CHAPTER 9

INVESTMENT-BASED CROWDFUNDING PLATFORMS AND THEIR REGULATION

Eugenia Macchiavello

University of Genoa

1. INVESTMENT-BASED CROWDFUNDING: MAIN CHARACTERISTICS UNDER A FUNCTIONAL APPROACH. SCOPE, OBJECTIVE AND STRUCTURE OF THIS CHAPTER

Modern crowdfunding started in the early 2000s as an instrument to fund specific projects through small contributions from users of online platforms (the 'crowd'). While the first initiatives consisted in funds donated, with or without expectation to receive a gadget or even a prototype of a product as reward ('donation-based' and 'reward-based' crowdfunding) and micro-loans provided indirectly and for free to micro-entrepreneurs in developing countries (eg Kiva in the US), such phenomenon soon developed worldwide to occupy also credit and investment markets (eg Zopa in the UK since 2005 and Lending Club in the US since 2006 for lending; and ASSOB-Enable Funding in Australia since 2007).[1] Crowdfunding growth has been spurred by the global financial crisis and its consequent banking credit crunch as well as distrust towards traditional finance. It now represents a market of nearly $114 billion worldwide, with USA and Canada leading the way by market size.[2]

This Chapter will not cover donation- or reward-based crowdfunding, although widely used also by entrepreneurs, and will focus instead on financial-return crowdfunding ('FRC', also called by international economic reports, 'investment crowdfunding'). This exclusion is motivated by the main topic of this Book, financial regulation, which comes into play when loans (sometimes even if not remunerated) and/or investments are involved, not simple donations or pre-sales.[3]

This category of crowdfunding might be defined as an open call from entrepreneurs or consumers addressed to a multitude of internet users to receive from the latter small contributions (when individually considered) in the form of loans (lending-based crowdfunding – LBC) or investments (investment-based crowdfunding – IBC) in specific projects, usually through specialised online platforms. Investments can consist in shares or equivalent forms of participation in ownership of a firm - equity-based crowdfunding (EBC) – or, definitely less frequently, debt-securities (eg bonds, mini-bonds) or other forms of investments, such as profit-sharing investment contracts (entitling the

[1] See A Kallio and L Vuola, 'History of Crowdfunding in the Context of Ever-Changing Modern Financial Markets', in R Shneor, L Zhao, BT Flåten (eds), *Advances in Crowdfunding* (Palgrave Macmillan 2020). The author is grateful to Chiara Valenti for her valuable research assistance during the preparation of this Chapter and to the participants of the authors' workshop (E&Y and ACLE, 20-21 April 2023) for their insightful feedback.

[2] In 2020, the main market shares were: US and Canada (65%), UK (11%), Europe (9%), Asia and Pacific (excluding China) (8%); Singapore and Australia were, respectively, the first and second country in Asia for equity crowdfunding: T Zieger and others, 'The 2nd Global Alternative Finance Market Benchmarking Report' (2021) https://www.jbs.cam.ac.uk/wp-content/uploads/2021/06/ccaf-2021-06-report-2nd-global-alternative-finance-benchmarking-study-report.pdf.

[3] On the regulation in Europe of non-financial/non-investment crowdfunding, please see E Macchiavello and C Valenti, 'Beyond the ECSPR and Financial-return: The Regulation of Donation and Reward-based Crowdfunding in the EU', in E Macchiavello (ed), *Regulation on European Crowdfunding Service Providers for Business: A Commentary* (Edward Elgar 2022) 619ff.

holder to a share in future sales revenue without ownership or governance rights).[4] Loans also can have differentiated features, such as subordinated loans and profit-sharing loans (with remuneration linked to the performance of the business). A separate form is invoice trading, through which entrepreneurs can satisfy their liquidity needs by selling credit rights related to receivables/invoices at a discount, on an online platforms, and to individuals or institutions.[5]

Business models deployed by crowdfunding service providers (CSPs) can vary too: under the basic model ('client-segregated account'), they facilitate the financing transaction between project owners and crowd-lenders/investors, putting them in contact through the publication of funding requests on an online platform. However, the CSP generally performs additional fundamental functions: pre-screening of the projects and applicants (sometimes even pricing), provision of templates of/pre-filled contracts. Most platforms also handle the contractual relationships between clients, including information flow, servicing, credit collection, mandate to renegotiate and/or vote. Especially in LBC, CSPs might adopt models allowing the automatically match of crowd-lenders' preferences (in terms of risks, maturity, sector, etc) with crowd-borrowers' characteristics, also to ensure diversification, or, to further mitigate risk, offer guarantee funds to (partially) compensate clients in case of crowd-borrowers' default. When not resorting to a separate payment service provider, platforms might also handle money transfers between different users. Under other LBC models, a bank originates the loans and then resells the credit rights to a Special Purpose Vehicle (SPV) created by the CSP and issuing notes to crowd-lenders ('notary model'), to cope with regulatory restrictions (banking monopoly: Germany and Korea; State-based banking licenses: US). Finally, the CSP might collect resources from crowd-lenders/investors through the issuance of financial instruments (itself or through *ad hoc* SPVs or investment funds) and then lend/invest such resources on its own account to project owners ('balance-sheet' model: US, Australia and Canada), sometimes guaranteeing a certain return to investors ('guaranteed-return' model).[6] Some platforms, mostly LBC, also offer crowd-lenders the opportunity to re-sell their rights to the platform (early reimbursement) or on P2P marketplaces ('bulletin boards').

Crowdfunding has been regarded as a useful tool to meet consumers' and businesses' (especially, start-ups and small and micro-enterprises) under/unmet financing needs, at reasonable costs as well as investors' need for diversified alternative investments finance and desire for a more 'democratic' financial system. It has also been presented as a form of 'disintermediated' finance, directly connecting financers and financees, reducing the traditional chain of financial intermediation through the elimination of underwriters, distributors (banks and investment firms), analysts, rating agencies, etc. However, crowdfunding platforms' activities present similarities with traditional financial services, suggesting a 're-intermediation' phenomenon and a (at least partial) role of crowdfunding platforms as gatekeepers.[7]

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[4] For widely used definitions of crowdfunding, see: A Schwienbacher and B Larralde, 'Crowdfunding of Small Entrepreneurial Ventures' in D Cumming (ed), *The Oxford Handbook of Entrepreneurial Finance* (OUP 2012) 369, 370–371.

[5] See also E Macchiavello, 'Introduction to the Crowdfunding Regulation' and R Shneor, 'The context: the crowdfunding market and its recent developments', in Macchiavello (n 3), 2ff and 15ff.

[6] Concerning crowdfunding models and characteristics: E Kirby and S Worner, 'Crowd-funding: An Infant Industry Growing Fast' (2014), www.iosco.org/research/pdf/swp/Crowd-funding-An-Infant-Industry-Growing-Fast.pdf; Committee on the GlobalFinancial System (CGFS)–Financial Stability Board (FSB), *FinTech Credit. Market Structure, Business Models and Financial Stability Implications* (BIS 2017) 11ff.

[7] For the definition of gatekeepers in the financial sector: J Payne, 'The Role of Gatekeepers', in N Moloney, E Ferran and J Payne (eds), *Oxford Handbook of Financial Regulation* (OUP 2015) 254. On crowdfunding and disintermediation/re-intermediation: E Macchiavello and A Sciarrone Alibrandi, 'Marketplace Lending as a New Form

Although relevant differences exist among countries, LBC has been associated with credit intermediation, banking/lending and payment services, while IBC with investment services, in particular reception and transmission of orders, underwriting without firm commitment (sometimes also investment advice, markets and execution).[8] Nonetheless, some countries, including the EU recently, have underlined the resemblance also of LBC to investment services and public offerings of investment products (although, generally, not involving transferable securities), facilitating the transfer of financial resources between parties through the reduction of information asymmetries and transaction costs.[9] From an economic point of view, a crowd-loan is very close to a bond,[10] although relevant differences might exist, also from a legal perspective, in terms of transferability and rights attached (making LBC a new asset class).

However, crowdfunding also present special features, which might influence its legal classification and treatment. For instance, investors seem motivated not only by the expectation of a financial return, but also by non-financial rewards, such as personal satisfaction from influencing a campaign's outcome and freely pick projects with shared principles and sense of involvement.[11] Moreover, crowd-investors appear to assign more importance in their investment decisions on soft information, 'signals' and non-financial factors[12] rather than on financial statements.[13] The instruments to communicate with and inform potential investors (simple documents, pitches and forums, instead of a long and complex prospectus and financial documentations)[14] and risk-mitigation instruments (mandatory diversification, 'all-or-nothing' rule[15], co-investing with experienced investors) in absence of underwriters and other pricing mechanisms are also distinctive.[16] Nonetheless, in consideration of the risks for investors, project owners and the system (frauds, instability, cyber-risks, etc.), crowdfunding has attracted more and more regulatory attention.

