

# REVIEW OF CROWDFUNDING REGULATION

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

**2014**



EUROPEAN  
CROWDFUNDING  
NETWORK



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## IMPRESSUM

Review of Crowdfunding Regulation. Interpretations of existing regulation concerning crowdfunding in Europe, North America and Israel, 2014

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## Switzerland

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

Overall, the Swiss Crowdfunding market remains rather small in comparison with the USA, Germany and France, although, on average, commitments seem to be higher than elsewhere. Nevertheless it is growing strongly. In 2013, CHF 11.6 million was collected through Crowdfunding in Switzerland. This is more than twice the volume of 2012.<sup>53</sup>

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

The biggest growth occurred in fund raising through Equity Model. In fact, the growth rate from 2012 to 2013 regarding the Equity Model amounts to 192%. The average volume for the successfully financed campaigns in 2013 was CHF 558,000. The Equity Model is, by volume of funds invested (CHF 5.58 million in 2013), the most important model in Switzerland to date.<sup>54</sup> However, the number of platforms is still small.

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

The Lending Model is, by volume of funds invested, the least important model in Switzerland. In 2013, it involved a volume of CHF 1.78 million. Nevertheless, compared to 2012, this amounts to a growth of +109%. The average volume for the successfully financed campaigns in 2013 was CHF 15,000.<sup>55</sup>

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

In 2013, the Donations or Rewards Model raised a volume of CHF 4.23 million. Compared to 2012, the growth of the volume amounts to +68%. Compared to the growth of the Equity and Lending Model, this is the lowest growth. Although it is the second biggest model by volume of funds invested, the average funds raised through successful campaigns was lower (namely CHF 7,000)<sup>56</sup> than for the Equity and Lending Model. This model is popular mainly in the art, music, film, sport and design scene, where several platforms operate using the Donations or Rewards Model. By contrast, community projects are practically unheard of in Switzerland.

<sup>53</sup> Source: DIETRICH, ANDREAS/AMREIN, SIMON, The Crowdfunding Monitoring Switzerland 2014, orderable under <http://blog.hslu.ch/retailbanking/Crowdfunding2014/>, p. 3 (cited: DIETRICH/ AMREIN, Monitoring).

<sup>54</sup> See DIETRICH/AMREIN, Monitoring, p. 3.

<sup>55</sup> Source: DIETRICH/AMREIN, Monitoring, p. 3.

<sup>56</sup> Source: DIETRICH/AMREIN, Monitoring, p. 3.



## 2 Recent developments regarding Crowdfunding regulation in Switzerland

### 2.1 Developments in politics and authorities regarding Crowdfunding regulation

#### 2.1.1 In General

By international standards, Crowdfunding did not trigger a major attention in Switzerland.<sup>57</sup> It received some media attention, which however did not lead to any legislative initiative.<sup>58</sup> This is particularly noteworthy considering that two major regulatory initiatives were launched in Switzerland.<sup>59</sup>

Swiss regulators did not address Crowdfunding in detail so far. As far as can be seen, only the Swiss Financial Market Supervisory Authority (FINMA) and the Swiss State Secretariat for Economic Affairs (SECO) addressed this issue in passing.<sup>60</sup>

#### 2.1.2 FINMA

FINMA has not addressed Crowdfunding in detail so far. It only commented on Crowdfunding in passing in a report called "How investors can protect themselves against unauthorized financial market providers".<sup>61</sup> In this report, FINMA noticed that more and more individuals seeking finance (borrowers) and investors are looking for alternatives to banks. However, since there is a huge variety of Crowdfunding platforms, no general answer to the question of whether such platforms require a license exists. Therefore, FINMA must review each business model on a case-by-case basis.<sup>62</sup>

Pursuant to newspaper articles, FINMA has issued rulings on at least three different platforms so far deciding that none of them is subject to the supervision of FINMA.<sup>63</sup> However, FINMA seems to take a cautious, if not suspicious, approach to Crowdfunding.

