, benefitting from their regulatory permissions. The authorised firm assumes responsibility for the regulatory compliance of its appointed representative/tied agent, usually in consideration for fees.

### **3.3 Prospectus requirements**

FSMA requires a prospectus to be published where transferable securities are offered to the public. Most Crowdfunding offers fall within an exemption for offers worth less than EUR 5 million in a period of 12 months. As part of the EU Commission's proposals for a new prospectus regime (published in November 2015), it was proposed that Member States be able to legislate to widen this exemption, to require that prospectuses only be published for offers of EUR 10 million or more provided that the offer is only made in that Member State. However

any offers with a cross-EEA border element would be restricted to EUR 500k under the proposals.

On 15 September 2016, the European Parliament resolved, on a partial vote, to adopt amendments to the Commission's proposal. Amendments to the Commission's proposal that were adopted by the European Parliament include:

- The threshold for the total consideration of offers below which the regulation does not apply has been increased to EUR 1 million (from EUR 500,000).
- Further amendments provide that member states may not require a prospectus, nor other disclosure requirements that could constitute a disproportionate or unnecessary burden, at a national level for such offers.
- The upper limit for the total consideration for offers to which member states may elect to exempt offers within their own domestic markets has been lowered to EUR 5 million (from EUR 10 million). Recital 13 clarifies that member states should be free to set out in their national law a threshold between EUR 1 million and EUR 5 million, expressed as the total consideration of the offer in the EU over a period of 12 months, from which the exemption should apply taking into account the level of domestic investor protection they deem to be appropriate.

Section 755 of the Companies Act 2006 also prohibits the offer of shares in a private limited company to the public. The involvement of the platform can be structured so as to reduce the risk of breach.

### **3.4 Regulation concerning Unregulated Collective Investment Schemes (UCISs)**

Where the profit share being offered to investors is not channelled through a standard corporate issuer/shareholder relationship (e.g. the investor receives a contractual entitlement to profits from a project), the investment may be characterised as units in a UCIS. Crowdfunding generally entails the pooling of investor contributions or the pooling of profits and/or income prior to distribution to the investor, with no investor involvement in the day-to-day management of the proposition (or project), the two key components of a "collective investment scheme".

Operating a UCIS and managing an alternative investment fund are regulated activities and must be conducted by an FCA-authorized firm. There is overlap between this regulated activity and the activity of managing an alternative investment fund (see the section on Regulation under the Alternative Investment Fund Managers Directive (AIFMD) regime below). There is potential for either the platform operator or the fund-seeking party to be a person that would conduct the regulated activity, depending on how the arrangements are structured. The promotion of UCISs is subject to greater restriction than the promotion of shares in a trading company, even when the promotion is communicated or approved by an FCA-authorized firm – for example, the platform operator needs to confirm the eligibility of investors to invest in UCISs before promoting the platform, whereas eligibility for investing

in non-readily realisable securities only needs to be determined before a direct offer of those investments is made. The potential categories of exempt funder to whom UCISs can be promoted is also narrower than for other non-readily realisable securities.

These UCIS promotion restrictions also apply to other forms of non-mainstream pooled investment, such as shares in a special purpose vehicle.

### 3.5 Regulation under the AIFMD regime

A range of measures implementing the Alternative Investment Fund Managers Directive (AIFMD) came into force in the UK from 22 July 2013, creating a new pan-European concept of "alternative investment fund" that sits alongside the existing UK regime for UCISs. Broadly, most UCISs will constitute alternative investment funds. The AIFMD has added a new layer of regulation on top of the UCIS regime. The AIFMD applies where the investment proposition involves an "alternative investment fund" (AIF), namely:

- a collective investment undertaking;
- which raises capital from a number of investors; and
- which invests in accordance with a defined investment policy for the benefit of its investors.

Most UCISs will be AIFs, but the AIFMD is also capable of applying to a body corporate that falls outside the UCIS regime. Managing an alternative investment fund is a regulated activity that also permits the firm to operate a UCIS. The AIFMD imposes a heavy regulatory burden above and beyond the UCIS regime on fund operators falling within scope, for example, the requirement to appoint an independent depositary. However, there is a light touch compliance regime for managers with total assets under management of less than EUR 100 million, which most UK-based platforms would fall into if they were managing an AIF. Under the limited compliance regime, the fund manager (e.g. the platform operator) will generally be required to become authorised as a small authorised AIFM and comply with a limited conduct of business and capital requirements regime.

The light touch regime for small AIFMs does not prohibit the marketing of AIFs to retail investors in the UK, provided the AIF is not also a UCIS.

### 3.6 Regulation under the P2P Regime

From 1 April 2014, platforms carrying out the new regulated activity of "operating an electronic platform in relation to lending" became subject to regulation by the FCA under an interim permission regime. Firms with interim permissions which failed to apply for full authorisation between August and November 2015 will have had their permissions revoked. Since April 2014, firms wishing to operate a P2P platform that have not benefitted from the interim permission regime have been required to apply for full authorisation.

Variations of the Lending Model can also lead to participants being offered units in a UCIS and/or an AIF, although platform operators generally try to avoid this because of the

associated marketing restrictions. Also note the changes introduced in January 2016 as discussed above which confirmed that firms carrying on the activity of operating an electronic system in relation to lending are not regarded as operating collective investment schemes.

The main tenets of the P2P regime (where the loan does not fall within the consumer credit regime described below) are:

- Publication of historic performance data on loans;
- Arrangements for investor protection in the event of platform failure;
- Capital adequacy requirements, based on the higher of a fixed requirement (GBP 20,000 rising to GBP 50,000) and a variable requirement relating to loan volumes;
- Client money segregation;
- Clear, fair and not misleading communications with lenders;
- An appointed representative regime (similar to the regime for securities Crowdfunding).

### 3.7 Regulation of Payment Services

The transmission of funds between the investor and the crowd funded business may involve the platform operator providing "credit transfer" or "money remittance" services under the Payment Services Regulations 2009 (as amended) (PSRs) implementing the Payment Services Directive in the UK. A platform operator will require separate FCA authorisation if it is conducting payment services.

Many operators have historically relied on the exemption for 'commercial agents' under the PSRs on the basis that they have authorisation to negotiate or conclude contracts on behalf of the funder and the fund seeker. However, in some member states the commercial agent exemption has been applied very narrowly, to exclude situations where the agent acts for both the payer and the payee. The difference in the application of the exemption was picked up by the European Commission as part of its proposed revision to the Payment Services Directive (PSD2). The recitals to finalised PSD2 state that e-commerce market places and platforms have unfairly relied on being the agent of both consumer and merchant, rather than of one or the other, to remain outside the scope of PSD. As a result, PSD2 narrows this exemption so that it only applies if the commercial agent is authorised to negotiate or conclude the sale or purchase of goods or services on behalf of only the payer or only the payee.

Where agents act on behalf of both payer and payee, they should be excluded only if they do not at any time enter into possession or control of client funds. The UK government has said that it expects that a number of 'platform' business models which match buyers and sellers for goods and services are unlikely to benefit from the revised exemption and so may now fall within the regulatory scope of the PSD2.

However, the FCA published its Consultation Paper on the UK implementation of PSD2 on 13 April 2017, which contains draft amendments to the FCA's Perimeter Guidance manual (PERG) and contains further proposed guidance on this point. The draft amended PERG text

states that the FCA would not generally expect operators of loan or investment based Crowdfunding platforms transferring funds between participants as part of that activity to be providing payment services as a regular occupation or business activity, which would mean that separate FCA-authorisation from a payment services perspective would not be required. The FCA consultation is open until 8 June 2017, after which the FCA will consider feedback received and finalise the PERG text.

### 3.8 Anti-money Laundering

The FCA expects all authorised firms, including those operating both loan-based and investment-based Crowdfunding platforms, to have systems and controls in place to mitigate the risk that they are misused for the purposes of financial crime. Such measures will depend on a firm's own assessment so the nature and extent of risk will vary. Financial crime risk could exist on either the lender/borrower or investor/investment side of the transaction. Institutional investors and other investors lending by way of business to consumers or commercial financing will also need to comply with the Money Laundering Regulations 2007 (these will be repealed from 26 June 2017 and new regulations will apply in order to implement the Fourth Money Laundering directive, "4MLD"). The FCA's financial crime guide provides guidance on their overall financial crime expectations and the Joint Money Laundering Steering Group provides guidance on complying with the Money Laundering Regulations.

### 3.9 Data Protection

On 25 May 2018, the General Data Protection Regulation (GDPR) will replace the UK's Data Protection Act 1998 (and other laws enacted across all EU member states to implement the EU's Data Protection Directive 1995). The GDPR will apply to all platform operators processing personal data in the context of an establishment in the EU, and to those which are not established in the EU but which offer services to data subjects (i.e. individual borrowers or investors) in the EU.

Platform operators – as data controllers – must process personal data in accordance with the requirements of the GDPR, which include a requirement to:

- make certain privacy information available to data subjects (usually in the form of a privacy policy);
- keep comprehensive records of processing activities;
- enter into robust contractual arrangements with third parties processing personal data on their behalf (for example, hosting providers);
- take appropriate technical and organisational measures to keep personal data secure (relative to the potential risk); and
- not transfer personal data outside the EEA without ensuring "appropriate safeguards" (for example, by incorporating the European Commission's standard contractual clauses).

Under the GDPR, the UK's data protection authority (the ICO) and all other EU data protection authorities will have the power to issue fines of up to the higher of 4% of worldwide turnover or EUR 20,000,000 for breaches of certain requirements (including the restriction on transferring personal data outside the EEA). There is a lower tier of fine (the higher of 2% of worldwide turnover or EUR 10,000,000) for breaches not falling within the higher tier. The GDPR also includes a right to compensation for data subjects, which, together with a new concept of the “representation of data subjects”, could create a significant new class action threat.

## 4 Regulatory barriers for Crowdfunding crossing borders

### 4.1 Applicable law

FSMA requires platform operators to become authorised by the FCA in order to conduct regulated activities in the UK. Conducting a regulated activity in the UK without authorisation is a criminal offence. As mentioned above, regulated activities associated with the Crowdfunding of securities transactions usually include:

- bringing about transactions in investments issued by the party seeking funding;
- making arrangements with a view to transactions in investments (which captures referral arrangements even where a specific issuer or investment is not identified); and
- safeguarding and administering investments (custody);
- agreeing to carry on a regulated activity; and
- in some circumstances, advising on securities.

In relation to P2P, platforms will be carrying out the new regulated activity of "operating an electronic platform in relation to lending". Other regimes, both EU and UK derived, may also apply in addition or in place of the above, as discussed in other sections of this overview.

FSMA provides that the requirement to be authorised only applies in relation to activities that are carried on 'in the UK'. In many cases, it will be quite straightforward to identify where an activity is carried on; but when there is a cross-border element, for example because a client is outside the UK or because some other element of the activity happens outside the UK, the question may arise as to where the activity is carried on. Even with a cross-border element a person may still be carrying on an activity 'in the UK'.

FSMA takes this further by extending the meaning that 'in the UK' would ordinarily have by setting out five additional cases. FSMA states that, in these five cases, a person who is carrying on a regulated activity but who would not otherwise be regarded as carrying on the activity in the UK is, for the purposes of the regulatory regime, to be regarded as carrying on the activity in the United Kingdom. The three of most relevance here are:

- the first case which is where a UK-based person carries on a regulated activity in another EEA state in exercise of rights under one of the Single Market Directives;

- the third case which is where a regulated activity is carried on by a UK-based person and the day-to-day management of the activity is the responsibility of an establishment in the UK; and
- the fourth case which is where a regulated activity is carried on by a person who is not based in the UK but is carried on from an establishment in the UK.

The application of the third and fourth cases depend on how the activities carried on from the UK establishment are set up and operated.