This Chapter will analyse the regulatory approaches towards crowdfunding activities in various countries/regions (EU, UK, US, Singapore and Australia), comparing the solutions adopted by each under the main areas and tools generally deployed in financial regulation (eg authorisation, prudential requirements, investor protection, etc) to attain the fundamental financial regulation goals (eg

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of Capital Raising in the Internal Market: True Disintermediation or Re-intermediation?', in E Avgouleas and H Marjosola (eds), *Digital Finance in Europe: Law, Regulation, Governance* (De Gruyter 2021) 37-85; E Macchiavello, 'The Licensing Principle and Investment-Based Crowdfunding', in D Moura Vicente, D Pereira Duarte and C Granadeiro (eds), *Fintech Regulation and the Licensing Principle*, (EBI/CIDP, 2023) 46-70; O Havrylchyk and M Verdier, 'The Financial Intermediation Role of the P2P Lending Platforms' (2018) 60 Comp Econ Stud 115–130; F Kaja, E Martino, A Pacces, 'Fintech and the law and economics of disintermediation', in IH Chiu and G Deipenbrock (eds), *Routledge Handbook of Financial Technology and Law* (Routledge 2021), 78-95, 83-84, 88-89.

[8] See for instance: Macchiavello (n 3) 44-67; E Macchiavello, 'Disintermediation in Fund-raising: Marketplace Investing Platforms and EU Financial Regulation', in Chiu and Deipenbrock (n 7), 291-306.

[9] On investment firms' functions: A Pacces, 'Financial Intermediation in the Securities Markets: Law and Economics of Conduct of Business Regulation', (2000) 20 Intl Rev Law Econ 279, 481-82.

[10] See Commission, 'Impact Assessment Accompanying the Document Proposal for a Regulation on European Crowdfunding Service Providers (ECSP) for Business' (8 March 2018); Macchiavello and Sciarrone (n 7).

[11] Among others: A Lukkarinen, 'Equity Crowdfunding: Principles and Investor Behaviour', in Shneor, Zhao, Flåten, (n 1) 96ff.

[12] Eg the availability of videos and updates, the perceived informativeness and clarity of the campaign material, certain entrepreneur's characteristics (eg patents, level of education), the involvement of a credible lead investor.

[13] Lukkarinen (n 11) 99.

[14] Please see Macchiavello (n 7) 49-50.

[15] ie, the project owner can obtain the financing only if the campaign reaches the declared target amount, convincing enough investors.

[16] Further on these differences: E Macchiavello, 'The Crowdfunding Regulation in the Context of the Capital Markets Union', in P Ortolani and M Louisse (eds), *The EU Crowdfunding Regulation* (OUP 2021) 25-46.

stability, investor protection, efficiency, etc) and govern regulated activities[17], highlighting similarities, differences and the level of relevant interests protected.

2. REGULATORY APPROACH: OVERVIEW OF THE MAIN LEGAL FRAMEWORK, CLASSIFICATION OF THE ACTIVITY/PRODUCTS AND AUTHORIZATION

2.1. The main legal framework: new special regulation versus *application of traditional financial regulation, scope and different balance of regulatory goals*

All analysed jurisdictions have decided to address crowdfunding in their regulations with the objective of facilitating SMEs' access to finance while protecting platforms' clients. Nonetheless, in doing so, they also present different approaches which reflect a different ranking in regulatory goals: the US and Singapore show a more 'traditional' and rigid approach, mostly relying on the pre-existing legal framework and favouring investor protection and the level-playing field; on the opposite side, the EU has introduced a special regime in exemption from the mainstream framework and willing to sacrifice traditional safeguards to expand SMEs' financing opportunities and favour cross-border crowdfunding; UK and Australia, instead, present a hybrid system, having introduced special rules only for certain crowdfunding models to better balance different regulatory objectives.

2.1.1. United States of America (USA)

In the US, both IBC and LBC are placed in an investment context since, based on a broad notion of 'security' grounded in a well-established US doctrine, even the loan notes issued by crowdfunding platforms within a 'notary' business model have been classified by SEC as securities[18] and therefore subject - in principle - to the whole set of securities regulation and to SEC supervision. In particular, issuers and platforms would be required to comply with the 1933 Securities Act which sets rules for the registration of securities with the SEC and their offering to the public (through long and costly processes for the registration and disclosure), and the 1934 Securities Exchange Act, which contains requirements for secondary markets, issuer disclosures and intermediaries' licenses.[19] Certain exemptions in Sections 4(a)(2) and 4(a)(5) of the Securities Act and the SEC's Regulation D and Regulation A might be used, such as the 'intrastate offering' exemption (for local offerings), the 'small offering' one (for amount not above $5 million) and the 'accredited investors' one (in case of offerings reserved to professional and experienced investors), but these entail several offering limitations or anyway extensive disclosure requirements. Therefore, in 2012 the Obama administration adopted the Jumpstart Our Business Startups Act (JOBS Act) to facilitate SMEs capital raising, which included a part (title III) dedicated to the Capital Raising Online Deterring Fraud and Unethical Non-Disclosure Act (CROWDFUND Act). This Act, completed in 2015 by a SEC Crowdfunding Regulation[20] (also recently amended in 2021), introduced a special exemption from

[17] See IOSCO, 'Objectives and Principles of Securities Regulation' (2017), https://www.iosco.org/library/pubdocs/pdf/IOSCOPD561.pdf; BCBS, 'Core Principles for Effective Banking Supervision' (2019), https://www.bis.org/basel_framework/standard/BCP.htm; J Armour and others, *Principles of Financial Regulation* (OUP 2016).

[18] See for instance, *In re Prosper Marketplace, Inc.*, Securities Act Release No 8984, SEC LEXIS 279124 (November 2008), available at http://www.sec.gov/litigation/admin/2008/33-8984.pdf, applying the milestones decisions *SEC v. W. J. Howey Co.*, 328 U.S. 293 (1946) and *Reves v. Ernst & Young*, 494 U.S. 56 (1990) about the notion of 'security' and the test to identify it.

[19] Current versions: Securities Act of 1933, 15 USC §77a ff (2022); Securities Exchange Act of 1934, 15 USC §78a ff (2022).

[20] SEC Rules 80 FR 71387. These rules refer to crowdfunding as follows: 'crowdfunding is a relatively new and evolving method of using the Internet to raise capital to support a wide range of ideas and ventures. An entity or individual raising funds through crowdfunding typically seeks small individual contributions from a large number of people. Individuals

the Securities Act for small offerings of securities issued by certain companies and intermediated by regulated brokers (authorised under Sec 15(b) Exchange Act) or specialised funding portals authorised under the new Section 4A(a)(1) Securities Act and rule 400 Crowdfunding Regulation,[21] both members of the Financial Industry Regulatory Authority (FINRA).[22]

In particular, the new regime covers any type of security offerings, up to $5 million (threshold raised in 2021) but only when issued by domestic companies and with the exclusion of investment companies, Special Purpose Acquisition Companies (SPAC), companies having already filed – or failed to provide - reports with the SEC under the Securities Exchange Act and 'bad actors' issuer (ie disqualified for business practices violations or felonies).[23] The 2019 review has allowed SPVs to be used in crowdfunding when the SPV acts solely as a conduit for investments in a crowdfunding issuer and under certain conditions, such as that investors in the crowdfunding SPV have the same economic exposure, voting power, and Regulation Crowdfunding disclosures as if the investors had invested directly in the crowdfunding issuer.[24]

2.1.2. Singapore

The initial approach to crowdfunding in Singapore consisted in the application of the general and pre-existing financial regulation framework, posing significant obstacles to such activity. Nonetheless, in 2016, exemptions and lower requirements for securities-based crowdfunding were introduced to support SMEs and their financing needs.[25]

In particular, any offer of securities requires the publication of a prospectus, unless exemptions apply, such as in case of small offers ('personal' offers up to SG$5 million in 12 months) or, conditional to no advertisement, private placements (up to 50 investors in 12 months) or offers to institutional/accredited investors only.[26] These general exemptions allow most crowdfunding offers to avoid prospectus obligations. The platform facilitating the securities issuance needs a Capital Markets Services (CMS) license under the Singapore's Securities and Futures Act (SFA) from the Monetary Authority of Singapore (MAS), generally for the service 'dealing in securities'.[27] Also the

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interested in the crowdfunding campaign—members of the "crowd"—may share information about the project, cause, idea or business with each other and use the information to decide whether to fund the campaign based on the collective "wisdom of the crowd."'

[21] Härkönen, 'ECSPR versus the United States crowdfunding regime', in Macchiavello (n 3), 796-807, 796.

[22] FINRA is a not-for-profit organization overseeing broker‑dealers. See also Härkönen (n 21) 799.

[23] 17 CFR §227.503. See Härkönen (n 21) 802.

[24] New Investment Company Act Rule 3a-9 i. About the 2019 Review see the synthesis at https://www.sec.gov/corpfin/facilitating-capital-formation-secg.

[25] P. Wisuttisak, N. Ba Binh, A. Terry, 'Regulatory frameworks of crowdfunding for startups in Singapore, Thailand, and Vietnam', in F. Taghizadeh-Hesary and others (eds), *Innovative Finance for Technological Progress* (Routledge 2022), 117; SL Tan, YW Tok and C Thitipat, 'Financing Singapore's SMEs and the crowdfunding industry in Singapore' in HT Hoon (ed), *The Singapore economy: Dynamism and inclusion. Research Collection School of Economics* (Singapore, 2021) 22ff, https://ink.library.smu.edu.sg/soe_research/2511. See https://www.mas.gov.sg/news/parliamentary-replies/2016/reply-to-parliamentary-question-on-the-new-licensing-regime-for-crowdfunding-platforms.