#### 2.1.3 SECO

In December 2013, SECO has published an opinion called "Diskussionspapier Risikokapital in der Schweiz" prepared by Vischer AG.<sup>64</sup> This document gives an overview over the forms of Crowdfunding, the platforms in Switzerland and the current regulation in Switzerland and some other countries. Moreover, the authors of the document formulated some recommendations in terms of the necessity to intervene in this area. They especially recommend that FINMA issue a policy paper stating its view on

<sup>57</sup> See KUNZ, PETER V., Crowdfunding, in: Jusletter 25 August 2014, para 1 (cited: KUNZ, Crowdfunding).

<sup>58</sup> See KUNZ, Crowdfunding, para 1 and 62.

<sup>59</sup> See below, chapter 2.2.

<sup>60</sup> KUNZ, Crowdfunding, para 52.

<sup>61</sup> This FINMA report can be downloaded under [www.finma.ch/e/privatpersonen/documents/kundenschutz-e.pdf](http://www.finma.ch/e/privatpersonen/documents/kundenschutz-e.pdf) (cited: FINMA report).

<sup>62</sup> FINMA report, p. 11.

<sup>63</sup> See e.g. <http://www.tagesanzeiger.ch/schweiz/standard/Die-Fallstricke-des-CrowdfundingBooms/story/27666437>.

<sup>64</sup> The opinion can be downloaded under <http://www.seco.admin.ch/themen/05116/05118/05319/index.html?lang=de&download=NHzLpZeg7t,lnp6loNTUo42lzZ6ln1acy4Zn4Z2q> (cited: SECO, Diskussionspapier).



various issues in relation to Crowdfunding. Furthermore, the report recommends amending various legislations to clarify the scope and applicability to Crowdfunding.<sup>65</sup>

However, this document caused neither wide discussions nor actions in Switzerland.<sup>66</sup>

## 2.2 Future Financial Services and Markets Act, Financial Market Infrastructure Act and Financial Institutions Act

Currently, the Swiss government has initiated a new regulatory initiative and published bills for three new legislative instruments, namely a new Financial Services and Markets Act (*Finanzdienstleistungsgesetz*, FSMA),<sup>67</sup> a new Financial Market Infrastructure Act (*Finanzmarktinfrastrukturgesetz*, FMIA),<sup>68</sup> and a new Financial Institutions Act (*Finanzinstitutsgesetz*, FinIA).<sup>69</sup> None of these bills addresses Crowdfunding directly.<sup>70</sup> Nevertheless, especially the FSMA and FMIA might have some impact on Crowdfunding platforms. The FMIA can be relevant to platforms if they qualify as a stock exchange or a trading system.<sup>71</sup> The FSMA can bear some consequences for the Equity Model since it aims to introduce a comprehensive prospectus regime for equity offerings. Moreover, platforms may be subject to rules of conducts if they, for instance, buy and sell securities, receive and transmit orders in connection with securities or if they hold assets for the account of a client.

## 3 Current Regulation of Crowdfunding in Switzerland

### 3.1 License under the Swiss Federal Act on Banks and Savings Banks (*Banking Act*)

#### 3.1.1 General Rule

The Swiss Federal Act on Banks and Savings Banks (*Bankengesetz*, Banking Act) and its implementing ordinance, the Banking Ordinance (*Bankenverordnung*, Banking Ordinance), require natural persons and/or legal entities (collectively **Persons**, and each a **Person**) mainly active in the financial sector intending to either (i) accept deposits from the public on a professional basis, or (ii) recommend themselves for financing any number of persons or companies (with which they do not form an economic unit of their own) with public deposits or by refinancing themselves from five or more banks, to obtain a license from FINMA. This licensing requirement also applies in case any Person intends to advertise any such services (in advertisements, prospectuses, circular letters, electronic media or similar publication media).

A Person is considered to act on a professional basis in case it constantly accepts more than 20 deposits from the public. The Banking Ordinance does not contain a positive definition of deposits; it does, however, contain a list of exemptions for funds not qualifying as deposits. According to this list, *inter*

<sup>65</sup> On the whole SECO, Diskussionspapier, p. 7 et seq.

<sup>66</sup> KUNZ, Crowdfunding, para 52.

<sup>67</sup> See <https://www.news.admin.ch/message/index.html?lang=en&msg-id=53561>.

