

A Comparative Overview of Crowdfunding Regulations in Australia, the UK, the European Union, and the USA.

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Abstract

Crowd funding has become a major means of financing of small-scale entrepreneurial ventures and star-ups. The world now more than ever needs to fund projects which are environment friendly and innovative. Mostly, startups face the **challenge** of scalability and hence are not able to attract investments from big financial institutions and venture capitalists. Crowdfunding can become a major tool for financing such innovative startups and give them the flexibility of growing at their own pace without the pressure of achieving quick profitability. This paper tries to compare the crowdfunding regulations of the some of the developed countries like the USA, Australia, the EU, and the UK which have the highest concentration of crowdfunding projects and platforms in the world. There is much to learn from the regulations in these countries that how the financial power of the masses can be used to boost the economic well-being of a country by boosting entrepreneurship at a small level.

Keywords: Crowdfunding, JOBS Act 2012, Crowdfunding regulations, entrepreneurial funding.

Introduction:

Crowdfunding has emerged as a popular method for raising capital, enabling entrepreneurs, artists, and innovators to gather financial support from a large number of individuals via online platforms. However, as this fundraising method gained traction, concerns regarding investor protection, fraud, and regulatory oversight came to the forefront. In response, governments around the world have implemented crowdfunding regulations to strike a balance between fostering innovation and safeguarding the interests of investors. This paper explores the key aspects of crowdfunding regulations and their impact on the global financial landscape.

Defining Crowdfunding:

Crowdfunding refers to the practice of raising funds from a large number of individuals, often through online platforms, for a specific project or venture. It allows entrepreneurs to access capital without relying solely on traditional funding sources such as banks or venture capitalists. Crowdfunding typically involves four

main models: donation-based, reward-based, debt-based, and equity-based crowdfunding.

Investor Protection Concerns:

Crowdfunding, while providing opportunities for innovators, also presents certain risks for investors. The absence of regulatory oversight may expose individuals to potential fraud, misrepresentation, or inadequate disclosure of information. Due to the nature of online platforms, it becomes essential to establish rules that protect investors from unscrupulous activities and ensure transparency in crowdfunding campaigns.

Regulatory Frameworks:

Governments worldwide have introduced crowdfunding regulations to mitigate risks and promote investor confidence. These regulations primarily focus on the following aspects:

a. Disclosure Requirements: Crowdfunding regulations often mandate clear and accurate disclosure of information about the project or venture seeking funding. This includes details about the business, financial statements, risk factors, and the purpose of the funds raised. Robust disclosure requirements ensure transparency and help investors make informed decisions.

b. Investment Limits: To protect investors from excessive risk exposure, crowdfunding regulations commonly impose investment limits. These limits set a maximum amount an individual can invest in a single crowdfunding campaign or within a specific time period. By preventing individuals from overextending themselves, investment limits aim to safeguard investors' financial well-being.

c. Platform Registration and Due Diligence: Regulators often require crowdfunding platforms to register and adhere to specific standards. Platforms are expected to conduct due diligence on the projects or ventures listed on their platforms, ensuring that they meet certain eligibility criteria. This scrutiny reduces the likelihood of fraudulent or illegitimate campaigns.

d. Investor Eligibility and Education: Some jurisdictions impose restrictions on who can participate in crowdfunding campaigns, limiting access to sophisticated investors or individuals meeting certain income or net worth thresholds. Moreover, regulatory frameworks emphasize investor education to ensure that participants understand the risks involved and make informed investment decisions.

Regional Variations in Crowdfunding Regulations:

Crowdfunding regulations vary across jurisdictions, reflecting differences in legal frameworks, financial systems, and cultural contexts. For instance:

a. United States: The Jumpstart Our Business Startups (JOBS) Act of 2012 introduced significant changes to crowdfunding regulations in the U.S. It established rules for equity-based crowdfunding, allowing non-accredited investors to participate in private securities offerings through registered online platforms.

b. European Union: The EU introduced the European Crowdfunding Service Providers (ECSP) Regulation in 2020, creating a framework for crowdfunding service providers to operate across member states. This regulation aims to facilitate cross-border crowdfunding while ensuring investor protection and harmonizing regulatory standards.

c. Asia: Countries like Singapore and Japan have implemented crowdfunding regulations to foster innovation. Singapore's regulatory framework focuses on providing a conducive environment for fintech startups, including crowdfunding platforms. Japan has established regulations to govern both donation-based and securities-based crowdfunding, enhancing investor protection and fostering market growth.

In the subsequent sections of the paper, we explore the nuances of the crowdfunding regulations of the USA, Australia, the EU, and the UK which have the highest concentration of crowdfunding projects and platforms in the world.

Country Wise Overview Of Crowdfunding Regulations

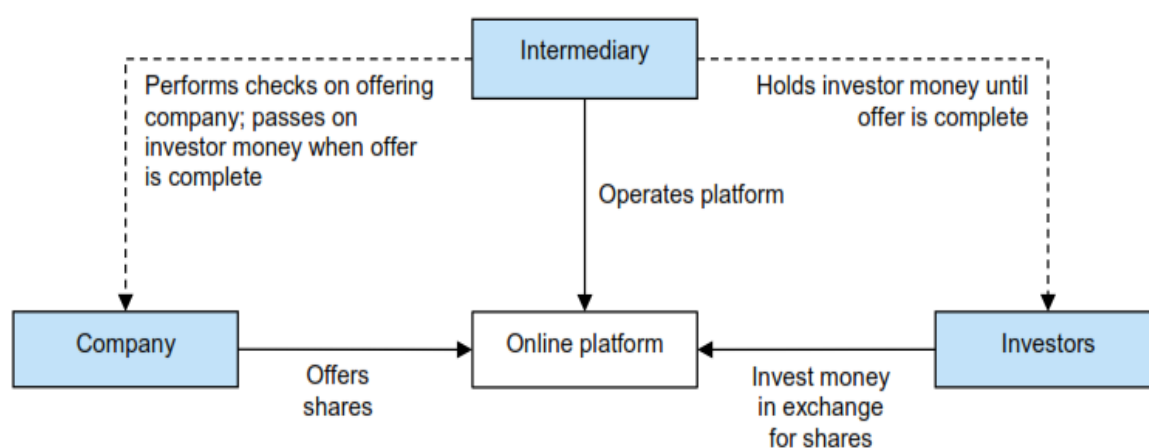
1. Australia

The Australian Securities and Investment Commission (ASIC) issued regulatory guidelines for crowdfunding on October 18, 2018 - '**Regulatory Guide 261**' (RG 261) - **Crowd Sourced Funding: Guide for Companies**. The guide offers comprehensive details regarding the eligibility of companies seeking funding through crowdfunding by offering shares under the Australian crowd-sourced funding regime as stated in the Australian 'Corporations Act' including the details of obligations and disclosures along with reporting, auditing and corporate governance required for making the offer. Australia as of now has no clear legislation regarding debt crowdfunding, therefore this section will deal with equity crowdfunding only.