[26] Securities and Futures Act §§240, 239(3); §272A, §272B, §274, §275. Accredited investors are: individuals with net personal assets above SG$2 million in value or income at least of SG$300,000 (or the equivalent in a foreign currency); corporations with net assets above SG$10 million in value: §4A(1)(a). See also MAS, 'Securities and futures Act (cap 289) financial advisers Act (cap 110) - FAQs on lendingbased crowdfunding' (2018), A16, https://www.mas.gov.sg/-/media/mas/regulations-and-financial-stability/regulations-guidance-and-licensing/securities-futures-and-fund-management/regulations-guidance-and-licensing/faqs/faqs-on-lendingbased-crowdfunding-8-oct-18.pdf; C. Hofmann, 'Crowdfunding regulation in Singapore', in C. Kleiner (ed) *Legal Aspects of Crowdfunding* (Springer 2021) 401; A Ang and S Kwek, 'Regulation of Crowdfunding in Singapore' (2020) 21 Bus L Int'l 59, 64.

[27] Securities and Futures Act § 342 Second Schedule, Regulated Activities Part I; MAS 2018; MAS, 'Securities and futures Act (cap. 289) FAQs on licensing and business conduct (other than for fund management companies)' (rev. July

classification as 'advice on corporate finance' or 'advice on securities' is possible, since such concepts cover also indirect advice and publication of research analysis[28]: in such cases, a CMS license or Financial Advisers Act (FAA) license are required.[29]

The concept of securities offering has been broaden to cover, within offer of debentures, also 'any invitation to a person […] to lend money to an entity' or 'any document […] issued by an entity acknowledging […] the indebtedness of the entity in respect of any money […] lent […] in response to such an invitation' (except the offer of units in collective investment schemes), so that also LBC is generally subject to securities law and MAS supervision (since 2018, Part I, section 2; 239 SFA). Moreover, if the platform acts as a professional lender or agent of the same in respect to loans to consumers, it also needs to obtain a license as money lender form the Singapore's Registrar of Moneylenders under the Ministry of Law.[30] Instead, platforms resorting to (alternative) collective investment scheme through limited partnership, remain mostly unregulated.[31]

Finally, invoice trading requires no CMS license if the creditor assigns to investors credit towards customers through the platform, because of the absence of a security, contrary to the case of the platform buying the credit from the creditor and agreeing with investors to lend money from them (which instead involves the issuance of debentures, considered securities).[32]

2.1.3. United Kingdom (UK)

The UK has provided differentiated solutions for IBC and LBC, although the FCA acts as supervisory authority for both. The former has been regarded as generally falling within existing regulated financial activities and requiring an authorisation from the FCA[33] for conducting a regulated activity such as: 'arranging deals in investments'[34], or 'making arrangements with a view to transactions in investments'[35] or, based on the particular model, also operating/managing an unregulated collective investment schemes or AIF, while other classifications ('dealing in investments as agent', 'advising on investments' or 'managing investments') are less frequent.[36] As a consequence, a relevant bulk of financial regulation applies: the Financial Services and Markets Act 2000, its secondary acts (eg RAO) and relative FCA handbooks concerning principles for businesses (PRIN), Senior management Arrangements, Systems and controls (SYSC), investment conduct of business sourcebook (COBS) (mainly derived from MiFID II), client assets rules (CASS), and, more recently, financial promotions (see below §4.4).

Instead, a special framework was introduced in 2014 in the FCA handbook to address LBC, as the new regulated activity of 'operating an electronic system in relation to lending' and, in particular, to a P2P agreement defined in Art. 36H. Consequently, loans covered are only the ones, facilitated by

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2022), No. 2 and 4, https://www.mas.gov.sg/-/media/mas/regulations-and-financial-stability/regulations-guidance-and-licensing/securities-futures-and-fund-management/regulations-guidance-and-licensing/faqs/faqs-on-licensing-and-business-conduct-other-than-for-fund-management-companies_18-jul-22.pdf. Hoffman (n 26) 397, 402; Wisuttisak (n 25) 107.

[28] Financial Advisers Act, c. 110, §2, Second Schedule; Hofmann (n 26) 406-7.

[29] SFA ibidem; Financial Advisers Act, c 110, §6.

[30] Moneylenders Act §5(5)(c), § 2(e)(ii)-(iii), §§2, 5. See also SL Tan, YW Tok and C Thitipat, 'Financing Singapore's SMEs and the crowdfunding industry in Singapore' (2021), https://ink.library.smu.edu.sg/soe_research/2511.

[31] Hofmann (n 26) 403.

[32] MAS FAQ on licensing, A17.

[33] Part 4a FSMA, section 55A.

[34] Art 25(1) RAO; service defined in broader terms than the MiFID II-reception and transmission of orders.

[35] Art 25(2) RAO.

[36] Respectively, Artt 21, 53 and 37 RAO. See K Baillie, 'Regulation of Crowdfunding in the UK: Past, Present and Future' (2019) 20(2) Bus L Int'l 148.

the platform (which does not act as lender), where the borrower is an individual (ie, a natural person, a partnership or an unincorporated body of persons) and either the loan does not exceed £25,000 or it is not wholly/predominantly for business. Requirements for LBC platforms have grown progressively, with the extension to this service, in 2016, of section 18.12 COBS, client money duties and financial promotions and dispute resolution rules; the 2019 FCA review has specified rules on disclosure and contingency funds and, more generally, increased the requirements for LBC, seen as more complex and varied than EBC.[37] Moreover, in case of borrowers who are also consumers, the 1974 Consumer credit act and FCS consumer credit rules (CONC) apply too.[38]

Neither regime entail a maximum threshold for crowdfunding offers but, in case of transferable securities, the general exemption from the Prospectus applies (total consideration in 12 months not above €8 million).[39]

2.1.4. Australia

Australia has adapted its legal framework to crowdfunding offerings and services through the 2017 Corporations Amendment (Crowd-Sourced Funding) Act (and related Regulations) and the following 2018 Corporations Amendment (Crowd-sourced Funding for Proprietary Companies Act) as well as minor modifications to the Australian Securities and Investments Commission (ASIC) Act 2001.[40] The regime covers only the offering of ordinary shares of Australian unlisted public companies with less than A$25 million in assets and annual turnover and proprietary companies with certain characteristics (at least two directors, annual financial and directors' reports, compliance with related party transaction rules), offered to retail investors through an online platform.[41] It also regulates liability issues, investor protection and CSPs. Reliefs from some requirements can be demanded to ASIC.[42]

Consequently, the offering of crowdfunding services related to securities (eg shares or debentures) is a regulated activity under part 6D.3A Corporations Act 2001[43] requiring an Australian financial service (AFS) license for this specific service and the compliance with financial regulation (including certain dedicated requirements).[44]

Instead, LBC (not specifically defined by law[45]) is generally offered in the country through collective investment schemes (managed investment scheme or 'MIS'), which must be registered and require again an AFS license and the publication of investment plan/constitution but only when presenting

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[37] See FCA, 'Loan-based ('peer-to-peer') and investment-based crowdfunding platforms: feedback on our post-implementation review and proposed changes to the regulatory framework' (2018) Consultation paper CP18/20, www.fca.org.uk/publication/consultation/cp18-20.pdf; F De Pascalis, 'Crowdlending and crowdinvesting in Europe: a comparative analysis between the UK and EU regulatory frameworks', in Macchiavello (n , 650-51.

[38] See G McMeel, 'Crowdfunding and UK Law', in Ortolani and Louisse, 70.

[39] FSMA 2000, s 86(1).

[40] AA Schwarz, *Investment Crowdfunding* (OUP 2023) ch 6; P Rajapakse, 'Regulatory and Policy Reforms in P2P Lending in Australia', in Rajapakse and others, *Law and Practice of Crowdfunding and Peer-to-Peer Lending in Australia, China and Japan* (Springer 2022). See also: https://asic.gov.au/regulatory-resources/financial-services/crowd-sourced-funding/.

[41] 738G-738H Corporations Act 2001; ASIC, 'Crowd-sourced funding: Guide for companies' (2020), RG 261.6, https://download.asic.gov.au/media/5702668/rg261-published-19-june-2020-20200727.pdf.

[42] ASIC (n 41).

[43] ASIC, 'Crowd-sourced funding: Guide for intermediaries' **(**2018), 262.28, https://download.asic.gov.au/media/cfxatjf5/rg262-published-18-october-2018-20220328.pdf.

[44] Section 738C Corporations Act.

[45] ASIC, 'Marketplace lending (peer-to-peer lending) products' Information sheet (INFO 213) (last updated 2020), https://asic.gov.au/regulatory-resources/financial-services/marketplace-lending/marketplace-lending-peer-to-peer-lending-products/.

more than 20 members or promoted by a person in the business of managing investment schemes and directed to retail investors.[46] Moreover, if the borrower is a natural person and requests the loan for consumption from a professional lender, he/she is considered a consumer and the platform needs a license as credit provider under the National Consumer Credit Protection Act 2009 (section 6) and its Schedule 1 (National Credit Code) when directly providing the loan or a credit-related service (eg credit assistance, intermediary, exercise right/obligation in debt collection), conditional to requirements similar to AFS.[47]

In principle, other possible classifications of the LBC service, requiring again an AFS license, are: 'financial product advice', ie recommendation/statement of opinion/report intended/reasonable regarded as to influence a person in making a decision in relation to particular shares, debentures, derivatives, interests in registered/unregistered MIS, in case the platform assigns grades to borrowers[48] or 'arranging for a person to engage in dealing in financial products'. When the platform offers an organized market for shares/debentures, it needs a license as regulated market.[49]

2.1.5. The European Union

The regulatory treatment of crowdfunding among European Member States have been fragmented for many years, with some countries having adopted special regulations dedicated to crowdfunding (eg France, Italy, Spain, Portugal), others applying pre-existing financial regulation (MiFID-derived rules; banking law; PSD-derived rules, etc) without adaptations, others instead resorting to general national frameworks in exemption from EU regimes (eg Art. 3(1) MiFID II: Germany) or introducing some limited exemptions/adaptations for crowdfunding (eg Austria).