## 4.2 Inbound

### 4.2.1 Crowdfunding platform from another EU country addresses investors in the UK

#### 4.2.1.1 Regulatory barriers for platforms (licence/other requirements)

##### (1) UK regulatory authorisation

As set out above, FSMA provides that the requirement to be authorised only applies in relation to activities that are carried on 'in the UK'. The key question then in determining whether UK regulatory authorisation is required will be whether a regulated activity is taking place in the UK. Where a platform based in the UK is providing services to UK borrowers and investors, any regulated activities will clearly be carried out in the UK. However, where there is a cross-border element to a platform's activities, for example because an investor is outside the UK or because an investee company is outside the UK, it may be more difficult to identify where the activity is going on. The factors which need to be considered in determining whether the activity is carried on in the UK are set out at 4.1 above.

If the platform is carrying on a regulated activity in the UK then it will be required to obtain FCA authorisation as an authorised person. The scope of the FCA authorisation required will depend on the regulated activities being carried on by the platform. As a result, the conditions which will need to be satisfied in order to obtain FCA authorisation will vary as between the different regimes, as will the on-going compliance and conduct of business obligations which the platforms will be subject to on an on-going basis as authorised firms.

##### (2) EU Passporting

Platforms based in Member States other than the UK and authorised under MiFID may be able to exercise passport rights under MiFID and provide the services for which it is authorised in all Member States across the EU without having to obtain authorisation on a country by country basis. Platforms wishing to take advantage of such passporting rights would need to notify their home state regulator of the exercise of their passport rights, which in turn would notify the "host" state (which may be the UK's FCA). In order to be within MiFID scope, a firm needs to be carrying on MiFID services/activities in relation to MiFID financial instruments, and not exempt. Further details of the MiFID requirements are set out at 4.4 below.

The Payment Services Directive (as updated by PSD2 as set out above) and applicable passport rights may also be relevant to the extent a firm is carrying on applicable services.

### **(3) Financial promotion requirements**

The UK has imposed restrictions on financial promotions such that persons must not (in the course of business) communicate an invitation or inducement to engage in investment activity (i.e. a "financial promotion") unless either: (a) the person communicating the promotion is an authorised person; (b) the communication has been approved by an authorised person; or (c) the communication falls within an exemption under the FSMA (Financial Promotion) Order 2001 (the Financial Promotion Order). Section 21(3) of FSMA states that, in the case of a communication originating outside the UK, the financial promotion restriction in section 21(1) applies only if it is capable of having an effect in the United Kingdom. In this respect, it is irrelevant whether the communication has an effect provided it is capable of doing so.

However, an exemption for communications to overseas recipients is set out at article 12 of the Financial Promotion Order, which prevents the financial promotion restriction from applying to communications which are not directed at persons in the UK, either where the financial promotion is made to a person who receives it outside the UK, or is directed at persons who are outside the UK. The exemption applies whether or not the financial promotion is made from the UK. However, as an exception to this, if it is an unsolicited real time financial promotion, it must be made from a place outside the UK and be for the purposes of a business carried on entirely outside the UK.

Additional rules apply such that if a financial promotion is sent or communicated from a place outside the UK, it will be conclusive proof that it is not directed at persons in the UK (even if it ends up being received by a person in the UK) if: (a) it is not referred to in or directly accessible from another communication (for example, an advertisement in a UK newspaper or a UK website) which is itself made to or directed at UK persons by the overseas person who is directing it; and (b) proper systems and procedures have been set up to prevent UK persons (other than those to whom the promotion could legally have been made to, e.g. because they fall within an exemption) from engaging in the investment activity to which the financial promotion relates with the overseas person.

Even where the person making the communication is within the UK, there can still be conclusive proof that it is only directed to persons outside the UK if it is accompanied by an indication that: (a) it is directed only at persons outside the UK; and (b) should not be acted on by persons in the UK. The FCA has stated that one factor it will take into account in assessing whether a communication in a website is directed at persons inside the UK is whether the website is registered with a UK search engine.

Where communications by persons in another EEA State are made to or directed at persons in the UK, account must also be taken of the effect of any relevant EU Directives

which may prevent the United Kingdom from imposing restrictions on incoming financial promotions. These should be looked at on a case by case basis.

#### **4.2.1.2 Regulatory barriers for foreign companies / projects (prospectus regulation/other requirements)**

Companies seeking to raise finance by issuing equity or debt securities are responsible for complying with all relevant legislation. In addition to complying with the disclosure and financial promotion requirements and restrictions in the FCA Handbook, it is for the firms operating Crowdfunding platforms, and the companies seeking finance through them, to satisfy themselves that they are meeting any requirement to publish a prospectus (or satisfy themselves that an exemption is available).

#### **4.2.2 Crowdfunding platform from another EU country addresses companies/projects in the UK**

Subject to the point below, the same considerations will broadly apply to foreign platforms promoting and providing services to UK-based companies or projects, similarly to where the platforms are targeting investors (and as detailed above). One point to note in these circumstances is that the fundraising entities will likely fall outside scope of the consumer credit regime where they are seeking to raise finance through loans, provided that they are set up as a corporate entity or partnership (which will generally be the case and may be a condition imposed by the platform).

Contravening the prohibition in FSMA of dealing (and other activities) in transferable securities without approved prospectus is a criminal offence. In addition, under the UK corporate regime, the Companies Act 2006 prohibits the offer of shares in a private limited company to the public, although it is possible to structure the involvement of the platform in such a way as to minimise any potential breach. Some platforms will provide assistance to companies seeking to raise finance in complying with relevant corporate obligations, although this will need to be considered in detail depending on the particular circumstances of any fundraise.

### **4.3 Outbound**

#### **4.3.1 Crowdfunding platform from the UK addresses investors in another EU country**

##### **4.3.1.1 Regulatory barriers for platforms (licence/other requirements)**

In this situation a UK platform would be addressing foreign (EU-based) investors. The UK regulator would be concerned with platforms doing business within the UK and so would be responsible for supervising and overseeing only the business activities which took place within the UK. Where a platform is targeting non-UK investors only then provided that the fundraising activity is also taking place outside the UK (i.e. the companies or projects seeking to fundraise through the platform are non-UK based), then UK conduct of business rules would not apply to these activities.

The UK licensing requirements would similarly not apply if no regulated activities are being carried on in the UK. In determining whether this would be the case the FCA would consider the factors set out at 4.1 above.

UK platforms should carry out due diligence on the regulatory regime of any EU country in which they are targeting investors or investment companies/ fundraising opportunities before launch, in order to determine which local licensing requirements and conduct of business obligations they will be subject to under the local regulatory regime.

As mentioned above, UK platforms seeking to passport into other EU jurisdictions under their MiFID platform would not need to obtain additional licences, but may be subject to additional conduct of business rules under the host state's regulatory regime.

UK platforms should be aware of EU-based regulation including in relation to data protection, AML and consumer protection, which set out common standards which UK platforms will be expected to comply with under local implementing legislation.

#### **4.3.1.2 Regulatory barriers for foreign companies/projects (prospectus regulation/other requirements)**

In circumstances where EU companies raise money through a UK platform (i.e. authorised and regulated here) which targets EU investors, regard should be had to both section 4.3.1 above and 4.3.2 below.

#### **4.3.2 Crowdfunding platform from the UK to companies/projects in another EU country**

Similarly to UK platforms addressing investors in another EU country, UK platforms targeting fundraising companies or projects in another EU country would need to keep in mind the same licensing and conduct of business set out at 4.3(a) above.

If the UK platform is seeking UK investors or lenders in relation to the foreign fundraising opportunity, then the UK licensing regime and UK conduct of business requirements described above would apply, such that the platform would need to be FCA-authorised and comply with the UK regulatory regime in the operation of the platform.

If the companies seeking to raise funds through the platform are based outside the UK, then UK corporate law would not apply to the raising of capital by the company. However, as the company will likely raise equity-based or debt-based securities as part of the fundraising round, the EU prospectus requirements (discussed at 3.3 above) will apply unless the minimum threshold is not exceeded, such that an exemption will be available. The foreign company or project would also need to comply with any local prospectus rules under the law of its home country (which would similarly be derived from the EU Prospectus Regulation, although may be subject to local law variations).

## 4.4 Impact of EU regulation

### 4.4.1 AIFMD

The AIFMD (2011/61/EU) introduced a harmonised regulatory framework across the EU for EU-established managers of AIFs. It entered into force on 21 July 2011 and had to be implemented by member states, including the UK, by 22 July 2013. A transitional period ended on 22 July 2014. The Directive was implemented by a combination of HM Treasury statutory instruments and FCA Handbook rules. The AIFMD regime mainly affects equity-based Crowdfunding platforms,

Managing an AIF is a regulated activity that also permits the firm to operate a UCIS as discussed above. The AIFMD imposes a heavy regulatory burden above and beyond the UCIS regime on fund operators falling within scope, for example, the requirement to appoint an independent depositary. However, there is a light touch compliance regime for managers with total assets under management of less than EUR 100 million.

Most UK-based platforms would fall into if they were managing an AIF. Under the limited compliance regime, the fund manager (e.g. the platform operator) will generally be required to become authorised as a small authorised AIFM and comply with a limited conduct of business and capital requirements regime. The light touch regime for small AIFMs does not prohibit the marketing of AIFs to retail investors in the UK, provided the AIF is not also a UCIS.

### 4.4.2 MiFID/MiFID II

The Markets in Financial Instruments Directive (2004/39/EC) (MiFID) came into force in the UK on 1 November 2007 and was implemented in the UK by amendments to UK legislation and by amending the rules in the FCA Handbook to accommodate its requirements.

Where applicable, MiFID would impose duties on the Crowdfunding platform in its capacity as investment intermediary. To be within MiFID scope, a firm needs to be carrying on MiFID services/activities in relation to MiFID financial instruments, and not exempt. The benefit to a platform of being within the scope of MiFID is that it has a passport to carry on the services/activities for which it is authorised throughout the EU without any additional authorization being required, in accordance with a single set of rules.

MiFID applies in relation to the list of 'financial instruments' set out at Section C of Annex 1 to the Directive. The financial instruments most likely to be used in Crowdfunding are transferable securities e.g. equities or 'mini-bonds', though others such as units in collective investment undertakings would be possible. Where financial instruments are involved, the question arises which services/activities a platform is carrying out. This needs to be assessed case-by-case as business models can vary and the definitions were not designed with these business models in mind. However, the activity most likely to be carried out by mainstream Crowdfunding platforms in the absence of regulatory constraints is the reception and transmission of orders: the platform receives orders from investors and transmits them to the

issuer or another third party intermediary. Additionally the activities of execution of client orders and, in some instances, investment advice are also relevant.

The MiFID II Directive (2014/65/EU) and the Markets in Financial Instruments Regulation (Regulation 600/2014) will repeal and recast MiFID. Whilst MiFID II broadens the scope of MiFID to cover new financial products, such as structured deposits and emissions allowances, the revised regime does not affect the scope of financial instruments and services/activities that are relevant to Crowdfunding.

It is worth remembering that investors can also acquire debt-securities through Crowdfunding platforms (not just equities) and that these fall into the MiFID regime for the distribution of securities, rather than the recently-created P2P regime.

The key impact of MiFID (and MiFID II from July 2018) is whether securities in question are those that fall within the MiFID definition of 'financial instrument' and, if so, the ability of the platform in question to passport their activities across Europe. There is substantial overlap between the UK regulatory regime and MiFID as you would expect but each platform needs to identify and confirm that their UK regulated activities fall within the scope of MiFID and can therefore be passported.

#### 4.4.3 Prospectus Directive

As a result of implementing the Prospectus Directive in the UK, FSMA requires a prospectus to be published where transferable securities are offered to the public. Contravening the prohibition in FSMA of dealing (and other activities) in transferable securities without approved prospectus) is a criminal offence. In addition, under the UK corporate regime, the Companies Act 2006 prohibits the offer of shares in a private limited company to the public. It is possible to structure the involvement of the platform so as to reduce the risk of breach.