<sup>68</sup> See [www.admin.ch/aktuell/00089/index.html?lang=en&msg-id=54305](http://www.admin.ch/aktuell/00089/index.html?lang=en&msg-id=54305).

<sup>69</sup> See <https://www.news.admin.ch/message/index.html?lang=en&msg-id=53561>.

<sup>70</sup> Cf. KUNZ, Crowdfunding, para 63.

<sup>71</sup> Cf. KUNZ, Crowdfunding, footnote 153 to para 63.



*alia*, the acceptance of (i) funds provided in consideration of a contract, due to the transfer of property or the rendering of a service, or (ii) funds which are transferred as a security are not considered as deposits.

### 3.1.2 Legal Consequences for the Crowdfunding Platforms in Switzerland

In order not to be required to obtain a banking license from FINMA, a Crowdfunding platform in Switzerland should generally refrain from collecting funds from investors on its own account and from keeping any accounts in the name of the investors, e.g. to keep accounts for the investors from which funds (for the purchase of shares or for loans to be granted) are debited and directed to the companies and to accept payments (interest, principal, or dividends) from the companies in the name and for the account of such investors.

Under the current Swiss legislation, it is not clear whether the purchase of equity securities and the provision of financing aids for the account of third parties qualify as financing under the Banking Act. Crowdfunding platforms should therefore generally be cautious in providing such services for the account of investors (e.g. to purchase shares or to grant loans to the companies in the name and for the account of the investors).

## 3.2 License under the Federal Act on Collective Investment Schemes

### 3.2.1 General Rule

According to the Federal Act on Collective Investment Schemes (*Kollektivanlagengesetz, CISA*), all Persons responsible for the management of collective investment schemes, the safekeeping of assets held in such schemes as well as the distribution of such schemes to retail (i.e. non-qualified) investors are required to obtain an authorization from FINMA.

Collective investment schemes are defined as assets raised from several investors for the purpose of collective investment, and which are pooled and collectively managed for the account of such investors.

Distribution is generally defined as any offering of and advertising for collective investment schemes and covers any kind of activity which is aimed at investors acquiring collective investment schemes.

An exemption from the above authorization obligation applies if (i) the funds are solely invested in one operating company which is active in a manufacturing, trade or service business and generates its revenues and profits with such business (and not solely by way of committing funds), or if (ii) the investment decisions are primarily made by the investors and not by the management of the investment scheme.

Loans granted to a collective investment scheme should in principle also be outside the scope of the CISA. However, each case needs to be assessed globally, i.e. taken as a whole it must in a specific case be excluded that a loan (due to its risk profile or repayment schedule) can be characterised as an investment in a collective investment scheme.



### 3.2.2 Equity Model

To be outside the scope of the collective investment scheme regulation, an equity based Crowdfunding platform should thus be set up in a way that it is able to primarily profit from the exemption applicable with regard to investments into operating companies; i.e. it should introduce possible investors to operating companies only and should refrain from any activities which could result in the platform pooling or managing any funds received from the investors for the account of such investors and subsequently investing them collectively into a company via the platform itself. It should be active only as an intermediary for purposes of information exchange (e.g. names, phone numbers and other contact details) with regard to possible direct investments into specific operating companies and not directly or indirectly transfer any funds from investors to companies.

### 3.2.3 Lending Model

A debt based Crowdfunding platform should generally avoid holding itself out as a collective investment scheme, i.e. the management of third party funds. Therefore and in order not to be subject to regulation by FINMA, such platforms should avoid (i) accepting funds from investors, (ii) pooling such investments from investors in the name of the platform in a way that the investments cannot be personalized anymore, and (iii) subsequently granting such investments as loans to a company advertising on the platform.

With regard to debt based Crowdfunding platforms, the situation is basically the same as described above with regard to Equity Models; i.e. loans granted directly to operating companies or to private persons only (and in particular not to the operator of the platform for further on lending) should fall outside the scope of the CISA. Even if loans were to be granted by an investor to a collective investment scheme presented on the platform (but operated by a party other than the operator of the lending platform), the operator of the platform should still not be subject to the CISA, because granting a loan to a collective investment scheme should not be qualified as distributing a collective investment scheme.