As per RG 261.1 - "Crowd-sourced funding involves a company raising funds—usually through an online intermediary—from a large number of individual investors who make relatively small financial contributions to the company." (ASIC, 2018).

RG 261.2 - The regulations apply only to the equity-based crowdfunding (even though there are other types of crowdfunding) wherein the company seeking funding raises it through the issue of ordinary equity shares in return for a '*relatively small cash investment*'. The AISC explains the process of crowd-sourced funding through the following flowchart.

Figure 1: How Equity Based Crowd-sourced Funding Works?



Source: (AISC, 2018) Figure 1, Page 5

As illustrated above, the intermediary has a very important role to play as it is responsible for establishing the authenticity of the company seeking funding and bridges the gap between the investors and the company. The intermediary or the crowdfunding platform is responsible for holding the money till the offer is complete and then passes it onto the company and the shares to the investors, much like the merchant bankers to an IPO (Initial Public Offering) do.

RG 261.3- The CSF (Crowd-sourced funding) is usually a low-cost funding option for start-ups, small or medium unlisted public or proprietorship enterprises which do not have a proven profitable track record due to them being in a developmental phase but have the potential to succeed and become profitable in future. It reduces the burden of regulatory requirements for making an initial public offering which requires ensuring adequate protection for retail investors.

RG 261.4- CSF is highly speculative and the investor is therefore at the risk of losing his entire investment resulting in a total loss. It specifically warns that unlike the regular share markets the investments done through CSF may be *completely illiquid* making it impossible for the investor to exit the company.

1.1 Regulating CSF:

According to the amended CSF regime (2017) included in Part 6D.3A section 738H (which defines eligibility of CSF company) of the Corporations Act 2001 (Parliament

of Australia, 2017), unlisted and proprietary companies with *less than* \$25 million (Australian dollars) in consolidated assets and annual revenue with Australia as their principal place of business and with majority of the board of directors residing in Australia, are eligible to make offers of ordinary shares to retail investors using a CSF document via licensed CSF intermediary platform. The eligible companies are allowed to raise up to \$5 million (known as 'Issuer Cap') in a 12-month period as per the CSF guidelines. The retail investors have an investment cap (also known as the '*investor cap*') of \$10,000 per company in the 12-month period as mentioned above. The investor can recall their investment from the CSF within five days of applying for investment. A prescribed warning detailing the general risk associated with the investment must be provided in the CSF offer document provided by the company. The CSF platform should also issue a similar statement of risk exposure. The investor must provide acknowledgement of reading and understanding the investment risk before applying for shares. In case of any correction or addition of new information to the CSF offer document, which may adversely affect the decision of the investors, all investors can withdraw their applications within fourteen days and the application money is refunded. CSF offers can be advertised as per guidelines provided in subsection 738ZG (1) but can be offered only through a licensed CSF intermediary platform. According to section 738L of the amended act the CSF offer of a company can be made through only one CSF platform and the offer document must comply with the provisions given in section 738J and the CSF company should not be seeking funding simultaneously during the same period of time from various other CSF intermediaries. Further section 738N states details regarding when an offer is '*made, open, closed, suspended and complete*'. A CSF offer is made when it is first published on the CSF platform, it is open during the subscription start and end date, closed- on the end date, suspended- if a defective information comes to light which is adverse to the compliance norms of the offer document, and complete- if the period of 3 months which is the maximum period for the subscription to be open starting from when the offer was made ends; minimum subscription amount has been achieved within the stipulated time or all timelines within which the application can be withdrawn have expired.

1.2 Responsibility of the Intermediaries:

The AISC Act 2001, considers CSF or crowdfunding as a financial service and the CSF platform as financial service provider if it fulfils all aspects and roles of a CSF as stated in Part D.3A of the Act and therefore makes the CSF intermediary responsible for checking the authenticity of the company seeking CSF. The intermediary has been entrusted with various roles to safeguard investors against fraudulent CSF schemes. Some of the important responsibilities of a CSF intermediary are as follows:

- a) It acts as a '*gatekeeper*' by conducting checks on the compliance and information provided in the offer document by the CSF company. Failure to comply would result in offence and will be subject to legal action under subsection 1311(1) of the amended CSF regime which is an offence of strict liability.
- b) The CSF intermediary should not publish the offer document until and unless it is fully satisfied with the information provided in the offer document provided by the CSF company. In case any issue comes to light after the publication of the offer, the intermediary should immediately suspend the offer (Section 738N).
- c) The CSF intermediary should ensure that the CSF company or any party related to the company have no more than one offer open at any one given time (i.e. during the period when the offer is open) on any other platform.
- d) The CSF intermediary should always provide a prominent, general forewarning regarding the risks associated with the investment on the offer platform, both, during open and suspended time periods of the offer document.
- e) The CSF intermediary should ensure that the subscriber should complete an acknowledgement regarding compliance and regulations while pursuing the application for subscription of the offer; failing which the application by the retail client is to be rejected. Also, the CSF intermediary must ensure that no applications are accepted if the offer is closed or suspended.
- f) The CSF intermediary should ensure that a communication facility is always available for the retail investors or clients to cater to any queries regarding the offer document, the CSF company or the intermediary itself during the offer period. Further the intermediary must ensure that the queries must be answered by '*an officer, employee or agent*' (subsection 738ZA (6)) of the company making the CSF offer or the intermediary on which the offer is published. The posts regarding queries and their answers should be visible to all.
- g) The CSF intermediary should ensure that the retail clients know about the method and right to withdraw application as stated in section 738ZD of the Act.
- h) The CSF intermediary should clearly state the fee it charges from the CSF company making an offer and any direct or indirect interests it may have in the company making the offer regarding the intermediary's intent to acquire the company or a related party of the company. Failure to disclose this information will be treated as an offence.
- i) The CSF intermediary is responsible for holding on to the money till the subscription offer is either complete, suspended or the client asks for withdrawal. If the offer is complete the CSF intermediary will pass on the money to the CSF company making the offer; the CSF intermediary will refund the money if the offer is suspended (permanently) or the subscribers application has been rejected due to any reason (noncompliance, close of offer etc.) or if the client applies for withdrawal from the offer within the stipulated time period (also known as *cooling-off rights*) of five business days after the application has been made as stated in paragraph 738ZA(8)(b).

Overall, it is clear that the Australian regulators primarily focus on equity crowdfunding as a source of entrepreneurial funding and have strict regulations for the platforms. Much of the responsibility of fair trade and funding has been put on the platforms and the due diligence needs to be strictly followed or else there would be legal implications against the platform and the firm seeking funding. Under these regulations Australian and in some cases New Zealand citizens above the age of eighteen years can invest on the CSF platforms. The regulations regarding debt CSF are not so clear or detailed as compared to equity CSF although the platform does require authorization to operate as a financial service provider from the relevant regulator.

