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EXECUTIVE SUMMARY

The objective of this report is to provide a **state of play of the crowdfunding industry** in Europe with a particular focus on equity-based crowdfunding and its regulatory aspects, providing initial concepts for self- or co-regulation of the sector.

The landscape of crowdfunding models can be grouped into two families: the **non-financial return models** (donation, reward or pre-selling) and the **financial return models** (equity or lending) which are all very different in terms of characteristics for the campaign owners and campaign backers. Europe has a scattered landscape of different models and within each model several variants exist, especially in the case of equity-based crowdfunding. The report focuses on equity-based crowdfunding on which the impact of regulation is most complex and demanding compared to the other crowdfunding models.

The global crowdfunding market has grown substantially over the past few years and a **large worldwide potential for crowdfunding is expected** to materialise in the next decade. The development and growth on a national level varies widely and depends on many factors situated in the demand, supply or cultural aspects.

Equity-based crowdfunding interacts in many ways with the established financing sector as a complementary or alternative financing method in the early stage financing market. The instrument succeeds in attracting funds from non-traditional investors and a new type of business angels emerges. Not surprisingly, the traditional actors are starting to look at this form of crowdfunding as well, with business angel networks increasingly using crowdfunding-alike technology to organise their network and investment syndicates, but also with venture capital investors actively engaging on platforms. Currently, the latter group of investors still see complications for follow-on investments after a crowdfunding round, but this is starting to change.

R&D close to commercialisation can enjoy crowdfunding by attracting seed equity financing or most commonly by pre-selling products or services on a non-financial crowdfunding platform. Crowdfunding of pure R&D activities is not very popular yet and the potential for it remains to be seen.

The **success factors for a crowdfunding campaign** are a complex set of interdependent drivers that can be categorised into 4 main groups: the platform characteristics, the campaign characteristics, the communication efforts and the investment case (only for equity and lending). A recipe for building an effective campaign cannot be given, however, committing sufficient resources to enable as many success factors as possible will certainly increase the likelihood of success.

Crowdfunding is a relatively **new funding instrument with a highly dynamic market** under continuous evolution. A few trends were identified such as the objective of established platforms to grow beyond their national borders. Secondly, most crowdfunding models are attracting the interest of well-known and trusted consumer brands who are starting to embrace this sector. Thirdly, institutionalisation of the sector, driven by traditional financial services actors, is expected. Lastly, new market segments will get challenged by crowdfunding actors, for instance the real estate sector and possibly the insurance industry.

European regulation, such as the Prospectus Directive and MiFID, provides most of the necessary building blocks for Member States to sufficiently regulate the sector. It is the **Member States' authority to translate the applicable European directives into national regulation or guidelines**. The wide array of instruments in equity-based crowdfunding is driven by the differences in national regulations. Each basic type of equity-based crowdfunding comes with variants offering different rights to the investors or liabilities to the investee. Contrary to what one would expect, fundraising by the means of issuing equity directly to the investor, is not the most common financing instrument brokered on the equity-based platforms.

Some EU Member States have implemented or started to implement national regulation or guidelines specifically applicable to financial forms of crowdfunding, triggered by a developing crowdfunding scene in their country. The current national regulations, aimed at enhancing the protection of retail investors, are quite diverse and form a barrier for platforms to operate cross-border.

On a global level, other countries' governments are also seen to develop adapted regulation to equity-based crowdfunding. The US authorities are in process of implementing a federal regulation, but delays have triggered individual states to publish intrastate regulations. Australia, which has seen an early success case of equity-based crowdfunding, has recently published a new regulation specific to equity-based crowdfunding. Japan or South Korea have similarly published or prepared regulation and also China considering regulation for equity-based crowdfunding.

A scorecard for equity-based crowdfunding could help regulatory stakeholders to monitor the market development and potentially assess the impact of new regulations over time. Four key groups of KPIs are proposed in this report: the market demand, the maturity of the regulatory framework, the supply of intermediary services and the supply of capital.

The EU institutions are taking various steps to support the development of crowdfunding as a means to spur economic growth whilst safeguarding the interests of retail investors. This report aims to

contribute to this effort and reflects the views from stakeholders from within and outside the crowdfunding sector on **various regulatory concepts** related to the non-financial and equity-based crowdfunding models. An enhanced regulatory framework is deemed to be beneficial to all stakeholders in these segments.

Currently, limited evidence of fraud or abuse is known for the non-financial return models, as it is inherently self-regulated by the characteristics and mechanisms of the model itself. Wisdom of the crowd, a relatively short feedback cycle and the public nature are limiting the potential of fraud. A **code of conduct** could further enhance transparency and leverage the trust-building between the campaign backer, campaigners and the platform.

The regulatory framework for the equity-based model needs to evolve to overcome the lack of transparency and differences between markets. A **quality label** could serve as an effective solution to address some issues in this model whilst improving investor protection in the near term. The EU could be instrumental in providing a forum for all actors in order to achieve this objective. In addition, the growth of the market could be spurred by a cross-border harmonisation effort, potentially driven by European industry associations and national authorities.

ABSTRACT

The objective of this report is to provide a state of play of the crowdfunding industry in Europe with a particular focus on equity-based crowdfunding and its regulatory aspects, as the impact of regulation on this model is most complex and demanding compared to the other crowdfunding models. After detailing the different crowdfunding models and introducing some of its variants, market trends in the sector and the potential of crowdfunding for R&D are discussed. The success factors of a crowdfunding campaign and the interaction of crowdfunding with other actors in the finance market are analysed. Furthermore, the report details the regulatory aspects related to equity-based crowdfunding from a European, national but as well international perspective and a legal perspective on each variant of equity-based crowdfunding is given. The report provides an initial consideration for a scorecard aimed at monitoring the market development of equity-based crowdfunding including an assessment of the regulatory framework. Lastly, the report provides initial concepts for self- or co-regulation in the sector in order to spur the development of the industry, whilst enhancing consumer protection and transparency.

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