Further, the investment decision to grant any funds to a specific company should always remain with and be made by the investor itself and not by the platform. Contractual arrangements appearing as third party management of funds should generally be avoided.

### 3.2.4 Donations or Rewards Model

Normally, these platforms are structured in a way that the contributions are not investments related to a direct return, if any, and therefore such platforms do not fall under the collective investment schemes regulations.

## 3.3 Federal Act on Stock Exchange and Securities Trading (SESTA)

### 3.3.1 General Rule

Pursuant to the Federal Act on Stock Exchange and Securities Trading (*Börsengesetz*, SESTA), all Persons qualifying as securities dealers are required to obtain an authorization from FINMA. A securities dealer is defined as a Person or partnership who, in its professional capacity, (i) buys and sells



securities on the secondary market, either for its own account with the intent of reselling them within a short period of time or for the account of third parties, (ii) publicly offers securities on the primary market, or (iii) creates derivatives and offers them to the public.

Securities dealers include in particular own-account dealers (dealers who, in their professional capacity, trade in securities for their own account on a short-term basis), client dealers (dealers who, in their professional capacity, trade in securities in their own name for the account of clients) and issuing houses (securities dealers who, in their professional capacity, underwrite securities issued by third parties on a firm basis or against commission and offer them to the public on the primary market).

Furthermore, SESTA requires a stock exchange to obtain a license from FINMA. A stock exchange is defined as an organization set up solely for the purpose of securities trading (e.g. shares and bonds) on the secondary market, which enables the simultaneous exchange of offers of securities (and not only the exchange of price-related information) among a number of securities dealers as well as the execution of such transactions.

In addition, the Federal Council may subject organizations which are, in whole or in part, similar to exchanges to the SESTA or exempt certain exchanges or similar organizations from the application of the SESTA whenever justified by the objectives of the SESTA. Exchanges, as well as organizations similar to exchanges, are organizations which facilitate secondary market transactions (and not the offering of new securities).

### 3.3.2 Legal Consequences for Crowdfunding Platforms in Switzerland

In the light of the foregoing, Crowdfunding platforms should, *inter alia*, refrain from the following business activities in order not to be considered as a securities dealer:

- a) Trading of shares (or similar participation rights) in companies presented on the platform in the name and for the account of the investors and, in particular, not (i) maintain any accounts for the settlement of transactions for such investors by itself or with third parties, and/or (ii) hold any shares (or similar participation rights) on behalf of the investors in safe custody with itself or with third parties but in its own name; and
- b) Underwriting any kind of securities (in particular shares or bonds) newly issued by companies presented on the platform on a firm basis or against commission and subsequently publicly offer such securities to investors.

Furthermore, a Crowdfunding platform should generally be careful not to qualify as a stock exchange or an exchange-like institution in connection with additional services offered to facilitate the execution of investments or subsequent divestments (i.e. services other than providing information on possible investments). Normally, Crowdfunding platforms should not qualify as a stock exchange or exchange-like institution because they present direct investment into new (not existing) shares and thus facilitate primary market transactions. Moreover, even if the investments presented on the platform were investments to be made on the secondary market (i.e. into existing securities), the platforms should not qualify as exchanges (however, the analysis might be different with regard to exchange-like institutions), as such platforms do not (yet) have the capability to enable the simultaneous exchange of



offers, the conclusion of the respective contracts or the settlement of such contracts concluded over the platform.

### 3.4 Anti-Money Laundering Act

#### 3.4.1 General Rule

Pursuant to the Swiss Anti-Money Laundering Act (*Geldwäschereigesetz*, AMLA), Persons providing services as financial intermediaries must be affiliated to a recognized self-regulatory organization or need to obtain a license from FINMA for their professional business activities. In addition, financial intermediaries must comply with the statutory provisions and procedures of the AMLA, e.g. verification duties regarding the identity of the customer (and the beneficial owner), duties to clarify and to keep records, and certain organizational measures.

Financial intermediaries are in particular Persons who, in their professional capacity, accept or keep third party funds or who assist in the investment or transfer of such funds, such as Persons carrying out credit transactions, providing services for payment transactions or assets, or securities managers and Persons making actual investments in their capacity as investment advisors. However, Persons solely providing investment advisory services (including platforms who act as intermediary without assisting in any kind of the flow of funds) are not considered as financial intermediaries.