2. The United Kingdom

In the UK, crowdfunding is regulated by the **Financial Conduct Authority** commonly known as the FCA. The FCA regulates both investment-based crowdfunding (equity) and the loan-based crowdfunding (debt) and are included under the **Financial Services and Markets Act 2000**. It also regulates the payment services of rewards-based and donation-based crowdfunding. The FCA explains the working of crowdfunding as:

“Crowdfunding usually takes place on a website platform that allows businesses or individuals to raise money, and investors to provide that money. The business or individual seeking finance often explains their project in a pitch to attract loans or investment from as many people as possible.” (FCA, 2018)

Although the FCA acknowledges the benefits of crowdfunding, it strictly warns the ‘consumers’ (investors) against the risks associated with both, equity and lending models as follows:

- a) Risks associated with all **Crowdfunding** models:
 - Consumers cannot avail benefit of the Financial Services Compensation Scheme (FSCS)¹
 - The investment is mostly illiquid and even though the CF platform may use it in the secondary market, the consumer may not be able to cash in quickly or may end up getting less than the amount invested.
 - Loan-based CF has much higher risk as compared to holding deposits and can result in complete loss of the investment.
- b) Risks associated with **investment-based** model:

¹ FSCS is the UK’s statutory fund which can pay compensation to the consumers of licensed and authorized financial services firms in case such firms fail or are likely to fail in the payment of claims against it. FSCS is a non-profit independent body under the Financial Services and Markets Act 2000 (FSMA) and is financed by the levies on authorized service firms. Individual consumers do not pay any charges or fee to FSMA.

- It is very likely that there is complete or 100 percent capital loss as most of the business startups fail.
- In case the company commits fraud or defaults, there would be no payment of initial investment or dividend.
- Since startup businesses undergo multiple rounds of funding, it is very likely that that the investment will be diluted with the issue of more shares by the firm and it is likely that the consumer may not receive income in form of dividends paid.
- The consumer needs to be patient with regard to receipt of payments as even successful startup ventures need time to generate income.
- If a platform fails or becomes insolvent and the firm handles client money without authorization from the FCA then there shall be no investor protection provided by the FCA.
- Most platforms do not have a secondary market for the consumers' investment.

c) Risks associated with *loan-based* model:

- It is most likely that there is total loss or part loss of investment.
- There will be no coupon payments if the company invested in fails or is fraudulent.
- With the increase in time the default risk of the firm/company increases.
- The securities offered on CF platforms are neither tradable i.e. cannot be traded in the secondary market nor are transferable. This means the consumer cannot cash in the investment.
- As stated above, any unauthorized handling of client money by the firm will void any investor protection recourse.

2.1 A Review of the Regulatory Regime for Crowdfunding as Published by the FCA:

The FCA set out to establish regulations for CF as early as March 2014, with a pending review in 2016. On April 1, 2014, the responsibility of regulating the crowdfunding platforms was transferred from consumer credit market to the FCA. The FCA published a detailed review of the crowdfunding regulatory regime in February 2015, which included key concern areas, new rules to be implemented henceforth and its effectiveness (FCA, 2015). In December 2016, the FCA published a post implementation review and feedback of the CF rules (FCA, 2016). As per the report the current regime for crowdfunding primarily applies to the CF platforms or intermediaries which are regulated under the FSMA (2000). The key features of this regime are as follows:

- a) The intermediary or platform must seek authorization from the FCA before providing any financial service in the UK. The intermediary's current and intended activities

should be clearly stated and it should meet the ‘*threshold*’² criteria in accordance to the FSMA.

- b) The intermediary’s business model should not overlap with that of investment management and banking sector as this may result overlap of markets and thus may result in taking advantage of arbitrage in the market, and since CF is already categorized as a high-risk investment, mixing it with other financial activities can be extremely risky.
- c) Complete transparency regarding information displayed is to be maintained and risk exposure must be communicated clearly to the clients.
- d) Regulations for Loan-based CF Platforms:
 - The CF platform will need to fulfil the requirements of the Consumer Credit Act (1974) as the terms upon which the investor makes the loan constitutes a regulated credit agreement in addition to authorization from the FCA.
 - Consumers interested in lending must have access to clear information which should be made available on the platform’s website. A complete detail of risk exposure will allow the investor to understand who is borrowing the money. The firm’s capital structure should be adequate (minimum capital to operate is £50,000) to protect the consumer’s money by fulfilling all the consumer protection norms. The platform should also have a ‘resolution plan’ in place so that in the event the platform collapses or exits the business the lenders continue to receive their loan repayments via other media.
 - If the platform provides a comparative analysis of its interest rates with that of the regular market, the information provided should be clear and not mislead clients.
 - In case the marketing materials used by the platform are found to be unfair and misleading the FCA can ban them. This includes deliberate omission of information that may lead to unrealistic and optimistic expectations.
 - Investors are free to approach the financial ombudsman in case of any complaint.
 - The lenders have a cooling off period of 14 days within which they can withdraw their application and the investment be refunded.
- e) Regulations for Investment-based CF Platforms:
 - These platforms facilitate investment for new and existing businesses by selling shares or debt securities of such businesses
 - These instruments are termed as ‘*non-readily realisable securities*’ by the FCA and are not listed in on regulated stock markets and carry considerable risk.

² The threshold conditions may include conditions like legal status of the firm like a) location of the firm’s offices, b) effective supervision (including the firm’s close links), c) the firm’s resources, d) suitability of the firm and its personnel and e) the firm’s business model. URL: <https://www.fca.org.uk/firms/project-innovate-innovation-hub/loan-based-crowdfunding-platforms-summary-our-rules>. Accessed on 03/01/2019

- Under the consumer protection rules of 2014, certain marketing restrictions have been imposed on firms regarding the sale of such securities to certain clients. The clients eligible to buy the securities should meet the following criteria:³
 - ✓ Ones who take regulated advice
 - ✓ Ones who qualify as high net-worth⁴ or sophisticated investors.⁵
 - ✓ Ones who confirm they will invest less than 10% of their net assets in this type of security.
- The platform needs to check that their clients understand the risks in case they do not take regulated advice.

The FCA has not yet published a webpage summarizing the provisions of investment-based CF as it has been done for the lending-based model. The FCA is continuously inviting consultation papers and suggestions to improve upon the regulations of the currently existing regulatory regime of crowdfunding and to counter and accommodate the changing structures of the evolving CF models. It is likely to publish an amended set of regulations in the second quarter of 2019 but till then it is continuously working on the feedback it receives from the industry, consumers, academia etc.