Harmonisation has been reached only through the adoption of the EU regulation No 1503/2020 on crowdfunding service providers for business (hereinafter, ECSPR)[50], with the relevant exclusion of P2P consumer lending. The ECSPR introduces a new special EU-wide license and regime, in exemption, under certain conditions, from MiFID II and Prospectus Regulation (PR) requirements, assigning the supervision of the activities to the national competent authority (generally, the financial one). It covers the offer of transferable securities (eg shares and bonds) and/or admitted instruments for crowdfunding purposes (ie shares of private limited companiesn not considered transferable securities by national law) and business loans (where unconditional and onerous), up to €5 million in total consideration (and including also offers of the same issuer covered by the PR 'small offers' exemption, up to €1-8 million), through a crowdfunding platform. The use of SPV is limited (eg only in case of indivisible and illiquid assets).[51]

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[46] Sections 601ED and 601FA Corporations Act. Investors are presumed retail unless certain conditions apply, such as the price of the financial product exceeds A$500,000, it is provided in connection with a non-small business or in presence of an accountant's certificate of net assets of A$2 million and gross income of $250,000 or in case of professional investor (AFS license holders, listed entities and persons controlling gross assets of at least A$10 million). Moreover, the financial intermediary should have reasonable grounds to believe that the person has previous experience in using financial services, the product or service is provided for use in connection with a business and investing in financial products and the client signs a written statement in this respect: Section 761G Corporations Act; ASIC (n 43), RG 262.23; Rajapakse (n 40) 69.

[47] ASIC (n 41); Rajapakse (n 40) 75-76.

[48] Ibidem, 71.

[49] Section 767A; ASIC (n 43), RG 262.17; Rajapakse (n 40) 85.

[50] Regulation (EU) 2020/1503 […] of 7 October 2020 on European Crowdfunding Service Providers for Business, and Amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 [2020] OJ L347/1.

[51] Recital 22 and Art 3(6) ECSPR; ESMA, 'Questions and Answers on the European crowdfunding service providers for business regulation' (updated 8 March 2023) ESMA35-42-1088, sec 1 (ESMA, 'Q&A').

Therefore, ECSPR regulates also the intermediaries operating such platforms and conducting crowdfunding services, ie the 'matching of business funding interest of investors and project owners through the use of a crowdfunding platform' and consisting of the facilitation of granting of (business) loans and/or the joint provision of placing without firm commitment and reception and transmission of orders, as identified in Section A of Annex I MiFID II, points 7 and 1 (Art 2(1)(a) ECSPR). The regulation allows (and seems to consider as crowdfunding services) the use of filtering systems based on objective factors (eg economic sector, type of instruments, risk category, interest rate). It is instead unclear whether pricing/scoring of offers and, even more, portfolio management of loans (even where the allocation is automatic), subjected to additional and stricter requirements, account still as crowdfunding services or as ancillary ones.[52] P2P consumer lending, invoice trading and crowdfunding offered through other types of services (eg financial advice, collective investment schemes, trading venues) remain subject to their respective national/EU regimes[53] and authorisations, which might be separately obtained by CSPs.

2.2. Authorization requirements, prohibited activities and reporting to the supervisor

As anticipated, the provision of crowdfunding services generally requires a license from the financial authority (UK, EU, Singapore, Australia), which verifies the compliance with certain authorisation requirements. The jurisdictions introducing a special license for crowdfunding have set requirements similar to the ones for traditional financial providers, except for some 'facilitations' (eg lower capital or proportional requirements), such as: appropriate resources[54], localisation in the relevant geographical area[55], fit and proper managers/main shareholders and suitable business model.[56] Some jurisdictions present a longer list of requirements: also organisational competence (eg including training: Australia) and measures to deal with conflicts of interest, compliance with outsourcing rules, dispute resolution, risk management (including certain double-checks as gatekeeper: see below § 4.3-4.4. about US, EU and Australia), insurance also to compensate retail clients (EU[57]; Australia[58]). Some require a minimum initial capital (Singapore[59]; UK[60]). The US requires crowdfunding portals to register with the SEC simply by submitting an online form, disclosing disciplinary history, compensation, client money protection, main shareholders, disciplinary history of associated persons

[52] See ESMA 'Q&A', sec 3.2 (where the Commission propends for the second option).

[53] Consumer LBC, after being removed from the Consumer Credit Directive (CCD) Review, remains subject so far to national law or national interpretations of CCD, while also invoice trading seems (implicitly) excluded; no mention of crowdfunding of security tokens in ECSPR but likely covered by ECSPR, DLT-pilot/MiFID II. Crowdfunding offered through investment advice or the operation of a trading venue is subject to MiFID II/MiFIR (+MAR, etc) or national law (when the advice is exempted under Art 3(1) MiFID II), while through collective investment schemes to AIFMD/national law. See Macchiavello (n 3) 50, 62-67.

[54] In Australia, CSP must have adequate resources in terms of human, technological and financial resources: see also below §3.2.

[55] The US regime admits non-residential funding portals but requiring an agent in the US and evidence of the SEC's ability to access their data/information: §227.400(f).

[56] For the UK: section 55B FSMA, schedule 6, part 1B; FCA handbook COND; McMeel (n 38) 77-78. For EU: Art 12(2)-(3) ECSPR.

[57] Artt 12(2) and 11(7) ECSPR.

[58] ASIC (n 43), 262.28ff.

[59] For moneylenders: deposit of SG$20,000; for CMA license holders offering IBC: SDG50,000 (lowered in 2016 from 250,000) in case of clients accredited investors and SDG500,000 in case of retail investors. MAS in 2016 also removed the SG$100,000 security deposit (set to protect investors) for CSPs but only when they do not handle customer monies/assets, do not act as a principal in transactions and only raise funds from accredited and institutional investors. See Hofmann (n 26) 396ff; Tan (n 30), 22-23.

[60] Minimum capital for FCA licenses range from £50,000 (eg reception and transmission of orders only and without holding clients' funds/securities) to £730,000 depending on the type of service.

and non-securities activities in addition to becoming a FINRA member, while brokers present stricter requirements (eg professional requirements of associated persons; minimum capital requirements).[61]

Many regimes consider crowdfunding intermediaries as limited intermediaries, prohibiting other regulated activities such as investment advice, handle investors' money/securities (US[62]; EU). Some regimes prohibit the solicitation of particular offers (US; EU; UK; Singapore).[63] Instead, platforms are allowed to make search engines for investors or highlight certain offers based on objective criteria (eg types of securities, geographic location, type of industry, etc) and language (US[64]; EU). Generally, platform do not benefit from an exclusive reserve of activity and other more strictly regulated intermediaries can offer crowdfunding services, along with other services not permitted to platforms (brokers in US; investment firms in the EU; CMA-license holders in Singapore[65]).

CF providers might be subject to a duty to report to the authority, such as on the amount collected, successful/unsuccessful offers, type of investors, exercise of cooling-off, complaints, outgages, remuneration (Australia[66]; EU[67]). Moreover, they must maintain records of transactions, communications and other related data for 5 years (US[68]; EU[69]).

3. ORGANIZATIONAL AND PRUDENTIAL REQUIREMENTS

3.1. Organizational requirements and conflict of interests

In addition to general requirements of adequate organization, most regimes require CSPs to have systems/measures to deal with conflicts of interests (UK[70]; EU[71]; Australia[72]), seen as a fundamental issue considering the particular intermediary role played (ie borrowers/investees' screening without bearing the risks) and limit/prohibit inducements (payments by third parties[73]). However, the EU and US present additional, although different, restrictions in this area: the US prohibit platform's managers and main shareholders to have financial participations in the offers/issuers, while allowing the platform itself to invest in the project owners under certain conditions;[74] the ECSPR, instead,

[61] SEC crowdfunding regulation. In the US, funding portals are not subject to any minimum capital requirements, contrary to broker-dealers for which minimum net capital requirements ranging from $5,000 (when not holding clients' funds/securities) to $250,000 exist (17 CFR §240.15c3-1).

[62] US: 17 CFR §227.402(b); Securities Exchange Act Section 3(a)(80); Section 304(b) JOBS Act. See also Y Li, 'The regulation of equity crowdfunding in the US: remaining concerns and lessons from the UK', (2022) 22(2) J Corp Law Stud 265 (online 1), 7-8; Härkönen (n 21) 800-01.

[63] In the US and EU, platforms cannot provide compensation for the solicitation/promotion of offers: Art 3(3) ECSPR; 17 CFR §227.402(b); in the UK, the solicitation can be conducted only when approved by an authorised person. See Li (n 62) 25.

[64] 17 CFR §227.402(b)(2); Härkönen (n 21) 801.

[65] Hofmann (n 26) 397ff.

[66] RG 262.196.

[67] Art 16 ECSPR.

[68] 17 CFR §227.404.

[69] Art 26 ECSPR.