#### 4.4.4 PSD/PSD II

The Payment Services Directive (2007/64/EC) (PSD), which was adopted at European level in November 2007, harmonised the regulatory regime for payment services across the EU. The PSD had to be implemented in member states by 1 November 2009. The PSD was implemented in the UK primarily by the PSRs which came into force on 2 March 2009.

PSD2 was published in the Official Journal of the EU on 23 December 2015, and came into force on 12 January 2016. The deadline for member states to transpose PSD2 into their national laws and regulations is 13 January 2018. PSD2 updates the current framework on payment services, extending its scope to payment service providers that were previously unregulated, and improving the transparency and security of payment services.

The transmission of funds between the investor and the crowd funded business may involve the platform operator providing payment services which require authorisation. As mentioned above, platforms have historically relied on the "commercial agent" exemption but this is being substantially narrowed as a result of PSD2 with the resulting expectation being

that many platforms will no longer be able to rely on it. The result will be the need for authorisation by the FCA in the UK unless an alternative structure can be found for the handling of payments although this is likely to create additional regulatory considerations. As a result, the changes being brought in by PSD2 (and the resulting UK legislation to transpose it) may be problematic for platform operators.

As noted at 3.7 above, the FCA has proposed amendments to its Perimeter Guidance handbook (PERG) which would clarify that loan and investment based Crowdfunding platforms transferring funds between participants as part of that activity would not be considered to be providing payment services as a regular occupation or business activity, such that separate authorisation would not be required. The PERG guidance is not yet final and will be subject to feedback on the FCA's consultation which closes on 8 June 2017, after which any draft guidance will be formally adopted.

#### 4.5 Summary

On 23 June 2016, the EU referendum took place and the people of the UK voted to leave the EU. Until exit negotiations are concluded, the UK remains a full member of the EU and all the rights and obligations of EU membership remain in force. During this period the UK government will continue to negotiate, implement and apply EU legislation. The outcome of these negotiations will determine what arrangements apply in relation to EU legislation in future once the UK has left the EU and this will obviously have ramifications for the 'impact of EU legislation' section outlined above.

## 5 Lessons learned from the UK regulation for a possible harmonised European Crowdfunding regulation

### 5.1 Role model

- "Light touch" regulation for Crowdfunding platforms overall and in comparison to some other European jurisdictions.
- Securities-based Crowdfunding is able to operate under the existing regulatory regime, as opposed to requiring platforms to comply with additional industry-specific requirements.
- New regulated activity was introduced in 2014 for loan-based Crowdfunding and an initial interim permission regime was established (although most platforms have now completed or are now in the process of converting to full authorisation) with an authorisation process which was less costly and the subject of less intensive scrutiny than the full authorisation route.
- Exemption for firms operating an electronic systems in relation to lending from operating collective investment schemes (note though they may still be Alternative Investment Funds (AIFs) under the Alternative Investment Fund Managers Directive (AIFMD)).

- Balance achieved between removing barriers to businesses whilst securing an appropriate standard of protection for investors (e.g. through mandatory arrangements in the event of platform failure, capital adequacy requirements, client money segregation and requiring communications with customers to be clear, fair and not misleading).

## 5.2 Aspects that should be avoided

- No "light touch" regime available for the financial promotion of Crowdfunding opportunities through the medium of social media, which does not naturally lend itself to extensive risk warnings.
- Lack of exemptions for Consumer Credit Lending, e.g. where a business is lending to an individual, resulting in the platform falling within the scope of the more onerous consumer credit regime.
- Increasing perception of Crowdfunding platforms as comparative to alternative investment funds.

## 6 Conclusion

The UK financial services regulatory environment is clearly favourable for Crowdfunding generally and there are no barriers to entry that particularly affect the ability for platforms to raise finance, particularly through debt securities or P2P loans. The UK market has grown rapidly and as a result, a number of changes and revisions will be made to the regime over the next 12-18 months. Whilst the focus of the FCA will be ensuring that investor protections are appropriate, the regulator's aim is to continue to ensure that the market in Crowdfunding develops in a sustainable fashion, allowing competitive forces to operate in the interests of consumers.

## 7 Summary – Crowdfunding Regulation

| Country  | United Kingdom  |
|--|---|
| <p><b>Summary</b></p> <p><b>Recent developments in Crowdfunding regulation</b></p> | <ul style="list-style-type: none"> <li>• The FCA is currently in the process of concluding a post-implementation review of its Crowdfunding rules which commenced in July 2016. The interim report published at the end of 2016 focused principally on loan-based Crowdfunding and how investor protections could be strengthened but also considered the content and timing of disclosures in investor communications for both loan and investment-based Crowdfunding. Further changes are likely when the review concludes mid-2017.</li> <li>• From 21 March 2016, advising on P2P agreements became a regulated activity and from 6 April 2016, the FCA's client money rules were simplified for firms that operate electronic systems in relation to lending and hold money in relation to both regulated and unregulated P2P.</li> <li>• In January 2016, HM Treasury amended secondary legislation so that firms carrying on the activity of operating an electronic system in relation to lending (i.e. operators of loan-based Crowdfunding platforms) are not regarded as operating collective investment schemes (though they may still be AIFs under the AIFMD).</li> <li>• On 29 March 2017, the UK government triggered the process for exiting the EU. The ramifications for the cross-border development of Crowdfunding into and out of the UK will largely depend on the basis of any transitional arrangements following Brexit as well as the outcome of the negotiations on the UK/EU relationship which will determine what arrangements apply in relation to EU legislation in future once the UK has left.</li> </ul> |
| <p><b>Current / planned Crowdfunding regulation</b></p>                            |   |
| <p><b>General regulation</b></p>   | <p>Securities Model generally entails conducting regulated securities business</p> <ul style="list-style-type: none"> <li>• FCA authorisation required</li> </ul> <p>For the Lending Model, the regulated activity of "operating an electronic platform in relation to lending" was introduced in April 2014</p> <ul style="list-style-type: none"> <li>• FCA authorisation required.</li> </ul> <p>Donations/Rewards Model is not subject to financial services regulation.</p> <p>For the Securities Model, FCA rules restrict the promotion of "non-readily realisable securities" to certain categories of retail investor.</p>   |

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|---|---|
| <p><b>Prospectus requirement</b></p>        | <p>Prospectus requirement for offering of transferable securities (such as shares):</p> <ul style="list-style-type: none"> <li>• Threshold: EUR 5 million per issuer within 12 months. Proposed EU Commission changes will permit Member States to impose an exemption from the requirement to produce a prospectus for domestic offers of up to EUR 10 million, and for non-domestic offers, a maximum raise of EUR 500,000 – although this may be subject to change given the European Parliament's current agreed position.</li> </ul> <p>For the Securities Model, where profit share is not channelled through a standard corporate issuer/shareholder relationship, investment may be characterised as collective investment scheme.</p>  |
| <p><b>AIFMD-regulation</b></p>              | <p>For the Securities Model, to the extent that an investment amounts to a collective investment scheme:</p> <ul style="list-style-type: none"> <li>• categories of investors to which unregulated collective investment schemes are narrower than for other non-readily realisable securities.</li> </ul> <p>Crowdfunding structure could constitute an AIF if it includes profit share arrangements otherwise than in a commercial company.</p> <p>Light-touch regime for managers with management assets under EUR 100 million:</p> <ul style="list-style-type: none"> <li>• FCA authorisation/registration and reporting requirements, but Directive marketing restrictions not applied.</li> </ul>   |
| <p><b>Payment service regulation</b></p>    | <ul style="list-style-type: none"> <li>• The transmission of funds between the investor and the crowd funded business may involve the platform operator providing "credit transfer" or "money remittance" services under the Payment Services Regulations 2009 (as amended) (PSRs) implementing the Payment Services Directive in the UK. A platform operator will require separate FCA authorisation if it is conducting payment services.</li> <li>• Historically operators have relied on the exemption for 'commercial agents' but this is unlikely to be possible post 13 January 2018 when PSD2 take effect. The FCA has published draft guidance on this point which, although not yet final, may mean that loan and investment based Crowdfunding platforms would not be considered to be providing payment services as a regular occupation or business activity, such that separate authorisation would not be required.</li> </ul> |
| <p><b>Further possible requirements</b></p> | <p>Money Laundering Regulations 2007:</p> <ul style="list-style-type: none"> <li>• platform operator has to verify the identity of clients.</li> </ul> <p>Note that the Money Laundering Regulations 2007 will be repealed from 26 June 2017 and new regulations will apply in order to implement 4MLD.</p> <p>From 25 May 2018, the General Data Protection Regulation will replace the UK's existing Data Protection Act 1998 and will impose wide-ranging requirements on platform operators in relation to their processing of</p>  |

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|                            | personal data. The consequences of breaching the GDPR can be significant.   |
| <b>Regulatory barriers</b> |   |
| <b>Inbound</b>             | <p><b>Foreign Crowdfunding platform addresses UK investors:</b></p> <ul style="list-style-type: none"> <li>Financial Services and Markets Act 2000: Platforms carrying on a "regulated activity" in the UK will be required to obtain FCA authorisation as an "authorised person". The scope of the FCA authorisation required will depend on the regulated activities being carried on by the platform. Platforms based in Member States other than the UK and authorised under MiFID may be able to exercise passport rights under MiFID without having to obtain authorisation on a country by country basis. Financial promotions directed at UK recipients will also likely be subject to additional conduct of business obligations under the UK financial promotion regime.</li> </ul> <p><b>Crowdfunding platform from another EU country addresses companies/projects in the UK:</b></p> <ul style="list-style-type: none"> <li>Companies seeking to raise finance through issuing debt or equity securities must satisfy themselves that they are meeting any requirement to publish a prospectus (or fall within an available exemption). Contravening the prohibition in FSMA of dealing (and other activities) in transferable securities without approved prospectus is a criminal offence. The Companies Act 2006 also prohibits the offer of shares in a private limited company to the public.</li> </ul>        |
| <b>Outbound</b>            | <p><b>UK Crowdfunding platform addresses foreign investors:</b></p> <ul style="list-style-type: none"> <li>UK platforms targeting non-UK investors only would not be subject to UK licensing requirements or conduct of business rules provided that the fundraising activity is also taking place outside the UK (i.e. the companies or projects seeking to fundraise through the platform are non-UK based). The FCA would consider a number of different factors in determining that this would be the case. UK platforms are likely to be subject to local licensing and conduct of business requirements (depending on the scope of their activities) and so should carry out due diligence on the regulatory regime of any EU country in which they are targeting investors or investment companies/ fundraising opportunities prior to launch.</li> <li>As mentioned above, UK platforms seeking to passport into other EU jurisdictions under their MiFID platform would not need to obtain additional licences, but may be subject to additional conduct of business rules under the host state's regulatory regime. UK platforms should be aware of EU-based regulation including in relation to data protection, AML and consumer protection, which set out common standards which UK platforms will be expected to comply with under local implementing legislation. Similarly, companies seeking to raise</li> </ul> |

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|---------------------------------------|---|
|                                       | <p>finance should be aware of any local requirements to issue a prospectus (or conditions which must be met in order to issue shares to the public).</p>  |
| <p><b>Impact of EU regulation</b></p> |   |
| <p><b>Prospectus regulations</b></p>  | <p>As a result of implementing the Prospectus Directive in the UK, FSMA requires a prospectus to be published where transferable securities are offered to the public. Contravening the prohibition in FSMA of dealing (and other activities) in transferable securities without approved prospectus) is a criminal offence. In addition, under the UK corporate regime, the Companies Act 2006 prohibits the offer of shares in a private limited company to the public. It is possible to structure the involvement of the platform so as to reduce the risk of breach.</p> |
| <p><b>AIFM-Directive</b></p>          | <p>Crowdfunding structure could constitute an AIF if it includes profit share arrangements otherwise than in a commercial company.</p> <p>Light-touch regime for managers with management assets under EUR 100 million which most UK-based platforms fall within as applicable:</p> <ul style="list-style-type: none"> <li>• FCA authorisation/registration and reporting requirements, but Directive marketing restrictions not applied.</li> </ul>  |
| <p><b>MiFID / MiFID II</b></p>        | <p>The key impact of MiFID (and MiFID II from July 2018) is whether securities in question are those that fall within the MiFID definition of 'financial instrument' and, if so, the ability of the platform in question to passport their activities across Europe. There is substantial overlap between the UK regulatory regime and MiFID as you would expect but each platform needs to identify and confirm that their UK regulated activities fall within the scope of MiFID and can therefore be passported.</p>   |
| <p><b>PSD / PSD II</b></p>            | <p>The reduction in scope of the 'commercial agent' exemption under PSD2 is likely to mean that many platform operators will need to be authorised to provide payments services on the basis that the transmission of funds between the investor and the crowd funded business can involve the platform operator providing "credit transfer" or "money remittance" services.</p>  |

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# United States

## 1 Recent developments in the market of Crowdfunding in the US

Since April 2012, when the JOBS Act was passed by bi-partisan Congressional approval and signed into law by the then President of the United States, there has been significant regulatory and commercial developments in United States regarding Crowdfunding in all of its many forms. Under the JOBS Act, there are three provisions which are relevant to the emerging Crowdfunding industry

- Title II – General Solicitation (also known as “506(c)”)
- Title III – Retail Crowdfunding and
- Title IV – Regulation A+.