3. The European Union

In the latter half of 2017, the European Commission of the European Union which is responsible for drafting and implementing regulations and policies in the region, took cognizance of the need of a unified capital market in the European region which would ease financing of businesses as most of the countries had their own set of policy, norms, and regulations, making it difficult to transfer securities and funding from one country to another. The Commission therefore created the Capital Market Union (CMU) to broaden the scope of and ease of access to finance for the SMEs, innovative entrepreneurs, business startups, scaling up of business startups, and the expansion of existing businesses. The 2008 subprime crisis had pushed many of the EU's member nations to the edge of bankruptcy resulting in the complete collapse of their respective economies. With the biggest names in the financial sector being completely wiped out, there were hardly any takers for financing even the best of the business ideas in the region. At this point of time, entrepreneurs started looking for the alternative sources of finance including crowdfunding. The mechanism and operation of crowdfunding was easy enough to understand and the Commission quickly recognized its importance in the future. The Commission put forth the idea that, *"scaling-up of crowdfunding across the Single Market can be facilitated so that it becomes a more important source of market-based financing in support of job*

³ See COBS 4.7.7R to COBS 4.7.10R - FCA Handbook under Conduct of Business Sourcebook (COBS) Section 4.7 Direct Offer Financial Promotions. 03/01/2018

⁴ See COBS 4.12.6 R, 10/10/2016

⁵ See COBS 4.12.7 R, 01/01/2014

creation and growth.” (European Commission, 2017) via the CMU Action Plan⁶. The Commission emphasizes that with the requisite safeguards and investor protection regulations, crowdfunding can become an important source for entrepreneurial finance in the future. The Commission observed that the rate of growth of the European alternative finance market, which majorly consists of crowdfunding, was slowing down despite it keeping an appreciable pace, since the data published suggests that since 2014 the crowdfunding market grew by 92 percent to reach a valuation of €5.4 billion in 2015 (European Commission, 2017). When compared to the US crowdfunding market (estimated at €33 billion⁷) and Asia-Pacific region (mostly China, estimated at €94.6 billion⁸) Europe seemed way behind and therefore the regulation of alternative finance market through the CMU Action Plan became the Commission’s number one priority. In the process of unification of the EU capital markets, the Commission faced two problems; first, the entire European CF market was too fragmented and most of the CF intermediaries and platforms restricted themselves to national boundaries resulting in a extremely low amount of cross-border funding which was attributed to differential market regulations in different countries; second, perceived lack of investor confidence in the reliability of CF platforms and other peer-to-peer lending platforms. Some of the risks associated with the platforms mentioned in the report (European Commission, 2017) were as follows: lack of transparency about project details, little or no information about the credit profiling and background checks of neither the project nor its proprietors, loan defaults, startup failures, fraudulent projects or activities or the collapse or exit of the CF platform from the CF business. It was therefore established by the commission that the legal basis for framing regulation on crowdfunding for the EU would be Article 114 of the **Treaty of Functioning of the European Union (TFEU)**. Further, the Commission maintains regular dialogue through biannual meetings with European Supervisory Authorities, Member Nations and representatives of the crowdfunding sector to keep itself abreast with the evolving trends developments in the CF market. The Commission’s aim to develop a single unified market for CF will help overcome the two above mentioned problems and result in a cost-effective cross border CF market. In March 2018, the Commission proposed the formation of

⁶ In a report titled “Action Plan on Building a Capital Markets Union” published in September 2015, The Commission to The European Parliament, The Council, The European Economic and Social Committee, and The Committee Of the Regions, jointly established that the Commission’s top priority is to fortify the European economy, after the major financial crisis of 2008, by stimulation of investments which would enhance job creation. Steps would also be taken to understand and harness the potential of the constantly evolving new sources of funding of businesses and focus on building a true single market for capital i.e. establishing a CMU (Capital Market Union) for all the Member States.

See COM(2015) 468 final, Brussels, 30.9.2015

URL: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015DC0468&from=NL>

⁷ See Ref. Ares (2017)5288649 - 30/10/2017 (European Commission) URL:

https://ec.europa.eu/info/law/better-regulation/initiative/1166/publication/124034/attachment/090166e5b61525a3_en

⁸ *Id* 7

a ‘*standalone voluntary European crowdfunding regime under the label of a European Crowdfunding Service Provider*’ (European Commission, 2018) which the CF platforms will be governed by in order for them to conduct cross border business, considerably reducing the market entry costs for such platforms which wish to operate in multiple markets. The proposed regime would apply, both to lending as well as investment-based CF platforms thus allowing flexibility, and the combinations of various business models of funding. The proposed regulations are in consonance with the Regulation (EU) No 2017/1129⁹ which asks for a prospectus to be published in case of public offering of securities being allowed to trade in the regulated market thereby reducing the risk of *regulatory arbitrage*¹⁰ and enabling cross border funding and investment activities while providing investor protection within a stable financial framework. The following are the key features of the CF Regulations proposed for adoption by the European Commission:

- a) Article 1 refers to the application of uniform regulations to crowdfunding service providers and their organization, authorization, and their supervision. There should be complete transparency in marketing and communication activities of the CF service provider.
- b) Article 4 stipulates that CF services can only be provided by persons with effective and stable establishment, and a legal status in any of the member states of the EU with authorization in accordance with Article 11 of this regulation. The CF service providers shall maintain fair and ethical business practices and act in the best interest of their current and prospective clients. In case the service provider acts or exercises discretion on behalf of their client they should be able to justify their actions to the clients’.
- c) Article 5 directs the CF service providers to establish and implement prudent management practices such as “*the segregation of duties, business continuity and the prevention of conflicts of interest, in a manner that promotes the integrity of the market and the interest of their clients.*”¹¹
- d) Article 6 directs CF service providers to have efficient complaint handling systems with consistent and prompt grievance handling without any cherry picking. Any information desired or complaint filed will be a non-chargeable service. Proper record of complaints received, and recourse taken is to be maintained. Article 37 of

⁹ On June 30, 2017, the “*Regulation (EU) 2017/1129 of the European Parliament and of the Council of June 14, 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC*” (the “**New Prospectus Regulation**”) was published on the Official Journal of the European Union. The New Prospectus Regulation represents a significant regulatory as it will repeal the Directive 2003/71/EC as amended and integrated (the “**Current Prospectus Directive**”).

URL: http://www.legance.com/00651/DOCS/L-ENG_Newsletter_-_New_Prospectus_Regulation_ENG.pdf

¹⁰ **Regulatory Arbitrage** refers to the event or activity of a firm capitalizing on the loopholes existing in a regulatory system in order to bypass unfavourable regulations. It can also result from taking advantage of the difference in regulations of two different markets by using financial engineering to design such financial instruments, restructuring financial transactions etc.

¹¹ See Proposal for a regulation - COM(2018)113/DOCUMENT-2018-31146 of the European Commission. Article 5, Page 22. URL: https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-5288649_en. Accessed on 03/03/2019

the Regulation provides details of the formats and documents to be used the complaint handling process.