[70] Principle 8 and SYSC 10.1.3R. The FCA, moreover, explicitly prohibits the preferential treatment of institutional investors over retail ones (FCA, 'Interim feedback to the call for input to the post-implementation review of the FCA's crowdfunding rules', 16/13, 12, https://www.fca.org.uk/publication/feedback/fs16-13.pdf).

[71] Art 4(1) and 8 ECSPR.

[72] s912A(1)(aa) Corporations Act 2001.

[73] See EU (for routing investors to particular offers: Art 3(3)), Australia (in case of retail advice: s963A Corporations Act 2001) and UK (since 2022 banning monetary and non-monetary benefits incentivizing promotions for high-risk investments: FCA, 'Strengthening our financial promotion rules for high-risk investments and firms approving financial promotions' (August 2022), PS22/10.

[74] Eg Same conditions as offered to other investors and in exchange for the services provided: 15 USC §77d-1 (a)(11); 17 CFR §227.300(b). See Härkönen (n 21) 801. Beside this, the US do not set a general conflict of interest regime: Li (n 62) 25.

prohibits the CSP/platform to invest in project owners but allows its managers and main shareholders to do so under certain conditions[75] (while not to be a project owners themselves). Australian CSPs cannot offer to investors financial assistance to buy shares on the platform (RG 262.191).

Most jurisdictions impose on platforms the requirement of adequate risk management systems and governance arrangements (including outsourcing rules) (UK, Singapore[76], Australia).

Nonetheless, additional risk management rules for LBC exist in some countries. The UK, since the 2019 review, imposes the presence of an independent risk management function and permanent effective independent compliance function (conditional to a proportionality principle), independent internal audit function and rules on credit risk assessment. Additional and stricter rules have been introduced, in the UK, EU and Singapore, for more complex models entailing the provision by the platform of pricing or, even more, portfolio management, concerning among other things, money allocation, minimum basis and timing for credit risk assessment, portfolio composition, calculation methods, contingent funds (with very detailed rules in the ECSPR).[77]

Dispute resolution (EU, UK, Australia) and continuity arrangements, for the case of platform's failure (UK[78], EU), are another typical requirement, in alternative to business cessation plan (Singapore).[79]

Finally, requirements for certain systems and procedure might derive from some gatekeeper duties (below §4.3-4.4).

3.2. Prudential requirements

Prudential requirements used to be reserved to large and systemic intermediaries, in particular with liquidity/maturity transformation functions. Nonetheless, especially after the global financial crisis, we have witnessed to a scope extension of such requirements (eg IFD/IFR[80] in Europe).

In the UK, IBC must comply with investment firms' prudential requirements for operational risks (derived from EU IFD/IFR), while LBC have dedicated requirements: the higher between £50,000 and a percentage of loaned funds.[81] Article 11 ECSPR, requires CSPs to maintain the higher between €25,000 and ¼ of overheads of the previous year in the form of CET1 or professional insurance or a combination of the two, following a IFD/IFR-like approach (for class-3 firms but lighter).

[75] eg disclosure to clients, investors' equal treatment and access to information: Art 8(1)-(2) ECSPR.
[76] MAS expects boards member to exercise effective oversight of their operations and review policies: MAS 2021, No. 15.
[77] For UK: COBS 18.12.5R–COBS 18.12.10R; COBS 18.12.11R–COBS 18.12.17R; P Chapman, 'Crowdfunding', in J Madir (ed), *Fintech. Law and regulation* (Edward Elgar 2021) 64-89, at 75-6; Pascalis (n 37) 653. For the ECSPR: Artt 4(2)-(4) and 6(1)-(2); Macchiavello and Sciarrone Alibrandi (n 7) 52-53, 61-63, 66-69, 77. In Singapore, the use of auto-allocation tools requires platforms, in addition, to 'educate users and warn them about [the] limitations' of such systems: MAS Circular No. CMI 27/2018 (2021), No. 14.
[78] See SYSC 4.1.8A R-SYSC 4.1.8E. After the 2020/21 review, also a resolution manual is required, with the description of the management of loans, day-to-day operations and resources. See also Chapman, 74-5.
[79] MAS Circular No. CMI 27/2018 (2021), No. 9.
[80] Directive (EU) 2019/878 and Regulation (EU) 2019/876.
[81] 0.2% for the first £50 million; 0.15% for the next £200 million; 0.1% for the next £250 million; 0.05% of any remaining balance above £500 million: FCA handbook IPRU-INV 12.2. See also Chapman, 73.

Australia has a complex and articulated system: CF providers must comply with the standard solvency and net asset requirement for AFS as well as with crowdfunding-tailored surplus liquid funds and cash needs requirements (in particular, 5% of projected/actual cash outflow).[82]

Instead, the minimum operational risk requirement for Singaporean CSPs is SGD 50,000, while the US set general Net Capital requirements only for brokers.[83]

4. CLIENT PROTECTION: CONDUCT REQUIREMENTS AND DISCLOSURE

4.1. General conduct rules

Considering the typical agency risk affecting crowdfunding, conduct rules and transparency requirements are particularly important, especially to protect investors.

Most jurisdictions apply the same general conduct requirements as for investment firms. EU CSP are required to act honestly, fairly and professionally in the clients' best interests (Art 3 ECSPR), with a formula replicating MiFID II general conduct duties. More specific duties are established for more complex models: for instance, CSPs offering individual portfolio management of loans must allocate the client's investments meeting at least two investor's preferences.[84]

In the UK, IBC and – after the 2019 review – LBC providers are subject to both the general FCA handbook principles and general conduct requirements specific for CF platforms indicated in COBS (the latter actionable in Court and derived from MiFID II), with standards comparable to the ECSPR general conduct duties.[85]

US brokers and funding portal, being both FINRA intermediaries, must meet 'high standards of commercial honour and just and equitable principles of trade'.[86] Moreover, special requirements apply to CSPs: communications 'must be based on principles of fair dealing and good faith and must be fair and balanced'.[87]

Similar general conduct requirements exist also in Australia but only for collective investment schemes licensed to offer to retail investors (not for the unregistered ones, reserved to sophisticated investors),[88] whom must also be treated equally and fairly (sect 601FD-FE).

4.2. Disclosure requirements

Disclosure is at the centre of FRC regimes to reduce information asymmetry (particularly high in case of SMEs) and generally entails the exemption from Prospectus or other documents required by traditional financial regulation, while introducing certain transparency requirements for both project owners/issuers and platforms.

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[82] ASIC, 'AFS licensing: Financial requirements' RG166 (2022), 166.365ff; ASIC Corporations (Financial Requirements for CSF Intermediaries) Instrument 2017/339, https://www.legislation.gov.au/Details/F2017L01215/Html/Text#_Toc493600973; Corporations Act s912A; ASIC 2018, 262.28ff; Rajapakse (n 40) 73; ASIC (n 41).

[83] Exchange Act Rule 15(c)3-1.

[84] Among the following: maximum and minimum interest rates and maturity, range and distribution of risk, likelihood of the promised target return (Art 3(4)-(5)).

[85] Duty to act honestly, fairly and professionally in the best interest of clients: COBS 2.1.1R and Art 24(1) MiFID II (see also FCA handbook PRIN, 2 and 6); clear, fair and not misleading communications: COBS 4.2.1 R; Art 24(3) and 30(1) MiFID II (see FCA handbook PRIN, 7). See also Chapman, 75.

[86] See FINRA, 'Funding Portal Rules', 200(a), https://www.finra.org/rules-guidance/rulebooks/funding-portal-rules/200.

[87] Li (n 62) 9.

[88] Duty to act honestly and in the best interests of the members (sect 601FC) and reasonable degree of care and diligence.

As regards issuers' disclosure duties, the dissemination of a special document based on a template, with only key information about the same, the project, offering, and products, including warnings about risks is often required (EU, US), with a stress on clear and simple language (EU; Australia for EBC).

In particular, EU project owners must prepare a Key Investor Information Sheet (KIIS), then made available by CSPs to investors (even professional ones) with reference to any particular offer and even when reserved to sophisticated/professional investors. In order to focus investors' attention on the most important aspects, the KIIS must be written in a plain and a-technical language, six pages maximum, without footnotes and contain information on the project owner, his/her activity (eg including key annual financial figures risks), the offering and the products (eg key rights and price, risk mitigation) as well as several warnings about risks and the lack of traditional protections.[89] Although the platform does not take part to the KIIS preparation, it might assist the project owner (also in terms of KIIS translation)[90] and is subject to relevant (but still uncertain) 'gatekeeping' duties (see §4.3). If the platform offers portfolio management of loans, it must take care of the KIIS, focusing the information on the selection criteria, portfolio composition methods, diversification strategies, and will be directly responsible for such information (Art 24).

In Australia, in case of EBC, the special crowdfunding regime exempts from Prospectus requirements but the issuer must prepare a CSF offer document (based on a template) written in a manner that is 'clear, concise and effective,' not misleading or deceptive[91] and with specific warnings about risks and information about the company (its directors, risks, capital structure, financial statements), the offer (period, minimum and maximum amount, use of funds, and the rights of investors (cooling-off, reporting, communication facility, etc). Beyond these cases, the offer of securities (shares or debentures) requires a prospectus containing all the information relevant for an informed decision (sect. 6D), saved for small offers or offers reserved to sophisticated investors.