Since the earliest days of Federal securities in the United States, the presumption has been that you may not offer securities to the public using general means of marketing or advertising without submitting full disclosure documentation to the Securities and Exchange Commission (the “SEC”), the chief U.S. securities regulator, for its review and comment. This process is generally known as “*Going Public*”. Although there has always been the notion that a company may nonetheless sell securities to investors with whom they nonetheless maintain a pre-existing and substantive relationship with prior to the financing, this is an exemption to registration with the SEC. This historic approach has been in place since 1933. In the United States though it is further complicated by all 50 states also having securities regimes which must be followed as well, known as the “*Blue Sky*” laws.

The various JOBS Act provisions have changed this conventional thinking to modernize the sale of securities in the context of the internet. The private placement exemption that many financings have relied on prior to the JOBS Act is Regulation D, Rule 506(b), which memorializes the rule about raising unlimited capital without the need to register with the SEC so long as you only sell to high net worth investors also known as “*Accredited Investors*”. Prior to Regulation D and the reasonably well-defined rules on accreditation the entrepreneur had to maintain a pre-existing and substantive relationship with all of its investors. What constitutes a pre-existing and substantive relationship has not been well-defined and been up to the subjective interpretation of regulators and lawyers. Regulation D sought to eliminate that arbitrariness and impose specific income or net worth requirements. The basic rationale was that if investors were financially substantial to make an investment and bear the risk of complete loss of their capital then the SEC need not intervene. The JOBS Act provisions seek to build upon that legacy and broaden the ability of entrepreneurs to raise capital online without going through a registration process with the SEC, or in the case of Regulation A+, where you still must make a submission to the SEC, make it easier and less costly.

Well before there was Crowdfunding, there has been a very active “*friends and family*” source of capital in the United States for entrepreneurs. By some measures, friends and

family may invest more in start-ups, including local bars and restaurants, than venture capitalists and angel networks. Even though, friends and family often back entrepreneurs there is an inherent inefficiency with having to contact everyone individually and share your vision of what you would like to do with the money that is being requested. Along comes online fundraising and all of the efficiencies that come with generally soliciting funds from a larger community, including the entrepreneurs social network, and doing it in a central location (i.e. the company's website or the CFP) and the entire capital formation process can be more effective. No different than the offline structuring of start-ups, the early Crowdfunding deals were largely equity investments.

The exemption of Title II – 506(c) of the JOBS Act, which has been in effect since 2013 has been the most actively used of the new Crowdfunding provisions. Since inception, thousands of issuers have raised billions of dollars of both debt and equity under this provision. While Title II offerings have gained in market acceptance as a way of proceeding to raise capital, the use of Title II – 506(c) versus the more traditional 506(b) exemption is still substantially less. Through the first two years of the new provisions, Title II – 506(c) was utilized approximately 10% of the time. For capital raising of investment funds, even fewer. It should be noted however that the trend lines suggest an increasing use however of general solicitation as some of the professional uncertainty around the new exemption is reduced. Use of online intermediaries, which is discretionary in this context, appears to be present in less than 30% of those financings.

Unlike other provisions of the JOBS Act, Title III – Regulation Crowdfunding for securities-based Crowdfunding had only slightly more than six months of results by the end of 2016, since this particular provision only went into effect May 16. Regulation Crowdfunding prescribes rules that permit securities-based Crowdfunding by private companies without registering the offering with the Securities and Exchange Commission (SEC) pursuant to new Section 4(a)(6) (15 U.S.C.S. § 77d) of the Securities Act of 1933, as amended (the “*Securities Act*”). Consequently, pursuant to this provision, this statutorily permitted form of Crowdfunding is only permissible in the United States, although there are versions of Regulation Crowdfunding in other jurisdictions. During the limited six-month initial period of Regulation Crowdfunding, there has been a slow but steady increase in all aspects of this emerging industry. On the day of implementation, there were fewer than 10 Financial Industry Regulatory Authority (FINRA) approved Crowdfunding portals and nearly 25 entrepreneurial campaigns posted to those same sites for investor consideration. By the end of 2016, there were 21 FINRA approved portals operating in the market with 186 entrepreneurs seeking to raise capital pursuant to these new rules. Of these 186 entrepreneurial campaigns, 79 have raised sufficient funds to close on at least the minimum amount of their proposed funding requirements. In the aggregate, these campaigns will raise nearly USD 17 million. While the aggregate amounts remain small, the initial metrics seem to be trending in an encouraging direction and well above any expectations for Regulation Crowdfunding's first six months. For a further discussion of Regulation Crowdfunding, see An Overview of the SEC's Crowdfunding Regulations.

Notable Transactions Of the 186 campaigns that sought to raise capital in 2016, three of such campaigns achieved the maximum permissible amount of USD 1 million under Regulation Crowdfunding: • Beta Bionics (Biotech) - July 28, 2016 - 954 Investors • Hops & Grain (Restaurant) - August 15, 2016 - 535 Investors • Legion M (Hollywood Studio) - August 9, 2016 - 2,882 Investors Legion M raised its USD 1 million on Wefunder and claims to be the first fan-owned entertainment company, working with top Hollywood creatives to make movies, TV, VR, and more. Beta Bionics, a Massachusetts-based diabetes medical device benefits corporation, also raised the maximum permissible through Wefunder, as did Hops & Grain as well.

After 18 months of activity, Title IV – Regulation A+ is still finding its footing. While there has been significant interest in this exemption, and nearly 100 submissions to the SEC, the issuers that have availed themselves of this provision have generally struggled to raise the funds that they had sought. In general, the REITs have had the greatest success using Title IV/Regulation A+. Fundrise has completed two eREIT fundings utilizing this provision. There are also a few other operating companies that have successfully used Regulation A+ and raised funding but typically less than they had hoped. Entrepreneurs need to realize simply because the rules permit issuers to raise up to US\$50mm doesn't mean that they are going to. While some of these issuers have also elected to work with broker-dealers, most have not. In both cases though, securing funding has been difficult. Also, an issuer may elect to work with an online platform or offer the securities on their own. One lesson issuers have learned is that just because an audience of potential investors have indicated that they are interested in investing in your company doesn't necessarily follow that they will actually invest. Professionals that promote Regulation A+ offerings often site that one of the benefits of the new rule is that an issuer may publicly solicit interest prior to undertaking the cost and burden of preparing the offering disclosure that must be filed with the SEC – so called “test the waters” (*TTW*). While *TTW* is a great idea in concept, investors don't seem to act on their initial interest after waiting 60/90 days for the actual documentation to be finalized. Despite the less than positive initial experience, Regulation A+ is a good development and commercial parties will make adjustments and identify the best use cases for this Crowdfunding provision as well. Part of the problem would seem to be that a large majority of the issuers are pre-revenue and might be better off with a Title III Regulation Crowdfunding offering first to determine if they really have an interested affinity group of potential investors.

Like with all new securities programs, these provisions will take time to be understood by entrepreneurs, funding platforms, broker-dealers and finance professionals, and until they are, Crowdfunding will develop slowly and cautiously and that is all for the good.

### 1.1 The Equity Model

Equity generally meaning the buying and holding of shares of stock (common, preferred) in an entrepreneurial opportunity in further anticipation of income from dividends and capital gains.

## 1.2 The Lending Model

Like its equity counterpart, debt-based lending represents a compelling opportunity for small business owners seeking financial assistance outside traditional lending institutions, including banks and credit unions. Debt Crowdfunding or “crowd lending,” as it is sometimes called, provides non-dilutive business financing on payment terms requested by the founder and funded by the crowd. In debt Crowdfunding you are also investing in a security of the company (namely a debt instrument of some type) where your goal is to loan your money to the company with a fixed repayment term and the company pays you a specified interest rate during the term of the loan. There are a variety of types of debt instruments that are available to investors. Some allow for conversion into common shares so that investors have the potential upside growth in the company while they receive steady interest payments, while others are straight interest yielding securities. There are secured and unsecured debt instruments. All of these factors plus the risk associated with the invest influence the interest rate and conversion rights (if any). Debt Crowdfunding is attractive for those investors who desire a fixed return, making it easier for financial planning purposes. Traditionally debt investments that are secured against the company assets are seen as less risky and hence provide a lower interest rate yield than the unsecured instruments. It should be noted that even though debt investments are perceived to be lower risk, the CFPs will still be required to do the same level of due diligence as they would for equity type investments. They will also have to assess the company’s ability to meet the repayment schedule to the investors.

### 1.2.1 Lending Laws and Lender Registration / Licensing

The extension of consumer credit in the United States is regulated at both the federal and state levels. An operator that conducts a nationwide business therefore may be subject to regulation under various laws and, potentially, by multiple jurisdictions. Generally, an internet-based consumer lending program will utilize a funding bank. The funding bank will be subject to both federal and state regulation but may, in certain instances, be able to rely upon federal law to preempt state laws that would otherwise apply. As discussed below, federal preemption will be particularly important to the Funding Bank in connection with state usury laws.

Even within start-up life, the most common source of debt financing for start-ups often isn't a commercial lending institution, but family and friends. It makes sense. People with whom you have close relationships know you are reliable and competent, so they are the logical first ask. Under the historic pre-JOBS Act rules however these financings were done without proper disclosure and often done haphazardly and in a noncompliant manner. While the most recognized version of small business lending done in an online environment, otherwise known as Peer to Peer and now known as Marketplace Lending, would appear to have many of the obvious elements of Crowdfunding, it is generally speaking not done pursuant to the various JOBS Act provisions but actually under the more rigorous process undertaken with a full registration statement and review by the SEC. There are many regulatory complexities to the debt lending models pursued by LendingClub, Prosper and OnDeck which really make them

a separate category than what we are tasked with discussing in this paper. Those securities are registered instruments and not exempt from the SEC rules and regulations. Other forms of Crowdfunding debt lending do exist though throughout the online financing space, particularly, in the real estate space.

### 1.3 The Donations and Rewards Model

#### 1.3.1 Donation Crowdfunding

This is the most popular type of Crowdfunding at this time. Donation Crowdfunding has two types: rewards Crowdfunding and charity Crowdfunding.