- e) Article 7 restricts financial participation of the CF service providers in the CF financial offers made on its platform. As per the Article 4(1)(35)(b) of Directive 2014/65/EU, the CF service provider will not accept those as clients who are directly or indirectly related to the employees, managers or shareholders of the service provider or platform or have a shareholding or voting rights of 20% or more in the platform to prevent conflict of interest. The service provider is required to provide the full disclosures regarding conflict of interest to all its clients, if it encounters any, and take measures to mitigate it. This is done to enable clients to take informed decisions which is a part of maintaining transparency of the process.
- f) Article 8 is concerned with outsourcing. Since a lot of financial organizations globally outsource their operational tasks to a third party due to cost concerns or enhancing systems' efficiency by outsourcing to experts, it is important that the CF service providers factor in all the risks that may arise out of outsourcing. The service provider should ensure that its service quality is maintained up to the standards with all its internal controls in place and should not hinder the monitoring by ESMA¹² and would be responsible for maintenance and compliance of all Regulatory obligations.
- g) Article 9 makes the CF service provider responsible to communicate the terms and conditions of safekeeping of the client's asset as applicable by the national law of the member state. It should be made clear whether the service provider or a third party acting on their behalf provides payment services, holding, and security of the assets. The Article 9 further states that, the CF service provider or the third party acting on its behalf shall not hold client funds (not provide any other financial service), other than the funds needed in regard the CF payment services. This is in accordance to the Article 4(11) of Payment Services Directive (PSD2) (EU)2015/2366¹³.
- h) Article 10 deals with the conditions that need to be fulfilled by the CF service provider to be eligible to apply to ESMA for authorization to operate as a CF service provider. The following are the essential contents of the application submitted to ESMA for authorization:
 - ✓ Proof of Address
 - ✓ Legal Status
 - ✓ Articles of Association

¹²European Securities and Markets Authority (ESMA) is an independent EU Authority that contributes to safeguarding the stability of the European Union's financial system by enhancing the protection of investors and promoting stable and orderly financial markets. URL: <https://www.esma.europa.eu/about-esma/who-we-are>. Accessed on 03/03/2019

¹³ The Payment Services Directive (PSD2 (EU)2015/2366) of the EU is administered by the European Commission (Director General Internal Market) to regulate payments and payment service providers of its member states. The purpose of the directive is to foster competition and participation in the payments industry, especially of non-banking financial service providers by providing equal opportunity to them and increasing awareness about consumer protection, and rights and obligations of both, the consumer and the service provider.

- ✓ Operation Details: Types of CF provided, corporate governance, internal control mechanisms and ensuring regulatory compliance.
- ✓ Systems, resources procedures- regarding control and safety of data processing.
- ✓ Business continuity and succession planning- identity and full background work-up of the successor; proof of good reputation, no criminal records, knowledge and experience in managing CF services etc.

Once the application is submitted to ESMA, within 20 working days ESMA provides the application completion status and in case of any deficiency found, the same should be informed to the applicant. In the next two months after the application is deemed complete, ESMA will review and either approve authorization or disapprove it. In case of disapproval, a detailed explanation for the same shall be communicated to the applicant service provider. The authorization is valid and effective for entire EU territory. The service provider need not have physical presence in all member states for conduct of business on cross-border basis.

- i) Article 12 states that all activities and services provided by the CF provider will fall under the purview and supervision of ESMA.
- j) Article 13 states that under the following conditions authorization of the service provider can be revoked:
 - ✓ If the service provider has not used its authorization within 18 months of obtaining it.
 - ✓ If the service provider has not provided CF services for successive 6 months.
 - ✓ If the service provider has obtained authorization using unethical or illegal means.
 - ✓ If the service provider has renounced its authorization.
 - ✓ If the service provider no longer meets the conditions under which it obtained the authorization.
 - ✓ If the service provider has seriously flouted any provision of the Regulation.
- k) Article 15 makes it compulsory for the CF service provider to ensure that the investors have full knowledge about the risk exposure of the CF offers and the CF service provider should advise their investors the best CF offer for investment as per the risk appetite of the prospective investor.
- l) Article 16 provides details of the contents regarding the “*Key Investment Information Sheet*” to be provided to the investors and clients which as the name suggests shall include important information (as per the regulation) regarding the CF offer and the CF service provider.
- m) Article 17 directs the CF service provider to have a bulletin board where all necessary announcements and interaction between CF service provider, client and fund seeker can be done.
- n) Article 18 requires all records to be maintained for a minimum period of 5 years by the CF service provider, with the clients having access to them at all times.
- o) Article 19 requires the CF service provider to maintain transparency regarding all marketing communications to the clients in one of the official languages of the

member states and no *ex-ante* notification and approval is required separately from member states.

- p) Lastly, Article 20 requires all the national competent authorities of the member states of the EU to regularly update and publish any changes in their respective national regulations applicable to marketing and communication of the CF service providers.

The above regulation was ratified by all EU Member States for it to be implemented after a series of suggestions and feedbacks were continuously exchanged by the European Commission with the representatives of the industry as well as policy makers of the member states. In the meanwhile, the individual member states have their own set of regulations for the CF service providers to conduct business in their respective national boundaries resulting in very low volume of cross-border CF funding. Amidst all this discussion it is very clear that all stakeholders view CF to have great potential in future for entrepreneurial funding and agree that dependency on venture capitalists, angel investors, banks etc. can be reduced to a great extent. To achieve smooth functioning, it is essential that the CF system be devoid of frauds, misinformation, and manipulation of the vulnerability of the clients. The CF service providers thus must be very vigilant as the proposed act puts the responsibility of the success of the CF, completely on the efficiency of the CF service providers. The formal CF regulations came into force in the year 2020.

European Crowdfunding Service Providers (ECSP) Regulation (2020):

The ECSP Regulation, adopted by the EU in 2020, is a comprehensive regulatory framework designed to facilitate crowdfunding operations across member states while ensuring investor protection. Key elements of the ECSP Regulation include:

a. Harmonized Rules: The ECSP Regulation establishes a set of harmonized rules for crowdfunding service providers operating in the EU. This harmonization reduces legal fragmentation and administrative burdens, making it easier for crowdfunding platforms to operate across borders.

b. Passporting Mechanism: The ECSP Regulation introduces a passporting mechanism that allows crowdfunding platforms to provide their services in multiple EU member states without the need for separate authorizations. This mechanism streamlines the regulatory process, encouraging cross-border crowdfunding and supporting the growth of European crowdfunding platforms.

c. Investor Protection: The ECSP Regulation places a strong emphasis on investor protection. Crowdfunding service providers are required to provide clear and accurate information about the crowdfunding projects listed on their platforms. This includes details about the project, the risks involved, and the financial situation of

the project initiator. Additionally, platforms must have adequate procedures in place to assess project eligibility and perform due diligence.

Types of Crowdfunding Covered:

The ECSP Regulation covers both investment-based crowdfunding and lending-based crowdfunding. Investment-based crowdfunding involves the offer of transferable securities or investment opportunities, while lending-based crowdfunding entails the provision of loans. By including these two main types of crowdfunding, the regulation ensures that a wide range of crowdfunding activities fall under its purview.

Investor Protection Measures:

To enhance investor protection, the ECSP Regulation introduces several important measures:

a. Investor Categorization: Crowdfunding platforms are required to categorize investors into different classes based on their knowledge and experience, financial situation, and ability to bear risks. This categorization helps ensure that investors are matched with appropriate investment opportunities.

b. Investment Limits: The ECSP Regulation sets investment limits to protect investors from overexposure to risk. Platforms must ensure that investors do not exceed these limits when participating in crowdfunding campaigns.

c. Disclosure Requirements: Crowdfunding service providers must provide investors with clear and comprehensible information about the crowdfunding projects, including the associated risks, costs, and expected returns. This transparency enables investors to make informed decisions.

d. Complaint Handling: The ECSP Regulation establishes mechanisms for handling complaints from investors. Crowdfunding platforms are required to have effective procedures in place to resolve disputes and address investor grievances.