The US regime appears one of the strictest, requiring the issuer to use a standard format (form C) with specific information about itself (in particular, organization and risks)[92], the offering (eg intended use of the proceeds, target amount and price), the securities,[93] and investor's 48-hours cancellation right. Such obligations appear closer to mainstream finance since issuers must always include financial statements, even reviewed or certified (depending on the size). Moreover, a significant difference, compared to the EU and UK in particular, is the obligation to provide progress updates when the issuer reaches 50% and 100% of the target, unless the platform already updates investors in this regard,[94] and ongoing disclosures,[95] which might be expensive for the issuer and not particularly informative and too complex for unassisted retail investors.[96] Investors have an explicit right of action against crowdfunding issuer for omissions or fraudulent statements (sec 4A(c)).

[89] Eg the risk of loss, illiquidity and lack of return; the opportunity not to invest more than 10% of their own net worth; lack of authorities' approval, of deposit/investment guarantee schemes and of an appropriateness test: Art. 23.
[90] Artt 23(3)-(4), (13); ESMA Q&A 5.17.
[91] Schwarz (n 40) ch 6. ASIC (n 41), RG 261.132.
[92] In particular, directors and officers, and large shareholders, ownership and capital structure, business, number of employees, financial condition of the issuer and particular risks.
[93] In particular, terms/rights, including aggregated amount, how valued, risks for minority shareholders, other exempted offerings: 17 CFR §227.203(a).
[94] Ibidem. 17 CFR §227.203 (a)(3).
[95] 17 CFR §227.201-203.
[96] Li (n 62) 11; Härkönen (n 21), 806.

Interestingly, both US and Singapore prohibit to issuers to advertise the offering, except for directing investors to the funding portal.[97]

Instead, UK issuers are generally exempted from Prospectus requirements under usual exemptions (eg total consideration) and not required to prepare other documents (except what contractually required by the platforms). Similarly, in Singapore, FRC offers are generally exempted from Prospectus requirements and the offeror, although not required to prepare another type of document[98], must explicitly declare that the offer does not entail a prospectus[99] and presents resale restrictions.[100] Investors have anyway access to public company information, business report, and general meeting report.[101]

As regards CSPs' disclosure duties, these generally require key information and in plain language about the intermediary, risks, costs, main rights, selection criteria and lack of traditional safeguards (EU, UK, Australia for EBC). For instance, under the ECSP, CSPs must disclose to their clients (both investors and borrowers/investees), publishing in a prominent part of the website, information about themselves, costs and charges, project selection criteria, in addition to warnings about specific risks and the lack of deposit guarantee/securities compensation coverage (Art 24 ECSPR and annex) as well as the compliance with other requirements (reflection period for un-sophisticated investors, conflict of interests, dispute resolution: Artt 8-10). Additional specifications depend on the service offered: LBC platforms must also disclose the default rates of the past 36 months (Art 20); platforms offering credit scoring/pricing must publish also the calculation method used and specify whether they use audited financial statements for this (Art 19); if individual portfolio management of loans is offered, a description of systems and procedures deployed for credit risk assessment, the composition of the portfolio and, when a contingent fund protect investors from risks, several additional information are required (Art 6(2)-(6)); platforms operating bulletin boards must disclose their nature, loan performance and, where present, pricing methodology (Art 25).

Platform's disclosure duties appear lighter in the US: CSPs must disclose information about its compensation and the person engaging in investment promotion and merely provide investors with educational materials with simple and clear information regarding crowdfunding and its risks.[102] Furthermore, CSPs must transfer to investors all information provided by an issuer no later than 21 days before any securities are sold to the same.[103] However, some authors believe that the above-mentioned Sec 4A(c) can be interpreted extensively, potentially covering also platform operators as offerors and therefore representing a basis for their indirect liability.[104] Interestingly, the US and Australian regimes are the only ones requiring platforms to establish communication channels between issuers and investors: however, in the US, the platform should only assume a moderating

[97] Since 2021, oral or written communications with prospective investors are permitted in the US once the offering statement Form C is filed under the specified circumstances: 17 CFR §227.204. In Singapore, issuers can advertise the offers (exempted under the small offers exemption) only to pre-identified person already in contact or explicitly interested): MAS FAQ licensing, No. 3; Hofmann (n 26) 401, 407. Contrary, the ECSPR in principle allows project owner to market their own projects: ESMA 'Q&A', 5.7.
[98] Hofmann (n 26) 415.
[99] §272A(1)(b)(i).
[100] §§§272A(1)(b)(ii), (3), (8).
[101] Wisuttisak (n 25) 106.
[102] 17 CFR §227.302(b).
[103] Härkönen (n 21) 801.
[104] Li (n 62) 14-15. See also CS Bradford, 'Shooting the Messenger: The Liability of Crowdfunding Intermediaries for the Fraud of Others' (2014) 83 University of Cincinnati Law Review 371.

role to protect clients' privacy, not taking part to the conversations,[105] while in Australia the communication facility should work among companies, investors and the platform.[106]

In the UK, CSPs were only required to provide 'accurate and sufficient' information, with no specific type of document or of information. However, the FCA, having registered in market practices too much variation and incompleteness, has more recently indicated the information considered appropriate, in particular on: CSPs,[107] the authorisation, performance reports expected, costs and charges, client money safeguards, risks, with certain warnings.[108] While risk disclosure requirements for IBC derive from Art 24 MiFID II (COBS 2.2.A), the 2019 reform introduced specifications for LBC (COBS 18.12.24R), such as information about borrowers' selection and loans' assessment, price determination, portfolio composition, procedure for late payments/defaults, calculation of tax and warning about the lack of a compensation scheme. In case of basic models, where investors select the loans, warnings must be provided on the risk of platform failure and, if present, on contingent funds, together with information on ongoing disclosures. Since December 2022, a warning about the risk of losing all sums invested and a link to further information must be added for all high-risk investments, including LBC and IBC.[109] The platform must also have basic written agreement with the essential rights and obligations.[110]

In Australia, LBC platforms generally recur to managed investment funds (MIS), which can be unregistered when reserved to sophisticated/professional investors and are not subject to particular disclosure requirements. Instead, licensed schemes require a constitution and compliance plan with a description of its functioning and a guide.[111] In particular, it must present a product disclosure statement (PDS), with information on the business structure, loans offered, matching system, interest rates calculation, returns, risks (in particular from loss, concentration, illiquidity, platform), process for borrowers' assessment, fees/costs, withdrawal (if possible), protection measures, notion of default.[112] Retail clients, also benefit from ongoing and periodic disclosure, as well as disclosure of material change.[113] If the LBC platform operates instead under a personal advice model (eg a platform matching based on the person's objectives, financial situation and needs), another type of PDS is needed, with specific information regarding the characteristics of the financial product, applicable fees, risks and benefits. In case of EBC, the platform must prominently display, before it is possible for investors to apply for shares, risk warning, fees by companies or other parties, cooling-off rights (statement and how can be exercised).[114]

Singaporean platforms must, before the investor can invest on the platform, disclose the key risks and obtain the investor's acknowledgement that he/she has understood the risks of total loss, lack of resale/redemption and dividends, dilution, platform risk and lack of sufficient information.[115] LBC platforms are required to disclose also defaults and interest rates based on MAS guidelines to ensure

[105] Härkönen (n 21) 801; Li (n 62) 8-9.
[106] Ibidem, RG 262.154
[107] FCA COBS 6 and 2.2 (2023 version); Chapman, 78.
[108] FCA COBS 2.2, 2.2A; 4.5; 4.5A.
[109] New COBS 4.12A.11R; FCA, 'Strengthening our financial promotion rules for high-risk investments and firms approving financial promotions' (August 2022), PS22/10.
[110] COBS 18.12.12R, 31R, 23R-38R. Baillie (n 36) 154; McMeel (n 38) 80-81.
[111] Rajapakse (n 40) 79-80; ASIC (n 41).
[112] Part 7.9. Corporations Act.
[113] Section 1017B-D.
[114] ASIC (n 43), RG 262.147 and RG 262.149.
[115] Hofmann (n 26) 405.

comparability.[116] Licensed crowdfunding operators (especially LBC) are also expected to have procedures to handle issuer defaults and to disclose to investors different recovery options and costs, obtaining their consent in advance.[117]

4.3. Due diligence and gatekeeper role

The level of due diligence imposed on platforms is closely linked to the role as gatekeeper assigned to the same and relies also on the interpretations of legal texts and the evolution of supervisory practices.