#### 1.3.2 Rewards Crowdfunding

Rewards-based Crowdfunding is where contributions are exchanged for current or future of goods or services. Individuals or companies who launch campaigns may compensate contributors with something like a t-shirt, a copy of whatever they're building or even just a thank you. Rewards-based Crowdfunding is perhaps the most prolific form of Crowdfunding currently taking place in the US. Appropriate for: Projects in the arts (movies, art, music, etc.), companies looking to test markets, charitable groups and causes

#### 1.3.3 Charity Crowdfunding

Donation Crowdfunding takes place when an individual, company or organization accepts charitable donations.

### 1.4 Real Estate Crowdfunding

Real estate Crowdfunding involves the pooling of funds by multiple investors in a real estate project. There are two main investment types to choose from:

#### A. Equity investments

Investors make investments in commercial or residential properties and in exchange, they hold an equity stake in the property. Each investor shares in a portion of the rental income the property generates.

#### B. Debt investments

Specifically, this means investing in a mortgage loan associated with a particular property. As the loan is repaid, the investor receives a share of the interest.

Between the two, equity investments offer the potential for bigger returns because the profitability of debt investments is limited by the loan's interest rate. On the other hand, equity investments are riskier and they typically require a longer holding period.

Real estate Crowdfunding platforms can vary widely in terms of how investments are structured and that affects what an investor owns. Some platforms create a separated limited liability company (LLC) for each equity investment opportunity. The LLC holds an interest in

the entity that owns the real estate at the center of the investment. Investors own shares in the LLC, giving them limited liability as well as certain tax benefits associated with pass-through entities. With debt and certain preferred equity investments, the investment is made in payment dependent notes belonging to the platform's subsidiaries. The notes are tied to the performance of a real estate loan or project investment made by an individual subsidiary. Investors have ownership in the note itself.

### 1.5 International approach

While the domestic market for Crowdfunding in the United States continues to accelerate, investors and entrepreneurs should recognize that Crowdfunding in the broadest sense is a truly worldwide phenomenon. The United Kingdom in many ways has led the industry but China, Southeast Asia and many European platforms are also gaining increased traction.

## 2 Recent developments regarding Crowdfunding regulation in United States

Unlike other provisions of the JOBS Act, Title III – Regulation Crowdfunding for securities-based Crowdfunding had only slightly more than six months of results by the end of 2016, since this particular provision only went into effect May 16. Regulation Crowdfunding prescribes rules that permit securities-based Crowdfunding by private companies without registering the offering with the SEC. During the limited six-month initial period of Regulation Crowdfunding, there has been a slow but steady increase in all aspects of this emerging industry. On the day of implementation, there were fewer than 10 Financial Industry Regulatory Authority (FINRA) approved Crowdfunding portals and nearly 25 entrepreneurial campaigns posted to those same sites for investor consideration. By the end of 2016, there were 21 FINRA approved portals operating in the market with 186 entrepreneurs seeking to raise capital pursuant to these new rules.

There have been no meaningful developments in the other JOBS Act related Crowdfunding provisions. They have been operating under their statutes since enactment without meaningful changes or problems. While Title II – General Solicitation continues to facilitate capital formation for entrepreneurs, Title IV – Regulation A+ has had less commercial success so far. Like with all new programs, Title IV – Regulation A+ will take a while for entrepreneurs and bankers to figure out how to properly use the new rules to better raise capital.

## 3 Current Regulation of Crowdfunding in the United States

### 3.1 Statutory Provisions in the market of Crowdfunding in the United States

As mentioned previously, there are several statutory provisions that accommodate for different forms of securities based Crowdfunding in the United States and knowing the differences is critically important in order to ensure proper compliance.

### 3.1.1 Title II – General Solicitation (also known as “506(c)”)

Unlike the basic notion underlying a private placement, like a 506(b) financing, and avoiding a registration statement with the SEC to conduct a full public offering, Title II or 506 (c), permits an entrepreneur to raise an unlimited amount of capital from investors and to conduct a general solicitation so long as the resulting investors are only Accredited Investors. For purposes of 506(c), the entrepreneur must take “*reasonable steps to verify*” that the investors are actually accredited. The safe harbor to that rule means getting from all such investors either an accountants, lawyers or financial advisors attestation of the investors accredited investor status. This differs from 506(b) in that the investor themselves were permitted to self-certify their status as an accredited investor. Assuming that the entrepreneur is prepared to verify, then they may publicly solicit and advertise its offering to identify potential investors, either online or off. So while the entrepreneur may only ultimately accept funding from an accredited investor, the offering may be made public for all to see. This is a meaningful departure from what was permissible previously. There is no limit on how much may be raised under a 506(c) offering, there is no specific disclosure that the entrepreneur, including financial statements, must be provided to investors and any domestic or foreign company may utilize this financing provision. Keep in mind though that just because the United States has elected to change its approach to general solicitation of investors doesn’t mean that any such solicitation is compliant with other international jurisdictions securities laws. We caution to make sure that you properly analyze such rules and consult appropriate international counsel.

### 3.1.2 Title III – Retail Crowdfunding

Regulation Crowdfunding enables any U.S. incorporated entity to raise up to USD 1 million in any twelve-month rolling period, but it must post the campaign for investment consideration on a Crowdfunding platform (CFP). CFPs have discretion to determine which campaigns they elect to post through their portals. CFPs have numerous statutory duties and obligations, including performing background, anti-money laundering, and Office of Foreign Assets Control checks. A CFP must establish proper and thorough onboarding procedures for potential investors as well as provide education materials for their online community and potential investors. The education should encompass information about the Crowdfunding industry and investing generally, risks associated with private illiquid securities, and the particulars of each campaign. All U.S. citizens may invest; however, there are investment caps on the amount that all investors may invest in Regulation Crowdfunding opportunities in each twelve-month rolling period as well. Although Regulation Crowdfunding financings are considered exempt from registration under the Securities Act, these campaigns may be marketed both offline and online, subject to very specific rules and SEC guidance.

The entrepreneur / issuer has the responsibility to prepare and submit a disclosure document to the SEC, referred to as the Form C prior to posting the entrepreneur’s campaign “live” on the CFP (see below section 3.3.1.2).

### 3.1.2.1 Bad Actors

Regulation Crowdfunding disqualifies a bad actor from utilizing this exemption. The events which make a bad actor under Regulation Crowdfunding are similar to the disqualifying events with respect to Rule 506 (17 C.F.R. § 230.506) of Regulation D under the Securities Act, and include:

- Certain criminal convictions
- Court injunctions and restraining orders
- Regulatory agency orders
- SEC disciplinary, cease-and-desist, and stop orders
- Suspension or expulsion from membership in self-regulatory organizations.

### 3.1.2.2 Financial Statements

The extent of the financial statements required to be included in a Form C are based on the amount offered and sold in reliance on Regulation Crowdfunding within the preceding 12-month period:

Issuers offering USD 100,000 or less: Financial statements of the issuer and certain information from the issuer's federal income tax returns, both certified by the principal executive officer, are required. If, however, financial statements of the issuer are available that have either been reviewed or audited by an independent public accountant, the issuer must provide those financial statements instead and will not need to include the information reported on the federal income tax returns or the certification of the principal executive officer.

Issuers offering more than USD 100,000 but not more than USD 500,000: Financial statements reviewed by an independent public accountant are required. If audited financial statements are available, however, the issuer must provide those financial statements instead and will not need to include the reviewed financial statements.

Issuers offering more than USD 500,000:

- For first-time Regulation Crowdfunding issuers: Financial statements reviewed by an independent public accountant are required, unless financial statements of the issuer are available that have been audited by an independent auditor.
- Issuers that have previously sold securities in reliance on Regulation Crowdfunding: Financial statements audited by an independent public accountant are required.

### 3.1.2.3 Notices

In accordance with the Title III statute, an entrepreneur conducting a Regulation Crowdfunding campaign may publicly disseminate a notice advising potential investors of the terms of its offering as described in the Form C. The notice may only include a limited number of permissible terms. An issuer may not advertise the terms of a Regulation Crowdfunding

offering except in a notice that directs investors to the intermediary's platform (see below section 3.4.2).

### 3.1.3 Title IV – Regulation A+

Regulation A+ was adopted by the SEC under Section 3(b) of the Securities Act in 1936 as an exemption from registration for small issues. The annual offering limit permitted under this exemption had been raised several times and was changed to USD 5 million by 1992. Nevertheless, the exemption has been used infrequently over the past two decades. The JOBS Act amended Section 3(b) of the Securities Act of 1933 directing the SEC to adopt rules exempting from the registration requirements of the Securities Act offerings of up to USD 50 million per year. As discussed in more detail below, the final rules provide an exemption for U.S. and Canadian companies that are not required to file reports under the Exchange Act to raise up to USD 50 million in a 12-month period. The final rules create two tiers:

- A. *Tier 1* for smaller offerings raising up to USD 20 million in any 12-month period, and
- B. *Tier 2* for offerings raising up to USD 50 million.

The new rules also make the exemption available, subject to limitations on the amount, for the sale of securities by existing stockholders. The new rules modernize the existing framework under Regulation A+ by, among other things, requiring that disclosure documents be filed on EDGAR, allowing an issuer to make a confidential submission with the SEC, permitting certain test-the-waters communications, and disqualifying bad actors. The final rules impose different disclosure requirements for Tier 1 and Tier 2 offerings. Tier 1 offerings will be subject to both SEC and state blue sky pre-sale review. Tier 2 offerings will be subject to SEC, but not state blue sky pre-sale review; however, investors in a Tier 2 offering will be subject to investment limits (except when securities are sold to accredited investors or are listed on a national securities exchange) and Tier 2 issuers will be required to comply with periodic filing requirements, which include a requirement to file current reports upon the occurrence of certain events, semi-annual reports and annual reports. The final rules provide a means for an issuer in a Tier 2 offering to concurrently list a class of securities on a national exchange through a short-form Form 8-A, without requiring the filing of a separate registration statement on Form 10.

#### 3.1.3.1 Eligible Issuers

The new Regulation A+ exemption, both Tier 1 and Tier 2, will be available to issuers organized in and having their principal place of business in the United States or Canada. The following issuers will be “ineligible” to offer or sell securities under Regulation A:

- an issuer that is an SEC-reporting company;
- a blank check company;

- any investment company registered or required to be registered under the Investment Company Act of 1940 (this includes business development companies); and
- any entity issuing fractional undivided interests in oil or gas rights, or similar interests in other mineral rights.

The exemption also is not available to: (1) issuers that have not filed with the SEC the ongoing reports required by Regulation A+ during the two years immediately preceding the filing of a new offering statement, (2) issuers that have had their registration revoked pursuant to an Exchange Act Section 12(j) order that was entered into within five years before the filing of the offering statement and certain bad actors.

### 3.1.3.2 Eligible Securities

The securities that may be offered under Regulation A+ are limited to equity securities, including warrants, debt securities and debt securities convertible into or exchangeable into equity interests, including any guarantees of such securities. The final rule excludes asset-backed securities.

### 3.1.3.3 Offering Limitations

As noted above, an issuer can choose a Tier 1 or a Tier 2 offering. Under Tier 1, an issuer may offer and sell up to USD 20 million in a 12-month period, of which up to USD 6 million may constitute secondary sales (except as noted below). Under Tier 2, an issuer may offer and sell up to USD 50 million in a 12-month period, of which up to USD 15 million may constitute secondary sales (except as noted below). The final rules set out an approach for calculating the offering limit in the case of convertible or exchangeable securities. In the issuer's initial Regulation A+ offering and any Regulation A+-exempt offering in the 12 months following that offering price of the particular offering, the selling securityholder component cannot exceed 30% of the aggregate offering. In addition, the final rules distinguish between sales by affiliates and sales by non-affiliates. Following the expiration of the first year following an issuer's initial qualification of a Regulation A+ offering statement, the limit on secondary sales falls away for non-affiliates only. Notably, the final rule eliminates the current prohibition on resales by affiliates in reliance on the exemption unless the issuer had net income from continuing operations in at least one of the last two years.