Regulatory Sandbox:

In addition to the ECSP Regulation, the EU has also introduced a regulatory sandbox for crowdfunding platforms. The sandbox allows platforms to test innovative business models and technologies within a controlled environment, with limited regulatory requirements. This fosters experimentation and promotes the development of new crowdfunding models while ensuring that investor protection is not compromised.

Impact and Future Perspectives:

The introduction of EU crowdfunding regulations has had a significant impact on the crowdfunding landscape within the region. The harmonization of rules and the passporting mechanism have facilitated cross-border crowdfunding, enabling platforms to reach a wider investor base and entrepreneurs to access capital from across the EU.

Moreover, the emphasis on investor protection has increased investor confidence in crowdfunding, leading to greater participation and a more robust crowdfunding ecosystem. The regulatory sandbox provides a supportive environment for platforms to innovate and explore new crowdfunding models, fostering continued growth and evolution in the industry.

Looking ahead, the EU crowdfunding regulations are expected to adapt to technological advancements, such as blockchain-based crowdfunding and the use of digital tokens. Regulatory frameworks will continue to evolve to address emerging challenges while maintaining a balance between promoting innovation and safeguarding investor interests.

The EU crowdfunding regulations, specifically the ECSP Regulation, have played a pivotal role in fostering innovation, cross-border crowdfunding, and investor protection within the region. By harmonizing rules, introducing investor protection measures, and providing a regulatory sandbox, the EU has created a conducive environment for crowdfunding platforms and entrepreneurs to thrive. As the crowdfunding landscape continues to evolve, the EU's regulatory frameworks will adapt to ensure that crowdfunding remains a trusted and efficient tool for raising capital and driving innovation in the European market.

4. The United States of America

The CF regulations in the USA are multidimensional in nature in a way that reward, and donation-based models of CF are essentially unregulated subject to transgressions that apply to all commercial transactions in the country (e.g. prohibiting fraud, misrepresentation of information, misleading advertisements etc.) whereas, equity based investing and lending based crowdfunding must comply with the 1933, Securities Act, registration and compliance requirements unless some exemption is available. The origin of the Act can be attributed to the Jumpstart Our Business Startups (JOBS) Act of 2012, which was signed into law by the then President of the USA, Mr. Barack Obama. The JOBS Act was a bipartisan effort to trigger economic growth in the aftermath of the 2008 subprime crisis. The crisis had severely hit the small businesses, and the investment, and funding opportunities had dried up. Entrepreneurs looking to raise startup and early stage capital were finding it difficult to obtain funds. In such a situation, the JOBS Act provisions allowed small businesses to raise limited amount of equity capital by offering limited amount of stocks/shares to private citizens through online CF platforms.

The ***Title III of the JOBS Act of 2012***, which was added in the Securities Act of 1933, as Section 4(a)(6), allows certain CF transactions to be exempted from registration. In the year 2015, ***Regulation Crowdfunding*** was adopted by the SEC¹⁴ to implement the provisions of the Title III, allowing eligible companies to raise capital through CF starting May 16, 2016. Initially, in the US, CF did not offer any kind of share or financial return to the investor in the profits of the business venture from the business activities as this kind of transaction is referred to as the “Equity-based model” and therefore come under the ambit of the SEC as it would involve sale and purchase of financial securities and thus the registration of the CF platform as the broker with the SEC would be required. Experts pointed out that registered offerings and the obligated reporting associated with it would require a sizable expense and hence would not be feasible raise money through small amounts of capital as it is done in a CF transaction. To overcome the issue of costing and heavy paperwork involved in raising funds through online CF the Title III of JOBS Act was introduced. The following are the key features of the Title III of the JOBS Act 2012:

- i. It amended the Securities Act by introducing Section 4(a)(6) providing exemption to certain CF transactions from registration requirements of Securities Act, Section 5. To be eligible for the exemption under the above section, the issuer (*‘all entities controlled by or under common control with the issuer’*) must meet the following criteria:
 - ✓ The amount raised for the venture should not exceed \$ 1 million in a 12-month period.
 - ✓ The individual investment by investors in all issuers of CF in a 12-month period is restricted to:
 - a) \$ 2000 or 5 percent of annual income or investor’s net worth, whichever is greater subject to the investor’s net worth or annual income being less than a \$ 100,000;
 - b) 10 percent of an individual investor’s annual income or net worth (not exceeding \$100,000), if annual income or net worth of the investor is greater than or equal to \$100,000; and
 - c) That all related transactions are conducted via an intermediary that either is registered as a *‘broker-dealer’* or is registered as a new type of entity known as *‘funding-portal’*.
- ii. It adds Securities Act Section 4A (United States Code, 2013) which states that certain information must be furnished by the issuers and the intermediaries to the investors and potential investors along with relevant actions to be taken and also provide the Commission with the relevant information and notices;
- iii. It adds Exchange Act Action 3(h) (United States Code, 2018) which requires the Commission to adopt conditional or unconditional exemption rules to exempt

¹⁴ SEC- Securities and Exchange Commission of USA was established in 1934 by the Congress as a federal regulator of securities market of USA. Like any other regulator, it protects the rights of the investors against frauds and financial malpractices and keeps a vigil on corporate activities in the US.

'funding portals' from having to register with the Commission as a broker-dealer with reference to Exchange Act Section 15(a)(1) (United States Code, 2018);

- iv. It mandates that the Commission should provide the conditions under which the issuer or intermediary may be disqualified or be restricted from availing the exemption under Section 4(a)(6);
- v. It adds Exchange Act Section 12(g)(6) (United States Code, 2018) in which the adoption of rules by the Commission regarding exemption from the registration requirements of the offered securities (with reference to Section 4(a)(6)) as per Section 12(g) either conditionally or unconditionally is stated.

The above amendments were then opened for comments from the public in general to improve upon the regulations. Observations and comments from the industry, trade associations, investors, investment organizations, funding portals, policy makers and law firms etc. affirmed the popularity and the need for a proper and elaborate regulation dedicated to crowdfunding only. The **Final Rule** for Crowdfunding was published by the SEC effective May 16, 2016. The published final rules can be summarized as under:

A) Crowdfunding Exemption, Limits and Exclusions:

As discussed above, Section 4(a)(6) provides some crowdfunding transactions the exemption from registration requirements of Section 5 of the Securities Act. The issuer and/or intermediary is exempted, subject to the following conditions:

1. **Limit on Raised Capital:** The aggregate amount of securities sold to all investors within a 12-month period cannot exceed \$1 million for securities offered in reliance to Section 4(a)(6) only. Such capital raised should not be combined with any other exempt offering under other exemptions or provisions of the Securities Act. Simply put, it means that concurrent offerings under different exemptions cannot be solicited or advertised by the issuer to the public. Such an act will result in violation of the Regulation Crowdfunding.
2. **Investment Limits:** An investment limit of a) \$2000 or 5 percent of the lesser of investor's annual income or net-worth, when the annual income or net-worth is less than \$100,000, whichever is greater; or b) 10 percent, of the lesser of, an individual investor's annual income or net worth (not exceeding \$100,000), if annual income or net worth of the investor is greater than or equal to \$100,000.