For instance, in Singapore, MAS expects IBC operators to simply disclose the scope of their due diligence, while LBC operators not to lend to a borrower with past due (saved for reasonable and disclosed justifications).[118] In the UK, although the law requires platforms to simply disclose to investors the level of due diligence performed, the FCA has clarified that a violation of the general obligation of care, skill and diligence and best interest has to be assumed when the platform has not carried enough due diligence to support the information material provided to clients. Moreover, LBC platforms must verify project owners' statement on future commercial success.[119]

US law does not expressly state due diligence obligations for CSPs[120] except for the duty to ensure systems and procedures to reduce the risk of frauds,[121] checking the background and securities enforcement regulatory history of the issuer's officers, directors and main shareholders. Anyway, the platform is liable for the violation of the duty to obtain a reasonable basis for believing that the issuer is in compliance with its relevant rules, being allowed to rely on issuers' representations unless there are reasons to question the reliability (with the consequent duty to remove the offer).[122] The SEC has recently won a case against a platform for failing this to address certain red flags and reduce the fraud risks on investors.[123]

The ECSPR requires the CSP to simply screen issuers for certain criminal and AML/CT records (Art 5 ECSPR). However, at the same time, it needs to have systems to ensure the completeness, clarity and the 'correctness' of the project owner's KIIS, having the power to suspend or even cancel the offer if it identifies an omission, mistake or inaccuracy which is not promptly corrected (Art 23(8), (11)-(12) and to request KIIS updates informing investors; see above 4.2). The first duty has been referred, in ESMA's Q&A, to 'inaccurate or misleading information' but specifying that the project owner is solely responsible for the information in the KIIS, 'unless those omissions are the direct result of inadequate procedures' by the CF provider 'in the collection of this information made

[116] MAS, 'Circular No. CMI 27/2018 - Controls and disclosures to be implemented by licensed securities-based crowdfunding operators' (rev. 2021), No. 4, https://www.mas.gov.sg/-/media/mas/regulations-and-financial-stability/regulations-guidance-and-licensing/securities-futures-and-fund-management/regulations-guidance-and-licensing/circulars/cmi-272018-controls-and-disclosures-implemented-by-licensed-sec-based-crowdfunding-operators-210310.pdf.
[117] Ibidem, No. 5-6.
[118] MAS Circular No. CMI 27/2018 (rev. 2021), No. 11.
[119] Chapman, 81.
[120] Ibidem.
[121] 17 CFR §227.301.
[122] 15 USC 77d-1(a); 17 CFR §227.301(a).
[123] The red flags consisted in the criminal records of issuers who diverted collected funds for personal benefit: *SEC v Shumake, Civil Action* No 2:21-cv-12193 (ED Mich Filed September 20, 2021), final judgement 23 dec. 2021, https://www.sec.gov/litigation/litreleases/2022/judgment25298-trucrowd.pdf; SEC, 'SEC Obtains Final Judgments Against Crowdfunding Issuer CEO and Registered Funding Portal and Its CEO", Litigation Release No 25298 (January 3, 2022), https://www.sec.gov/litigation/litreleases/2022/lr25298.htm. See Härkönen (n 21) 800, 806.

available in the KIIS':[124] the liability regime established at national level will ultimately set the level and intensity of platforms' gatekeeping role.[125] .

On the extreme side of the spectrum, Australian platforms are attributed an explicit role of gatekeepers performing specified types of due diligence on the companies and offers[126]: in addition to identify the company and verify whether eligible, they must reasonably check if the offer document contains the required information and, under a strict liability standard, if this is clear, concise and effective. They have also the duty to inform the company and remove the offer where they are not satisfied with the identity check or have reasons to believe that the officers/directors do not have good fame/character or the company knowingly engaged in omissive or misleading/deceptive conduct.[127] They respond for breach of such gatekeeping duties, where no systems/arrangements for conducting the same are in place or the offer document is deceptive and they had reasons to believe so (RG262.192).

4.4. Investor protection: special measures

Some jurisdictions have introduced additional protections, such as investor tests, cancellation rights or caps on investors' commitments.

a) Investor tests

The UK requires platforms to check that the client has sufficient knowledge and experience to understand the risks. FCA guidelines, since 2019, differentiate such assessment between IBC and LBC. In particular, for IBC, the assessment should take into account the type of service, the transaction, familiar investments, nature, volume and frequency of client investments and period, level of education and profession. For LBC, platforms must ensure that the client has enough knowledge to understand the nature of contractual relationship with the borrower and the firm, the exposure to credit risk, capital at risk and absence of a compensation scheme or comparability with deposits, characteristics of agreement/portfolio, risk diversification measures, contingent fund, illiquidity risk, role of platform and platform risk (COBS 10.2.9G). In 2022, appropriateness rules for high-risk investment (crowdfunding included) have been reinforced: in case of negative result, the investor must wait at least 48 hours before re-taking the test.

Similarly, in Singapore, CSPs must assess whether potential investors have the financial competence (knowledge/experience, based on their education or work in finance or previous investments) or are suitable to invest in crowdfunding given their investment objectives and risk tolerance.[128] In case platforms provide advice (with a CMS or FAA license), they must issue a reasonable recommendation based on sufficient relevant information about the investment and a good understanding of the client's investment objectives and financial situation.[129]

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[124] ESMA, 'Q&A', 5.2. See also 5.9 (which seems to set a stricter standard): '[…] The CSP maintains the responsibility to have adequate procedures in place to identify cases where inaccurate or misleading information may be provided by the project owner and to take appropriate action. The requirement to verify the completeness, correctness and clarity of the information contained in the KIIS should apply both (i) prior to the publication of the KIIS on the crowdfunding platform CSPs operate or manage and (ii) on an on-going basis afterwards for the duration of the crowdfunding offer, where new information comes to light that would give sufficient reason to believe that the KIIS document might be incomplete, incorrect or unclear'.

[125] Macchiavello (n 7) 61.

[126] Reg 6D.3A.08(2)-(4).

[127] ASIC (n 43), RG 262.130ff; RG262.145; RG262.172.

[128] Hofmann (n 26) 404.

[129] Financial Advisers Act §25; Hofmann (n 26) 406.

The ECSPR, instead, reserves, only to non-sophisticated investors,[130] special measures: an entry-knowledge test aimed at assessing investors' knowledge and previous experience with crowdfunding and early-stage companies, therefore similar somehow to an appropriateness test but pertaining to crowdfunding services in general (instead of a particular financial instruments) and at a preliminary stage.[131] Moreover, platforms must also make available to investors a system to simulate their ability to bear losses, calculated as 10% of their net worth, based on certain information. In case of a negative result in either/both tests, investors can nonetheless still invest after a simple acknowledgment (Art 21(5)-(6)).

Lighter requirements exist in the US and Australia: US platforms must obtain from investors a declaration that they understand the risk of losing the entire investment and they can bear such a loss and ensure they complete a questionnaire after reviewing the relevant educational material.[132] However, if brokers offer investment advice to retail investors (which funding portals cannot provide), they are subject to the suitability duty. Australian CF providers, must obtain from retail investors, before the investment, an acknowledgment of risks.[133]

b) Reflection period/cancellation right

Online transactions, being faster and easier to be made, might be more dangerous: EU law generally allows consumers to have second thoughts.

The FCA (UK) has considered applicable to the initial contract with the platform the 14-days cancellation right derived from the Directive on distant financial services (not applicable in case of fluctuations)[134] but, since 2023, a 24-hours cooling-off period (starting with investor's access to offers) applies to all high-risk investments (crowdfunding included), during which, however, other procedures (eg AML/CT checks, appropriateness test, etc) can be conducted. Similarly, a reflection period right is recognised to EU non-sophisticated investors (4-days) and Australian investors (5-days). Instead, in the US, investors have the right to cancel the order until 48-hours before closing.[135]

c) Maximum offer size and investment limits

The ECSPR sets at €5 million (including all offers exempted from the Prospectus under the small/private offers exemptions) the maximum threshold for crowdfunding offers. Instead, it does not set investment limits but in case of investment above €1,000 or 5% of the investor's NW, platform

[130] Sophisticated: legal entities meeting one of the following conditions: a) at least €100.000 own funds; b) turnover of at least €2 million; c) balance sheet of at least €1 million; 2) natural persons meeting at least two of the following conditions: a) personal gross income of at least €60.000 or a financial instrument portfolio (including cash deposits and financial assets) exceeding €100.000; b) professional experience in the financial sector in a position requiring knowledge of the transactions or of the services envisaged or an executive position in the legal entities listed under 1) for at least 12 months; c) operations of significant sizes on the capital markets, at an average frequency of 10 per quarter, over the previous four quarters. ECSPs must take reasonable steps to ensure that investors effectively meet such requirements but can approve the request unless they have reasonable doubt that the information provided is correct (see annex II).

[131] However, the final version of the ECSPR requires platforms to collect information also about investors' investment objectives and financial situation (*cf* suitability test), which sounds incoherent with the evaluation described above and questionable even under a GDPR perspective, although financial situation information is useful for the loss simulation test (Art 21(1)-(4)).

[132] 17 CFR §227.303(b). Härkönen (n 21) 800; Li (n 62) 8.

[133] Reg 6D.3A.07; RG 262.188.

[134] FCA, 'The FCA's regulatory approach to crowdfunding over the internet, and the promotion of non-readily realisable securities by other media', (2014), PS14/4, https://www.fca.org.uk/publication/policy/ps14-04.pdf; Baillie (n 36) 154; Chapman 84.

[135] With offers open for at least 21 days. See Härkönen (n 21) 804.

must simply issue a warning and receive investor's explicit consent and evidence of understanding (Art 21(7)).