Regulation A+ did not contain a limit on the amount of securities that may be purchased by an investor. However, to address potential investor protection concerns, the final rules impose an investment limit for Tier 2 offerings. The investment limit will not apply to accredited investors and will not apply if the securities are to be listed on a national securities exchange at the consummation of the offering; otherwise a nonaccredited natural person is subject to an investment limit and must limit purchases to no more than 10% of the greater of the investor's annual income and net worth, determined as provided in Rule 501 of Regulation D (for non-accredited, non-natural persons, the 10% limit is based on annual revenues and net assets). Investors must be notified of the investment limitations, and may

rely on a representation of compliance with the investment limitation from the investor, unless the issuer knew at the time of sale that any such representation is untrue.

## 3.2 Licensing (Broker-Dealer, Investment Advisor and Debt Lending)

### 3.2.1 Equity Model / Lending Model

#### 3.2.1.1 Broker-Dealer

A central element of the investor protection scheme established by the federal securities laws is the comprehensive framework for the registration and regulation of persons engaged in the business of buying and selling securities. The Securities Exchange Act of 1934 (the “Exchange Act”) is the primary federal legislation governing “*brokers*” and “*dealers*” in securities. With certain exceptions, Section 15 of the Exchange Act requires registration with the SEC.

The Exchange Act defines a “*broker*” and a “*dealer*” differently. However, most rules do not distinguish between a broker or a dealer in their application. The underlying policy for the broker-dealer registration requirement and associated regulatory framework is to provide important safeguards to investors. The Exchange Act’s regulatory scheme is designed to ensure that all registered broker-dealers and their associated persons satisfy professional standards, have adequate capital, treat their customers fairly, and provide adequate disclosures to investors. Section 15(a)(1) compels registration of most broker-dealers by prohibiting the use by any broker or dealer of the mails or any means or instrumentality of interstate commerce to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers’ acceptances, or commercial bills) unless such broker or dealer is registered with the SEC in accordance with the Exchange Act. The registration requirement extends not just to entities, but also to natural persons (other than natural persons who are associated with a broker-dealer).

In the SEC’s no-action guidance and enforcement actions, receiving commissions or other transaction-related compensation is one of the determinative factors in deciding whether a person is a “broker” subject to the registration requirements under the Exchange Act. Transaction-related compensation refers to compensation based, directly or indirectly, on the size, value or completion of any securities transactions. The receipt of transaction-based compensation often indicates that a person is engaged in the business of effecting transactions in securities. As a policy consideration, transaction related compensation can induce high pressure sales tactics and other problems of investor protection often associated with unregulated and unsupervised brokerage activities. Absent an exemption, an entity that receives commissions or other transaction-related compensation in connection with securities-based activities generally would be viewed as a broker-dealer.

The rationale for this position is summarized by the SEC as follows: Persons who receive transaction-based compensation generally have to register as broker-dealers under the

Exchange Act because, among other reasons, registration helps to ensure that persons with a “salesman’s stake” in a securities transaction operate in a manner consistent with customer protection standards governing broker-dealers and their associated persons, such as sales practice rules. That not only mandates registration of the individual who directly takes a customer’s order for a securities transaction, but also requires registration of any other person who acts as a broker with respect to that order, such as the employer of the registered representative or any other person in a position to direct or influence the registered representative’s securities activities. Courts have found that receipt of transaction-based compensation in connection with securities transactions alone – without the presence of other factors – may not be sufficient to be considered engaging in the business of effecting transactions in securities. Receiving transaction-related compensation, however, is not the only factor that the SEC has considered in its decision to bring enforcement actions.

### 3.2.1.2 Investment Advisor

The SEC regulates investment advisers, primarily under the Investment Advisers Act of 1940 (the "Advisers Act"), and the rules adopted under that statute (the "Rules"). One of the central elements of the regulatory program is the requirement that a person or firm meeting the definition of "investment adviser" under the Advisers Act register with the Commission, unless exempt or prohibited from registration. Generally only larger advisers that have USD 25 million or more of assets under management or that provide advice to investment company clients are permitted to register with the Commission. Smaller advisers register under state law with state securities authorities.

Subject to certain limited exclusions discussed below, Section 202(a)(11) of the Advisers Act generally defines an "*investment adviser*" as any person or firm that: (1) for compensation; (2) is engaged in the business of; (3) providing advice, making recommendations, issuing reports, or furnishing analyses on securities, either directly or through publications. A person or firm must satisfy all three elements to be regulated under the Advisers Act.

The Division construes these elements broadly. For example, with respect to "compensation," the receipt of any economic benefit suffices. To be deemed compensation, a fee need not be separate from other fees charged, it need not be designated as an advisory fee, and it need not be received directly from a client. With respect to the "business" element, an investment advisory business need not be the person's or firm's sole or principal business activity. Rather, this element is satisfied under any of the following circumstances: the person or firm holds himself or itself out as an investment adviser or as providing investment advice; the person or firm receives separate or additional compensation for providing advice about securities; or the person or firm typically provides advice about specific securities or specific categories of securities. Finally, a person or firm satisfies the "advice about securities" element if the advice or reports relate to securities. The Division has stated that providing one or more of the following also could satisfy this element: advice about market trends; advice in the form of statistical or historical data (unless the data is no more than an objective report of facts on a non-selective basis); advice about the selection of an investment adviser; advice concerning

the advantages of investing in securities instead of other types of investments; and a list of securities from which a client can choose, even if the adviser does not make specific recommendations from the list. An employee of an SEC-registered investment adviser does not need to register separately, so long as all of the employee's investment advisory activities are within the scope of his employment.

### 3.2.2 Donations or Rewards Model

Although the donations and rewards model of Crowdfunding is not regulated by any securities regulatory agency, the Federal Trade Commission and many state consumer protection agencies have taken a more active approach to protecting consumers.

### 3.3 Exemptions from licensing requirement

Section 202(a)(11)(A)-(E) of the Advisers Act expressly excludes certain persons or firms from the definition of an investment adviser. These persons or firms need not register under, and generally are not regulated by, the Advisers Act. Excluded are:

- Domestic banks (defined in Section 202(a)(2) of the Advisers Act) and bank holding companies (defined in the Bank Holding Company Act of 1956). Savings and loan institutions, federal savings banks, foreign banks, and credit unions do not fall within this exclusion.
- Lawyers, accountants, engineers, and teachers if their performance of advisory services is solely incidental to their professions.
- Brokers and dealers if their performance of advisory services is solely incidental to the conduct of their business as brokers and dealers, and they do not receive any special compensation for their advisory services. This exclusion is not available to a registered representative acting as a financial planner outside the scope of his employment with the broker employer.
- Publishers of bona fide newspapers, news magazines, and business or financial publications of general and regular circulation. Under a decision of the United States Supreme Court, to enable a publisher to qualify for this exclusion, a publication must satisfy three elements: (1) the publication must offer only impersonal advice, i.e., advice not tailored to the individual needs of a specific client, group of clients, or portfolio; (2) the publication must be "bona fide," containing disinterested commentary and analysis rather than promotional material disseminated by someone touting particular securities, advertised lists of stocks "sure to go up," or information distributed as an incident to personalized investment services; and (3) the publication must be of general and regular circulation rather than issued from time to time in response to episodic market activity or events affecting the securities industry. See *Lowe v. Securities and Exchange Commission*, 472 U.S. 181 (1985).
- Persons and firms whose advice, analyses, or reports are related only to securities that are direct obligations of, or obligations guaranteed by, the United States, or

by certain U.S. government-sponsored corporations designated by the Secretary of the Treasury (e.g., FNMA, GNMA).

In addition to these exclusions, the Advisers Act gives the Commission the authority to exclude, by order, other persons and firms not within the intent of the definition of investment adviser. Any person or firm seeking such an order should refer to Rules 0-4 and 0-5 under the Advisers Act and Investment Advisers Act Release No. 969 (April 30, 1985).

Unfortunately, there isn't a clear cut, one size fits all answer to whether or not Crowdfunding platforms need to be absolutely licensed to be either a broker-dealer or a registered investment advisor. Clearly, it is a statement of the obvious that having any license is more likely to provide comfort to a regulator and provide the CFP with practical cover in avoiding further regulatory scrutiny. While this isn't a technical answer it nonetheless is an important business decision. A knowledgeable regulators will look at the specific activity of the CFP to determine what licensing is actually necessary and required. Less experienced regulators or more aggressive regulators will simply be uncomfortable with a completely unlicensed CFP and look more carefully to find fault in the analysis as to why there isn't some form of license in place. Additionally, CFPs need to recognize that even an appropriately unlicensed CFP may experience a higher degree of skepticism from a potential source of capital (and their counsel) to fund their activity (same in an M&A context as well).

### **3.4 Disclosure Documentation Requirements**

#### **3.4.1 Equity Model / Lending Model**

##### **3.4.1.1 Disclosure under Title II – General Solicitation**

Under Title II – General Solicitation, the entrepreneur does not have any regulatory prescribed disclosure requirements, although all securities offerings must comply with the general anti-fraud laws protecting investors.

##### **3.4.1.2 Disclosure under Title III – Retail Crowdfunding**

Title III – Retail Crowdfunding, as described above, requires the preparation and submission with the SEC of a Form C disclosure document. The Form C must be made available to all investors for their review. The entrepreneur/issuer has the responsibility to prepare and submit a disclosure document to the SEC, referred to as the Form C prior to posting the entrepreneur's campaign "live" on the CFP. The Form C, which doesn't have to be prepared by specialized securities counsel (although in our considered view, one ought to review the Form C to ensure compliance with the rules and reduce legal liability for potential securities law violations), is a relatively detailed offering statement that includes specified information, including:

- Name, legal status, physical address, and website of the issuer

- Certain information with respect to the issuer’s directors, officers, and persons who are beneficial owners of 20% or more of the issuer’s outstanding voting equity securities, calculated on the basis of voting power
- Description of the business and anticipated business plan of the issuer
- Current number of employees of the issuer
- Risk factors, which should be tailored to the issuer’s business and the offering
- Target offering amount and the deadline to reach such amount
- Whether the issuer will accept oversubscriptions and, if so, how they will be treated
- Use of proceeds
- Description of the process for completion of the transaction or cancellation of an investment commitment and the process for reconfirming investment commitments in the event of a material change of information
- Offering price of the securities (or the method for determining such price)
- Description of the ownership and capital structure of the issuer
- Certain information relating to the intermediary, including any financial interest in the transaction
- Description of the material terms of any indebtedness of the issuer
- Description of exempt securities offerings conducted within the prior three years
- Description of certain related-party transactions
- Discussion of the issuer’s financial condition, including, to the extent material a discussion of the issuer’s liquidity, capital resources, and historical results of operations (covering the period for which financial statements are provided, as discussed below)
- Certain disqualification events with respect to the issuer and other covered persons
- Location on the issuer’s website, and time of availability of its ongoing annual reports under Regulation Crowdfunding, as well as any failure to comply with ongoing reporting requirements
- Any other material information necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading

#### 3.4.1.3 Disclosure under Title IV – Regulation A+

Title IV, Regulation A+ requires a complete disclosure document to be prepared and submitted to the SEC for its review and comments. The disclosure has many of the same elements listed for a Title III Crowdfunding, although much more extensive. The offering process for either Regulation A-Plus Tier 1 or Tier 2 offerings centers on the electronic filing with the SEC of an “Offering Statement” on Form 1-A. The key part of the Offering Statement is an “Offering Circular,” a narrative disclosure document. Except for solicitation communications, discussed below, no offer of securities may be made until the Offering Statement is filed. Thereafter, oral offers may be made, as well as written offers by means of

solicitation communications meeting certain conditions, or a “Preliminary Offering Circular,” described further below. However, no sales of securities may be made until the issuer’s Offering Statement has been “qualified” by the SEC. Key elements of the offering process are summarized further below.