Table 1. Example of Calculation of Investment Limits.

<i>Investor's Annual Income</i>	<i>Investor's Net Worth</i>	<i>Calculation</i>	<i>Investment Limit</i>
\$30,000	\$105,000	Greater of \$2,000 or 5% of \$30,000 (\$1,500)	\$2,000

\$150,000	\$80,000	Greater of \$2,000 or 5% of \$80,000 (\$4,000)	\$4,000
\$150,000	\$100,000	10% of \$100,000 (\$10,000)	\$10,000
\$200,000	\$900,000	10% of \$200,000 (\$20,000)	\$20,000
\$1,200,000	\$2,000,000	10% of \$1,200,000 (\$120,000), subject to \$100,000 cap	\$100,000

Source: *Final Rule Crowdfunding, SEC, Page.26* (2016)

This rule is commonly applicable to retail, institutional as well as accredited investors.

3. **Transactions Conducted through an Intermediary:** Section 4(a)(6)(C) requires compliance under Securities Act Section 4A(a) that any CF transaction be conducted via funding portal or broker. Rule 100(a)(3) of Regulation Crowdfunding provides that the issuer can offer CF through only one intermediary's platform so that all the information regarding the offer comes from one source, there is one platform for the crowd to discuss and share information thereby reducing chances of dilution of the crowd and multiple interpretations of information. A single platform will also allow easy vigilance over fund collection subject to the provisioned limits. The *online only*, platform has been defined under Rule 300(c)¹⁵ as *"a program or application accessible via the Internet or other similar electronic communication medium through which a registered broker or a registered funding portal acts as an intermediary in a transaction involving the offer or sale of securities in reliance on Section 4(a)(6) of the Securities Act (15 U.S.C. 77d(a)(6))"* (Final Rule Crowdfunding, 2016). The funding portals should not encourage or initiate any physical contact with the investors for any kind of solicitation, promotion recommendations etc. Rule 300(c)(4) allows the intermediary to conduct the back-office and administrative functions off the platform.
4. **Exclusion of certain Issuers from Eligibility under Section 4(a)(6):** Under Securities Act Section 4A(f), the conditions and list of issuers excluded from the eligibility to engage in CF transactions is provided. The exclusion includes:
 - ✓ Non-US Companies
 - ✓ Existing, Exchange Act reporting companies
 - ✓ Selected investment firms/companies
 - ✓ Companies disqualified as per Regulation Crowdfunding disqualification provisions.
 - ✓ Companies failing compliance regarding annual reporting in pursuant with the Regulation Crowdfunding in the preceding two years after the initial CF offering.
 - ✓ Companies with ambiguous business plans with indications of merger or acquisition with unknown or unidentified company.

¹⁵ The Rule 300 series of Regulation Crowdfunding apply to broker-dealers and funding portals or platforms ("intermediaries").

B) Issuer Requirements**1. Mandatory Disclosures:**

Any issuer of a CF offer must file the offering statement electronically via Form C¹⁶ through the “*Commission’s Electronic Data Gathering, Analysis and Retrieval (EDGAR) system and with the intermediary facilitating the crowdfunding offering.*”¹⁷ The disclosures include:

“

- ✓ *the name, legal status, physical address and website address of the issuer;*¹⁸
- ✓ *the names of the directors and officers (and any persons occupying a similar status or performing a similar function), and each person holding more than 20 percent of the shares of the issuer;*¹⁹
- ✓ *a description of the business of the issuer and the anticipated business plan of the issuer;*²⁰
- ✓ *a description of the financial condition of the issuer;*²¹
- ✓ *a description of the stated purpose and intended use of the proceeds of the offering sought by the issuer with respect to the target offering amount;*²²
- ✓ *the target offering amount, the deadline to reach the target offering amount and regular updates about the progress of the issuer in meeting the target offering amount;*²³
- ✓ *the price to the public of the securities or the method for determining the price;*²⁴ and
- ✓ *a description of the ownership and capital structure of the issuer.*^{25”}

¹⁶ Available at <https://www.sec.gov/about/forms/formc.pdf>, format of the for Form C of Regulation Crowdfunding. Accessed on 12March, 2019.

¹⁷ Available at <https://www.sec.gov/info/smallbus/secg/rccomplianceguide-051316.htm>. Accessed on 12March, 2019.

¹⁸ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(A).

¹⁹ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(B).

²⁰ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(C). Regulation Crowdfunding, Rule 201(d)

²¹ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(D).

²² US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(E). Regulation Crowdfunding, Rule 201(i)

²³ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(F). Regulation Crowdfunding, Rule 201(g)

²⁴ US Securities and Exchange Commission, Securities Exchange Act Section 4A(b)(1)(G). Regulation Crowdfunding, Rule 201(l)

²⁵ Section 4A(b)(1)(H). Specifically, “*Section 4A(b)(1)(H) and Regulation Crowdfunding, Rule 201(m) requires a description of: “(i) terms of the securities of the issuer being offered and each other class of security of the issuer...; (ii) a description of how the exercise of the rights held by the principal shareholders of the issuer could negatively impact the purchasers of the securities being offered; (iii) the name and ownership level of each existing shareholder who owns more than 20 percent of any class of the securities of the issuer; (iv) how the securities being offered are being valued...; and (v) the risks to purchasers of the securities relating to minority ownership in the issuer, the risks associated with corporate actions, including additional issuances of shares, a sale of the issuer or of assets of the issuer, or transactions with related parties.*”

2. Continuous Reporting by the Issuer:

- ✓ Within 120 days of the end of the financial year annual report to be submitted²⁶.
- ✓ Posting of annual report on the issuer's website is a must though no physical copy is to be provided.
- ✓ Financial statement of the issuer certified by the "*principal executive officer*"²⁷ of the issuer "*true and complete*" in all respects or financial statements audited by independent certified public accountant.
- ✓ Under the following conditions the annual report submission by the issuer may be exempted or terminated:
 - a) The issuer regularly files such annual reports under the Exchange Act Sections 13(a) or 15(d); or
 - b) The issuer has less than 300 security holders and has filed a minimum of one annual report; or
 - c) The issuer has total assets not in excess of \$1 million with a minimum of 3 annual reports filed; or
 - d) The issuer / another party re-purchases / purchases all the issued securities, or, redemption of all redeemable issued securities is complete; or
 - e) The issuer itself files for liquidation or dissolves as per the applicable state laws.

3. Prohibitions and Restrictions on Advertisement Terms of the Offer:

The Advertisement notice of the offer can only include:

- a) Statement of the Issuer of the offer, intermediary name, and, the web link for the investor to explore the offer.
- b) Offer terms
- c) Key information about the issuer.