Singapore and the UK do not set either maximum offer threshold (beside general small offer exemptions from Prospectus) or investment caps. However, the UK presents restrictions on financial promotions: direct offers of unlisted securities (non-readily realisable securities) or P2P investments (agreements or portfolios) cannot be directed to retail clients unless they are certified or self-certified sophisticated investor or HNWI or receive regulated advice or are a restricted investor (ie no >10% net worth in 12 months)[136] and, anyway, only if they pass the required test (see above §4.4.a: COBS 10-10A; COBS 10.1.2R).[137]

The US limit instead both issuers' requests (up to US$ 5 million in 12 months; raised in 2021)[138] and investors' commitments. In particular, non-accredited investors[139] cannot invest, depending on the category and wealth, more than: if the annual income or net worth (NW) is less than $124,000, the greater of $ 2,500 or 5% of (the greater) of the investor's annual income or NW; if the non-accredited investor's annual income and NW are equal to or more than $124,000, 10%. Platforms can ensure compliance with these limits, having reasonable basis for relying on the investor's representations.[140]

In Australia, retail investors cannot invest more than A$10,000 per year and per company offer and CSPs must have system and procedures to ensure compliance.[141] However, no limit is placed on the total number of offers in which they can participate.[142]

d) Client money protection measures and exclusion from compensation schemes

All regimes tend to entail client money protection measures: the ECSPR does not allow platforms to hold clients' money, unless they also obtain a PSD2, bank or equivalent license. Similarly, in the UK, client money protection measures apply to LBC platforms, requiring to have the money secured in segregated bank account and never obtain the ownership of client money.[143] Again, US funding portals cannot hold client money, contrary to brokers; moreover, the law requires that the funds are transferred to the issuer only if and when the target amount is reached (otherwise, the funds must be returned to investors within 5 days).[144] In Singapore and Australia, CSPs must segregate and place all monies they receive from customers into trust accounts and assets into custody accounts.[145]

Crowdfunding, in fact, are generally excluded from existing compensation scheme: this is the case under the ECSPR and in the UK for LBC (while IBC, being regulated under MiFID II, is instead covered). US funding portals are not members of the Securities Investor Protection Corporation,

[136] FCA handbook COBS 4.12A (2022 version). FCA has also improved client categorization, requiring, for instance, declarations to use plain English and to support relative categorization (eg clients must state their indicative income); moreover, CSPs must look for supporting evidence.
[137] McMeel (n 38) 78-79; Baillie (n 36) 154-55.
[138] Crowdfunding securities cannot be re-sold for 12 months, unless through registered offerings, to accredited investors or investor family members: 15 USC §77d-1(e); 17 CFR §227.501.
[139] Accredited investors, not covered by investment limits are: financial companies, companies with total assets in excess of $5 million, and natural persons with a net worth of $1 million or with earned income above $200,000 (or $300,000 together with a spouse) in previous 2 years or holding in good standing one or more professional certifications or designations or credentials: 17 CFR § 230.501. See Härkönen (n 21) 805; Li (n 62) 6.
[140] 15 USC §77d(6); 15 USC §77d-1(a)(8); 17 CFR 227.303(b). See Härkönen (n 21) 803.
[141] MAS RG 262.190.
[142] Schwarcz (n 40) ch 6.
[143] Chapman, 82.
[144] 17 CFR §227, 402(a); Chapman, 82; Härkönen (n 21) 801, 804.
[145] Hofmann (n 26) 407.

contrary to brokers, which therefore can ensure coverage to their customers from loss of cash/securities up to $500,000 if they become insolvent.[146]

e) Additional rules: records and ADR

Crowd-investors commit small sums to each issuer and, sometimes, through a certain platform: filing a claim for small amounts appears expensive and creates collective action problems. Therefore, ensuring investor fast and cheap access to records and alternative redress systems is particularly important.

Both the ECSPR and the US regime require platform to maintain for 5-year the relevant records.[147] Recourse to ADR or complaint systems is the common standard: in the UK both IBC and LBC are covered by the Financial Ombudsman service.[148]

4.5. Other clients: borrower protection

The type of platforms' client receiving the highest protection is the investor. Nonetheless, especially in case of LBC, some jurisdictions recognize protection also to the client requesting the financing, although the assimilation of loans with investments have favoured the focus on investor protection and, in part, stability, while putting aside investees/borrowers' protection.

In the UK, the rules implementing the EU Consumer Credit Directive (CCD) and the UK CCA 1974 (unfair relationship regime) apply when the borrower is an individual (consumer) or relevant person (ie sole trader or small partnership or other unincorporated body), borrowing no more than £25,000 and not exclusively for the purposes of the borrower's business.[149] However, the full set of rules only apply if also the lender is a professional one (eg institutional investors): pre-contractual credit information using a certain form, content and execution of the credit agreement, as well as CONC rules about assessment of credit-worthiness and affordability,[150] adequate explanations of key features of lending arrangements before signing the contract, notices of sums in arrears and default consequences.[151] Instead, in case of non-commercial lenders, specific CONC rules apply for P2P lending and to platforms as regards creditworthiness assessment (CONC 5.5A) and 14-days withdrawal right (CONC 11.2).

In Australia, only the need of a credit provider license (see above §2.15.) brings also the responsible lending obligation of Chapter 3 National Credit Act, including a creditworthiness assessment with reasonable inquiries about the consumer's requirements and objectives and reasonable steps to verify the information provided by the consumer as well as the provision of a credit guide with information about the credit providers, costs and dispute resolution processes, interest rates caps. In case of either a consumer or a business borrower, misleading/deceptive communications and harassment/coercion practices in collection are prohibited.[152]

[146] Restrictions exist on brokers' use of clients' securities: see FINRA's customer protection rules (Rule 4330).
[147] Even of the communications channels (US): 17 CFR §227.303(c) and §227.404. See Härkönen (n 21) 802.
[148] McMeel (n 38) 76-77.
[149] Baillie (36) 153.
[150] Ibidem; McMeel (n 38) 82.
[151] Baillie (n 36) 153.
[152] ASIC (n 41).

The ECSPR protects (business) borrowers only through the general conduct duties, website disclosures and complaints handling requirements (referred to 'clients': see §4.1-4.2). Consumer borrowers in P2P loans (outside the scope of the ECSPR) might be protected in the future by the revised CCD.

5. FINANCIAL CRIME PREVENTION: ANTI-MONEY LAUNDERING (AML)

While the UK identifies CF platforms as obliged entities under AML rules[153], the ECSPR refer to the payment service providers necessarily involved in the transaction the burden to verify parties' identities and other related obligations.

In the US, only brokers are so far subject to the Bank Secrecy Act (BSA) and therefore to AML obligations (eg reports of suspicious activity, procedures for ongoing customer due diligence, response to information requests from the Financial Crimes Enforcement Network).[154] However, also funding portals, being FINRA operators, must identify their clients (FINRA 'know your customer' requirement). [155]

In Australia, crowdfunding platforms are not explicitly listed as 'designated service' covered by the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Chapter 6) but this might apply in case the platform anyway provides a financial service or is considered 'operating a network of persons where 'the persons […] provide a designated service' (item 32A).

6. CONCLUSIONS

Regulatory approaches in the jurisdictions analysed range from the application of traditional financial regulation rules (at most with small adaptations: US and Singapore), to more articulated and hybrid regimes (Australia, UK, in particular for LBC), to, finally, *ad hoc* special regimes (EU), reflecting a different ranking in regulatory goals.

Such adaptations or special rules apply to only certain models and services (EU, US, Australia), leaving more complex ones subject to stricter traditional or special regulation (UK, EU, US, Singapore), also to ensure proportionality, competition and a level-playing field. Moreover, CSPs are often regarded as limited/specialized intermediaries, limiting the use of indirect/managed models (eg SPVs and investment funds: EU, US) or solicitation/advice (US, EU, Singapore). Only few jurisdictions at least mention more recent crowdfunding models (securities tokens, invoice trading, real estate crowdfunding: Singapore and EU). All require CSPs to obtain an authorization/registration, with requirements similar to traditional financial intermediaries' ones but lighter and less detailed.

All jurisdictions seem to focus their regimes on general conduct duties (close to traditional intermediaries'), conflict of interest (even stricter) and disclosure requirements for both issuers (specific on particular offers) and platforms (general on crowdfunding features and risks). In particular, warnings requirements are widespread and tailored to the special crowdfunding features/risks, as well as templates of informative documents with plain language and key

[153] See also FCA handbook SYSC 3.2.6.
[154] FINRA, '2022 Report on FINRA's Examination and Risk Monitoring Program' (2022); 31 CFR §§ 1023.100 et seq; 17 CFR § 240.17a-8; FINRA Rule 3310; LW Rosen and RS Miller 'The Financial Crimes Enforcement Network (FinCEN): Anti-Money Laundering Act of 2020 Implementation and Beyond' (2022), 8, https://crsreports.congress.gov/product/pdf/R/R47255.
[155] FINRA (n 154).

information. Nonetheless, the US put the main disclosure burden on issuers with obligations closer to traditional ones (financial statements and ongoing disclosure), while the UK and Singapore on platforms; the EU and Australia on both; finally, Singapore presents the lightest disclosure regime (for EBC platforms, only warnings and client acknowledgement). Anyway, additional requirements exist for certain LBC models (EU, UK, Singapore) or have been added over time to respond to market practices (UK, moving to principle-based and light touch regulation /supervision to more rule-based and hard-touch one).

Investor protection measures sometimes involve investor tests close to the traditional appropriateness one (UK and Singapore) but the ECSPR has created a special one, resulting in lighter (and, likely, less effective) protection, being closer to a simple acknowledgment (as in US and Australia). Reflection periods for investors and ADR/redress requirements are progressively common, contrary to AML/CT requirements.

Many jurisdictions set investment limits or restrictions to financial promotions for retail/un-sophisticated investors but the thresholds set by ECSPR only trigger warnings and relative investor acknowledgement. In principle, CSPs are not bound by due diligence requirements, having simply to disclose their screening procedures. However, national supervisors have over time specified their expectations in this regard, creating the grounds also for private/public enforcement (UK, US). In certain jurisdictions, CSPs have been assigned an explicit gatekeeping role in EU (uncertain) and Australia).

Instead, organizational and prudential requirements, although often present, play a less relevant role. Finally, such regimes do not contain resolution rules but continuity arrangements/cessation plans are generally required.