### **(1) Solicitation of Interest (“Testing the Waters”)**

At any time before the qualification of an Offering Statement, including before the non-public submission or public filing of the Offering Statement, an issuer or any person authorized to act on behalf of the issuer may solicit interest in a potential offering. Solicitation materials are made subject to the antifraud provisions of the federal securities law, and certain conditions apply. The communications must state that no money or other consideration is being solicited, and if sent in response, will not be accepted, and also that no offer to buy the securities will be accepted until the Offering Statement is qualified. The communication must also state that a person’s indication of interest involves no obligation or commitment of any kind. When used after the Offering Statement is publicly filed, the communication must either include the Preliminary Offering Circular or state from whom the most recent version of the Preliminary Offering Circular may be obtained, including contact information. This requirement may be satisfied by providing the uniform resource locator (URL) where the Preliminary Offering Circular, or the Offering Statement itself, may be obtained. The communication may include a means by which a person may indicate interest in the potential offering.

### **(2) The Offering Statement**

Issuers must electronically file an Offering Statement with the SEC through the EDGAR System. The Offering Statement content is prescribed by Form 1-A under the Securities Act, and consists of three parts. Part I serves as a notice of certain basic information about the issuer and the offering, and helps confirm the availability of the exemption. Part II is the Offering Circular, a narrative disclosure document, which includes financial statements as required. Part III is comprised of required exhibits. Importantly, an issuer whose securities have not previously been sold pursuant to a Regulation A offering or an effective registration statement under the Securities Act may submit a draft Offering Statement for non-public review by the SEC staff before public filing. Draft Offering Statements must also be submitted electronically through EDGAR. Provision for submission of draft Offering Statements is intended to allow a preliminary assessment of content and identification of staff concerns that could delay or prevent qualification of the offering when publicly filed.

### **(3) Financial Statement Requirements**

Financial statements for Tier 1 and Tier 2 issuers include a balance sheet and related financial statements for the previous two fiscal years (or such shorter period as the issuer may have been in existence), which are dated not more than nine months before the date of non-public submission, filing, or qualification, with the most recent annual or interim balance

sheet not older than nine months. Where interim financial statements are necessary, they must cover a period of at least six months. The financial statements of Tier 2 issuers must be audited in accordance with U.S. GAAP or the standards of the Public Company Accounting Oversight Board.

#### **(4) The Offering Circular and Preliminary Offering Circular**

Issuers in Regulation A-Plus offerings have always been required to utilize a structured disclosure document, the Offering Circular, containing information specified by Form 1-A. That requirement is preserved for offerings of either Tier under Section 3(b)(2) of the Securities Act. As with prospectuses in a registered offering, the Offering Circular for Regulation A offerings is the core of the Offering Statement filed with the SEC. The Offering Circular covers numerous categories of information about the issuer and the offering, and more closely aligns Regulation A disclosure with the smaller reporting company disclosure requirements for registered offerings, but with some specifically scaled elements. Also, for Tier 2 offerings, issuers are required to include audited financial statements.

After the Offering Statement is filed, but prior to its qualification by the SEC, issuers may offer the securities utilizing a Preliminary Offering Circular. The document must be identified as a Preliminary Offering Circular and include a prescribed legend highlighted by prominent type or otherwise stating, among other things, that the securities may not be sold, nor may offers to buy be accepted, before the Offering Statement filed with the SEC is qualified. The Preliminary Offering Circular must contain substantially the information required in the Offering Circular by Form 1-A, although certain pricing and related information may be omitted. It is filed with the SEC as part of the Offering Statement. Issuers that offer to prospective purchasers in reliance on the delivery of a Preliminary Offering Circular must, not later than two business days after completion of a sale, provide the purchasers with a copy of the final Offering Circular, or a notice containing the URL where the final Offering Circular or the Offering Statement in which the final Offering Statement is contained, may be obtained.

#### **3.4.2 Donations or Rewards Model**

Subject to the general anti-fraud advertising and marketing rules to protect consumers in the United States, there aren't securities rules or regulations in place to govern donations and rewards Crowdfunding.

### **3.5 Advertisement**

#### **3.5.1 Title II – General Solicitation**

Title II Offerings permit the general solicitation of investors through general marketing and advertising.

#### **3.5.2 Title III – Retail Crowdfunding**

In accordance with the Title III statute, an entrepreneur conducting a Regulation Crowdfunding campaign may publicly disseminate a notice advising potential investors of the

terms of its offering as described in the Form C. The notice may only include a limited number of permissible terms. An issuer may not advertise the terms of a Regulation Crowdfunding offering except in a notice that directs investors to the intermediary's platform and includes no more than the following information:

- A statement that the entrepreneur is conducting an offering pursuant to Section 4(a)(6) of the Securities Act, the name of the intermediary through which the offering is being conducted, and a link directing the potential investor to the intermediary's platform
- The terms of the offering, which mean the amount of securities offered, the nature of the securities, the price of the securities, and the closing date of the offering period
- Factual information about the legal identity and business location of the entrepreneur, limited to the name of the issuer, the address, phone number, and website of the issuer, the e-mail address of a representative of the issuer, and a brief description of the business of the issuer

Although advertising the terms of the offering outside of the CFP's platform is limited to a brief notice, an issuer may communicate with investors and potential investors about the terms of the offering through communication channels provided on the CFP's platform. An entrepreneur must identify itself as the issuer and persons acting on behalf of the issuer must identify their affiliation with the issuer in all communications on the intermediary's platform. An issuer is allowed to compensate others to promote its Crowdfunding offerings through communication channels provided by a CFP, but only if the issuer takes reasonable steps to ensure that the promoter clearly discloses the compensation with each communication. The SEC's guidance on this point, through its published CD&Is (Compliance and Disclosure Interpretations), enables an entrepreneur to advertise on social media in a more meaningful manner arguably than the original statute might have contemplated. See Questions 204.01 – 205.01 of the SEC's Crowdfunding CD&Is (May 13, 2016), available at <https://www.sec.gov/divisions/corpfin/guidance/reg-Crowdfunding-interps.htm>. Clarification on this point with the SEC staff has also facilitated greater communications with investors and additional financing in larger amounts. Keep in mind that any communication, marketing or otherwise, for an entrepreneur/issuer in the context of a securities transaction remains subject to the broad anti-fraud rules.

However, issuers need to realize that in order to conduct a successful campaign, they must already have social currency, meaning that Practical guidance at they must already have an affinity group of loyal followers. The data suggests that unless an issuer has a couple of thousand online contacts (Facebook friends and/or LinkedIn contacts) it will have difficulty raising even USD 100,000. On the other hand, if the issuer has a social network closer to 10,000 contacts, then depending upon how actively engaged they are with the issuer's opportunity, the offering may raise anywhere from a couple of hundred thousand dollars up to the Regulation Crowdfunding maximum. In addition to the entrepreneur's social network,

the use of a high-quality video to explain the offering and the business is equally critical to the financial success of the offering. So far, there have been an average of nearly 300 investors in each financing successfully closed.

So in essence, Regulation Crowdfunding allows an entrepreneur to make a semi-public solicitation to investors and have the transaction still be considered a private placement. For established securities lawyers, this will no doubt be difficult to reconcile. Call it the “publicification” of the private market, in a similar manner to Title II, which enables an issuer to conduct a general solicitation of investors, so long as only accredited investors participate in those financings and reasonable steps have been taken to verify their accredited status.

### **3.5.3 Title IV – Regulation A+**

At any time before the qualification of an Offering Statement, including before the non-public submission or public filing of the Offering Statement, an issuer or any person authorized to act on behalf of the issuer may solicit interest in a potential offering. Solicitation materials are made subject to the antifraud provisions of the federal securities law, and certain conditions apply. The communications must state that no money or other consideration is being solicited, and if sent in response, will not be accepted, and also that no offer to buy the securities will be accepted until the Offering Statement is qualified. The communication must also state that a person’s indication of interest involves no obligation or commitment of any kind. When used after the Offering Statement is publicly filed, the communication must either include the Preliminary Offering Circular or state from whom the most recent version of the Preliminary Offering Circular may be obtained, including contact information. This requirement may be satisfied by providing the uniform resource locator (URL) where the Preliminary Offering Circular, or the Offering Statement itself, may be obtained. The communication may include a means by which a person may indicate interest in the potential offering.

## **3.6 Permissible Compensation of Crowdfunding Platforms**

### **3.6.1 Title II – General Solicitation**

A General Solicitation offering doesn’t need to be conducted through an online platform or a registered broker dealer. An entrepreneur may conduct such offering on their own, pursuant to a self-directed financing. They may not pay compensation to themselves or their management, directly or indirectly, for the successful raising of such capital. Payment of any transaction-based compensation would require broker-dealer registration. If those entrepreneurs elect nonetheless to conduct their offering through an online platform which are not themselves so licensed either, many such online platforms arrange for the securities that are being purchased by their online crowd of investors to purchase those securities through a separate entity, often a limited liability entity, commonly referred to as a special purpose vehicle (SPV). The advantage of the SPV is that it enables an affiliate of the platform to act as the ongoing general partner of that SPV. As the general partner, like with any investment partnership, the general partner may be compensated for such activities on an ongoing basis with management fees and participation in the future upside of such investment opportunity (i.e. Performance Based Compensation). Performance Based Compensation if

structured properly ought to be exempt from broker-dealer regulations. In addition to the structure on compensation, there are other broker-dealer guidelines that need to be complied with as well.

### **3.6.2 Title III, Retail Crowdfunding**

A funding platform that is either a licensed Crowdfunding intermediary or a broker-dealer is entitled to receive transaction based compensation (i.e. a commission). There is ongoing discussion with FINRA about non-cash based forms of compensation which is not identical in nature to the securities received by the investors. A funding platform may not have ownership of securities in the entrepreneur prior to the proposed financing.

### **3.6.3 Title IV, Regulation A+**

The entrepreneur would only be permitted to work directly with a registered broker-dealer in order to facilitate its financing and to pay a commission.

## **3.7 Other financial regulation**

### **3.7.1 Secondary Trading**

Each of the JOBS Act Crowdfunding provisions focuses on the initial sale of securities and the raising of capital by the entrepreneur, although the investors ultimately are looking for some kind of liquidity event. Unless a CFP is properly registered with FINRA to conduct secondary market transfers of securities and receive remuneration to be able to do so, they typically are not licensed to conduct such activity, even though the securities themselves may be permitted for transfer.

### **3.7.2 Blue Sky Laws**

In addition to registering its securities under the Securities Act, an issuer must register its securities in every state in which the securities are offered for sale to the public unless an exemption from registration applies. In many states, the state securities commission has authority to apply “merit” regulation and to deny registration to any securities it deems unsuitable for sale. The Securities Act does preempt the right of the states to require the registration of certain categories of securities offerings. In particular, the states are not permitted to require the registration under the Blue Sky laws of any securities that are offered in a private placement pursuant to Rule 506 of Regulation D (although the states may require the issuer to submit certain notice filings and pay associated filing fees).

Title III – Regulation Crowdfunding also pre-empts state securities laws, although the state of incorporation has the reserved power of enforcement. Title IV – Regulation A+ also pre-empts state securities laws, although certain states have filed lawsuits challenge the SEC’ constitutional authority to grant such pre-emption. The Securities Act also prohibits the states from requiring the registration of any securities listed on the New York Stock Exchange or the Nasdaq National Market System (“Listed Securities”). The Blue Sky laws historically have included exemptions for the securities of listed companies because such companies (i) must

satisfy stock exchange listing standards (which can, to some degree, be used as a proxy to identify “quality” companies), and (ii) are subject to ongoing regulation under both stock exchange and SEC rules. The Blue Sky laws, however, may nonetheless impose significant restrictions on resales. An important point – and one that is sometimes overlooked – is that the Blue Sky laws apply not only to an issuer’s sale of its securities but also to all secondary market sales.