The **terms** used in the advertisement is restricted to:

- a) Amount of Securities Issued;
- b) Type of security;
- c) Price of security; and
- d) End date of the offer.

4. Compensation of Persons Promoting the Offer:

The issuer should not directly or indirectly engage, "*compensate or commit to compensate*" any other channel or person besides the ones provided by the intermediary barring the exceptions stated in Rule 205(b) of Regulation Crowdfunding.

5. Miscellaneous Requirements:

- a) Oversubscription is allowed but should not exceed the stipulated annual limit of \$1 million.²⁸ The limit, allocation and intended use of the oversubscribed amount should be clearly defined by the issuer.

²⁶ Regulation Crowdfunding, Rule 202(a)

²⁷ *Id* 26

²⁸ Regulation Crowdfunding, Rule 201(h)

- b) Method used to determine the offer price of the security to be disclosed.
- c) Type and Valuation of the Security to be defined.

C) Intermediary Requirements:

1. Defining a 'Funding Portal' and Persons Associated with it:

- a) Funding Portal, as per the Exchange Act Section 3(a)(80) and Rule 300(c)(2) of Regulation Crowdfunding *"as any person acting as an intermediary in a transaction involving the offer or sale of securities for the account of others, solely pursuant to Securities Act Section 4(a)(6), that does not: (1) offer investment advice or recommendations; (2) solicit purchases, sales or offers to buy the securities offered or displayed on its website or portal; (3) compensate employees, agents or other persons for such solicitation or based on the sale of securities displayed or referenced on its website or portal; (4) hold, manage, possess or otherwise handle investor funds or securities; or (5) engage in such other activities as the Commission, by rule, determines appropriate."*²⁹
- b) Rule 300(c)(1) of Regulation Crowdfunding defines the term *"person associated with a funding portal or associated person of a funding portal to mean any partner, officer, director or manager of a funding portal (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling or controlled by a funding portal, or any employee of a funding portal, other than persons whose functions are solely clerical or ministerial"*³⁰.

2. General Requirements:

- a) Registration with SEC and membership of SRO (Self-Regulatory Organization) as a funding portal is required. In Accordance to Exchange Act Section 3(a)(26) and Rule 300(a)(2), the intermediary must be registered with any national securities association registered under Exchange Act (e.g. FINRA-Financial Industries Regulatory Authority).
- b) The intermediary and its office bearers should not have any financial interest in the issuer in terms of ownership or economic interest.

3. Measures to Avert Risks/Frauds:

- a) The intermediary should ensure issuer's compliance to provisions stated in the Act.
- b) Complete and true records of the security holders and their related transactions must be maintained meticulously.
- c) In accordance to Rule 301(c)(1) of the Regulation Crowdfunding, the intermediary has the right to deny issuer the access to the platform provided it has reasonable basis of belief that the issuer is liable to be disqualified under Rule 503 of Regulation Crowdfunding.
- d) The privacy and protection of the information collected from the investor should be maintained and ensure that non public information of the investors is not leaked as it may result in identity theft of the investor.

²⁹ Final Rule Crowdfunding, Page 151. Available at - URL : <https://www.sec.gov/rules/final/2015/33-9974.pdf>
Accessed on 11 March, 2019.

³⁰ Id 29

4. Accounts and Electronic Delivery:

All offer related transactions of the investors should be done only through the account of the investor that is opened and registered with the intermediary. Also, all materials (such as securities, educational material, notices etc.) are to be delivered through electronic means only.

5. Requirements for Transactions:

- a) All information regarding the issuer and its compliance to the provisions of the regulations should be available to the public on the website for the investors.
- b) Investor qualifications regarding the investment decision to be ensured via uploading of financial documents of the investor to check adherence to investment limits and in addition provide other general information about the investor on the website.
- c) In accordance with Rule 302(b)(2) the acknowledgement of risk by the investor is required.
- d) The intermediary's platform should provide communication channels to registered users with full identity disclosure.
- e) The intermediary should provide all the necessary information, notices and other relevant materials to the investor once it has received the notice of '*Investment Commitment*' by the investor.
- f) The intermediary should maintain and transmit funds of the investors in accordance to Rule 303(e)(1) of Regulation Crowdfunding, that is, hold the investment till the offer is complete, and/or, return the funds in case of oversubscription, cancellation of investment commitment or withdrawal from the offer by the investor as per Rule 303(e)(2). The funds are to be held by a qualified third party registered with the NCUA (National Credit Union Association, USA).
- g) In accordance to Rule 303(f)(1) of Regulation Crowdfunding, the disclosure of brokerage charged by the intermediary and the confirmation receipt of all transactions of the investor, and documents related to the terms of the transactions is to be provided to the investor by the intermediary as it is important for maintaining transparency and investor protection.

6. Completion of Offerings, Cancellations and Reconfirmations:

The Securities Act section 4A(a)(7) allows cancellation of investment commitment by the investor through the intermediary's platform. In case the target funding has been achieved ahead of the proposed deadline, investors will be provided a notice to cancel/reconsider their investment until 48 hours³¹ prior to the offer deadline.

7. Payments to Third Parties:

Intermediaries are permitted to compensate third parties for general business advertising of its platform, etc., but it should be strictly unrelated to (directly or indirectly) to the sale or purchase of the offering/s available on its website.

³¹ See Rule 304(b) of Regulation Crowdfunding for the conditions under which early closing of the offer can be initiated by the intermediary before the end of the offer deadline.

The Regulation Crowdfunding was adopted by the SEC on October 30, 2015, for implementing the CF regulations in USA. The rules are in effect from May 16, 2016, although the submission of registration applications of brokers, potential issuers, agencies etc. were allowed from January 2016. The USA is one of the pioneer countries to recognize the potential of CF in promoting the entrepreneurial ventures. It is the first country to have fully functional regulations on CF. The regulations have elaborate guidelines both for the issuer and the intermediaries and offers transparency in all the processes as everything is available online. Walking in the footsteps of USA, the other economies across the world are pushing towards formalizing the CF regulations for their countries as well.

Impact And Future Perspectives Of Crowdfunding Regulations:

Crowdfunding regulations have had a profound impact on the financial landscape. On one hand, they have increased investor confidence, encouraged innovation, and facilitated access to capital for startups and small businesses. On the other hand, compliance with regulations can be burdensome for crowdfunding platforms, potentially stifling their growth, or limiting their ability to support entrepreneurs.

Looking ahead, as crowdfunding continues to evolve, regulatory frameworks will likely adapt to address emerging challenges such as tokenization and blockchain-based crowdfunding. Striking the right balance between innovation and investor protection will remain a key objective for regulators worldwide.

Crowdfunding regulations play a crucial role in nurturing a vibrant crowdfunding ecosystem while safeguarding investors' interests. By ensuring transparency, imposing investment limits, promoting due diligence, and educating investors, these regulations foster a more trustworthy environment for crowdfunding activities. As the global financial landscape continues to evolve, regulatory frameworks will continue to evolve to strike the right balance between innovation and investor protection, fostering the growth of crowdfunding as a viable financing option for entrepreneurs and innovators.

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