### **3.7.3 Investment Company Act**

The Investment Company Act of 1940 (the “Investment Company Act”) requires “investment companies” to register with the SEC before selling any of their securities to the public. The Act defines an “investment company” (in relevant part) as any person engaged in the business of investing in or holding “securities” and that (subject to certain adjustments) owns “securities” having a value exceeding 40% of the value of its total assets.

### **3.7.4 Bank Lending**

The extension of consumer credit in the United States is regulated at both the federal and state levels. A CFP or lender that conducts a nationwide business therefore may be subject to regulation under various laws and, potentially, by multiple jurisdictions. Generally, an internet-based consumer lending program will utilize a third party bank to assist in the facilitation of such loans. The third party bank will be subject to both federal and state regulation but may, in certain instances, be able to rely upon federal law to preempt state laws that would otherwise apply. Federal preemption is important to the third party bank in connection with state usury laws, which limit the amount of interest that may be legally charged in connection with a loan.

### **3.7.5 Usury Laws**

Most states limit by statute the maximum rate of interest that lenders may charge on consumer loans. The maximum permitted interest rate can vary substantially between states. Some states impose a fixed maximum rate of interest while others link the maximum rate to a floating rate index. Absent an exemption, these laws would be binding on the lender making the borrower Loans (whether operating under license or utilizing a third party bank) and would have to be observed in setting the interest rate for each loan.

### **3.7.6 Regulation AB (Asset Backed)**

Regulation AB under the Securities Act sets forth the disclosure requirements that apply to registered offerings of asset-backed securities and to certain periodic reports that the issuers of registered asset-backed securities must file.

## **4 Regulatory barriers for Crowdfunding crossing borders**

The JOBS Act is a United States only series of securities laws. Entrepreneurs are encouraged to work with securities lawyers in all jurisdictions where their investors are either resident or domiciled to ensure that acceptance of their subscription for securities is

permissible. Utilizing an online platform to facilitate a financing creates novel issues and international regulators are concerned about issuers of securities offering and issuing securities from one jurisdiction into another without proper compliance being followed. Regulators have expressed concern and are on alert.

We would admonish all participants to recognize that the sale of online securities is highly sensitive in nature and while conventional analysis is a good starting point for any discussion, all new securities law programs are subject to heightened regulatory attention and must be considered in light of increased focus and opportunistic interpretation of historic rules and regulations. There seems to be too much complacency and expediency by cross-border participants which in our considered view is unsustainable.

## **4.1 Applicable law**

### **4.1.1 Title II – General Solicitation**

Enables domestic and foreign entities to raise capital under these provisions and such entities may select the jurisdiction of applicable law to construe the arrangements, although United States securities laws will necessarily also be implicated.

### **4.1.2 Title III – Retail Crowdfunding**

Only United States and Canadian incorporated companies may raise capital pursuant to these provisions.

### **4.1.3 Title IV – Regulation A+**

Similar to Title III, only United States and Canadian incorporated entities may avail themselves of these provisions, although there are very specific rules about the actual operations of such entities being predominantly in those countries as well.

The applicable regulatory law (Broker-Dealer, Investment Advisor, Investment Company Act, Federal and State Banking Laws) depends on a range of issues, including, what type of securities are being offered by the Crowdfunding Platform, the compensation model for the Crowdfunding platform and the other activities its offering to the public.

## **4.2 Inbound**

Any foreign CFP seeking to raise capital from investors in this country must comply with the securities laws of the United States, both at the federal level and within the states. Securities laws regulate both the purchase and sale of securities. Any offering of securities that seeks to raise capital from individuals or entities within the geographic boundaries of this country trigger our regulations – in all likelihood it will be deemed a public solicitation and either have to satisfy one of the exemptions or be registered with the SEC prior to being offered. Likewise, if a CFP is involved and is going to receive compensation with respect to the capital formation activity it will be subject to all of the various statutory regimes that have been discussed. A solicitation of investors in the United States is very broadly defined, unlike other jurisdictions that we understand require more than an online posting to a CFP. Our

understanding is that they almost require a special directed selling effort to be deemed a general solicitation – this is not so here.

### 4.3 Outbound

Even in the example of a U.S. based platform only offering securities of foreign incorporated opportunities to foreign investors, we believe that the CFP, depending upon its compensation model and actual activity, would require a standard U.S. regulatory review and possibly licensing. Obviously, the analysis only becomes more sensitive and burdensome when either the investors are U.S. or the entity raising the capital is incorporated here. As mentioned above, we believe that proper regulatory process for any non U.S. Crowdfunding must involve experienced foreign securities law analysis in the jurisdiction where any securities are offered and sold.

### 4.4 Impact of EU regulation

As the US is not an EU member-state, the European regulation is not applicable.

## 5 Lessons learned from United States' regulation

### 5.1 Role model ("dos")

Although Crowdfunding in each of its form is intended to be a more efficient means of raising capital and approaching a broader group of potential investors more easily, it should be noted that each of the different statutory provisions has strengths and weaknesses. The strengths and weaknesses vary based upon the particulars of the entrepreneur raising the capital. Understanding the needs and limitations of the entrepreneur has to be properly assessed in order to determine which if any of the JOBS Act provisions is better suited for the entrepreneur.

An entrepreneur that is seeking more than USUSD 1,000,000 must understand that a Title III – Regulation Crowdfunding offering doesn't permit such an offering. A foreign incorporated entrepreneur similarly may not avail itself of that same offering exemption. Regulation A+, while it will permit a larger offering, doesn't permit foreign incorporated entities from using this provision either. A Regulation A+ offering also is much more expensive, requires a full disclosure filing that gets a review by the SEC. For any entrepreneur a Title II – 506(c) may be a very attractive alternative but only wealthier investors may participate which may dramatically reduce the number of qualified investors. Although Title II – 506(c) for the right entrepreneur may be the least expensive and permits an unlimited amount of funds to be raised.

### 5.2 Aspects that should be avoided ("don'ts")

While the JOBS Act has provided entrepreneurs with a very exciting series of new tools for exploring capital formation, countries around the world are experimenting with different forms of Crowdfunding as well. How each of these programs evolve will be interesting to study. The three U.S. approaches provide a useful guide as they become more utilized. With Title II

being the oldest and most utilized, it is fair to say that there have been limited problems to date and that generally speaking entrepreneurs have raised capital more easily than they would have pre-JOBS Act. There are no current proposed changes to these rules specifically, although the SEC continues to consider changes to the definition of an “Accredited Investor”, which would impact who could invest in those financings if this were to be adopted. Title III is little more than a year old and while we believe that it is useful new options, there are many proposals being considered to improve the rules; such as, increasing the maximum amount permitted, allowing investors to invest through special purpose vehicles, etc. Although entrepreneurs have been initially more interested in Title IV – Regulation A+, the success rate of those offerings has been limited. So while there are no meaningful proposals to amend those rules, there needs to be better counselling on what companies can actually utilize a Regulation A+ pathway and actually raise capital.

## 6 Conclusion

Title III, Regulation Crowdfunding turns one year old this week, May 16, 2017. So far (knock on wood) most of the concerns of regulators and investor protection advocates have not presented themselves. This should not be confused with success or that the industry can become complacent, it should just be recognized that the beginnings of a new way to raise capital haven’t been the hot bed of fraud that was projected. At this point, neither has it been the holy grail of new found investment returns for investors. Only time will tell. Judging from the longer success of online Title II, 506(c) and 506(b) Crowdfunding, there is little doubt that online financing as a new industry is here to stay. That industry continues to grow and different professionals in new industries are learning to use online capital formation as a new method for themselves. Like many other emerging programs, as time elapses, and much of the media negativity dissipates, Crowdfunding will become even more commonplace and the rules and regulations will be liberalized to make better accommodations online. While it is certainly a cliché, these are just the early days.

## 7 Summary – Crowdfunding regulation

| Country  | USA  |
|--|--|
| <b>Summary</b>   |  |
| <b>Recent developments in Crowdfunding regulations</b> | <ul style="list-style-type: none"> <li>• Title II of the JOBS Act; no new developments, although the definition of Accredited Investor continues to be under review</li> <li>• Title III of the JOBS Act went into effect May 16, 2016</li> <li>• Title IV of the JOBS Act; no new developments.</li> </ul>  |
| <b>Current / planned Crowdfunding regulation</b>       |  |
| <b>General regulation</b>                              | <ul style="list-style-type: none"> <li>• SEC Advisory Committee<br/><a href="https://www.crowdfundinsider.com/2017/06/102019-upcoming-sec-investor-advisory-committee-meeting-will-tackle-financial-choice-act/">https://www.crowdfundinsider.com/2017/06/102019-upcoming-sec-investor-advisory-committee-meeting-will-tackle-financial-choice-act/</a></li> <li>• House of Representatives passes<br/><a href="https://www.crowdfundinsider.com/2017/06/101700-house-approves-financial-choice-act-dodd-frank-replacement/">https://www.crowdfundinsider.com/2017/06/101700-house-approves-financial-choice-act-dodd-frank-replacement/</a></li> </ul> <p><b>General Regulation</b></p> <ul style="list-style-type: none"> <li>• The JOBS Act enables three different forms of securities based Crowdfunding, each of which has different rules and regulations – Title II, Title III and Title IV. Entrepreneurs and their counsel are encouraged to consider each as means to facilitating a potential capital raise.</li> </ul>  |
| <b>Prospectus requirement</b>                          | <ul style="list-style-type: none"> <li>• Title II—This provision doesn't require any specific disclosure BUT remains subject to the anti-fraud provisions of the securities laws. We believe that best practice requires the entrepreneur to provide risk factors.</li> <li>• Title III—This provision requires the completion of a disclosure document referred to a Form C which must be submitted to the SEC. The SEC does not review and comment upon the filing. The specific requirements are similar to a private placement memorandum.</li> <li>• Title IV—This provision requires the completion of a disclosure document referred to a Form 1-A which must be submitted to the SEC for review and comment. The specific requirements are similar to a full S-1 IPO prospectus.</li> <li>• Funding Platforms <ul style="list-style-type: none"> <li>- Depending upon the compensation model for a funding platform and its activity it may be required to become a registered Broker-Dealer with FINRA or registered investment advisor.</li> <li>- Funding Platforms and issuers must comply with both KYC and AML regimes.</li> </ul> </li> </ul> |

|                            |   |
|----------------------------|---|
|                            | <ul style="list-style-type: none"> <li>- Best practice requires that the funding platforms typically not “touch” or handle funds but cause independent and qualified escrow agents to maintain funds pending release conditions.</li> </ul>   |
| <b>Regulatory barriers</b> |   |
| <b>Inbound</b>             | <ul style="list-style-type: none"> <li>• While there are no limitations on foreigners becoming owner/operators of funding platforms they would still require proper approval from FINRA, the SEC and/or State regulators.</li> <li>• Just because an entrepreneur or funding platform is conducting an authorized US financing under on of the provisions of the JOBS Act it doesn’t suspend their requirements to satisfy international regulations wherever they are conducting the offering and raising capital from foreign investors.</li> <li>• Title II—any US or foreign entity may avail itself of this provision of the JOBS Act and raise capital.</li> <li>• Title III—only US entities may raise capital under this provision of the JOBS Act.</li> <li>• Title IV- only US and Canadian entities may raise capital under this provision of the JOBS Act.</li> </ul> |
| <b>Outbound</b>            | <ul style="list-style-type: none"> <li>• Without proper registration of the offering or an exemption-- a foreign entity or Crowdfunding platform should not accept US investor may</li> <li>• There are no restrictions on US entities raising capital abroad so long as they comply as necessary with local law.</li> </ul>  |

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