#### 3.4.2 Legal Consequences for the Crowdfunding Platforms in Switzerland

Whether an operator of a Crowdfunding platform (irrespective of the model operated) falls under the money laundering regulation very much depends on whether it limits its services to (i) providing information on possible investments, (ii) acting as intermediary with regard to possible transaction, and/or (iii) provides solely advisory services (in each case without assisting in the transfer or flow of funds), in which cases the money laundering regulation should theoretically not apply.

Other services offered in connection with investments presented on a platform, such as (i) services facilitating the execution of a transaction (e.g. assisting investors and/or companies or borrowers in the investment or transfer of funds), (ii) accepting or keeping funds of investors and/or companies or borrowers, (iii) the platform making investments on behalf of investors, or (iv) the platform enabling the operator of the platform to dispose of funds or financial assets (even on the basis of specific instructions only), need to be carefully analyzed. In particular, services provided by the operator of the platform in connection with (i) the flow of funds, (ii) keeping securities, or (iii) keeping accounts of investors will most likely bring a platform operator within the scope of the money laundering regulations as it will be considered a financial intermediary subject to the AMLA.

### 3.5 Consumer Credit Act

#### 3.5.1 General Rule

According to the Swiss Consumer Credit Act (*Konsumkreditgesetz*, CCA), a Person regularly acting as a consumer credit broker is required to obtain an authorization from its canton of residence for the provision of such services.





A *consumer credit agreement* is defined as an agreement according to which a Person who regularly grants credits in the course of its business (creditors) grants or promises to grant a credit to a consumer in the form of a deferred payment, a loan or a similar financial accommodation. Credit agreements entered into by creditors who do not regularly grant loans are not considered to be *consumer credit agreements*. Furthermore, certain consumer credit agreements are excluded from the scope of the CCA, in particular those with an amount of less than CHF 500 or exceeding CHF 80,000, those with a duration of less than three months or those repayable in maximum four instalments during a period of twelve months.

Besides the authorization requirement for consumer credit brokers mentioned above, the CCA requires that *consumer credit agreements* comply with certain material and formal requirements and that the consumers shall not be obliged to pay any compensation to a credit broker.

### 3.5.2 Legal Consequences for Crowdfunding Platforms in Switzerland

Crowdfunding platforms (including debt-based platforms) do normally not grant credits falling under the definition of a consumer credit mainly because the lenders normally are not Persons who regularly grant credits in the course of their business. However, should the credit agreements offered on the platforms be qualified as *consumer credit agreements*, the operators of such platforms would most likely qualify as consumer credit brokers and thus require authorizations from their canton of residence. To avoid such qualification, operators of lending platforms exclude lenders who regularly grant credits in their professional capacity.

### 3.5.3 Prospectus Requirements

In case equity securities or bonds are publicly offered for subscription, the issuing company needs to establish and issue an issue prospectus containing certain information regarding, *inter alia*, the company and its business activities. Generally speaking, any invitation to subscribe for equity securities which is not addressed solely to a limited number of Persons is considered as a public offer.

According to our knowledge, Crowdfunding platforms in Switzerland are not making any public offers for their own equity or debt securities. Therefore, they are generally not subject to the prospectus requirements under Swiss law. If in a particular case, an issue prospectus is required, the company itself would be the one obligated to produce, issue and publicly distribute such prospectus to the investors.

Despite the obligation to produce an issue prospectus lying with the companies offering their shares publicly, one needs to keep in mind that anyone who, upon the issuance of shares, intentionally or negligently contributed to an issue prospectus (or similar distribution material) containing incorrect, misleading or incomplete information, is liable to the acquirers of such newly issued and publicly sold shares for any damage caused in connection with the public offer of such shares. Accordingly, operators of platforms should put adequate measures in place to limit the risk of such prospectus liability.





## 4 Lessons learned from Switzerland's regulation for a possible harmonized European Crowdfunding regulation

### 4.1 Role model ("dos")

Currently, the Swiss prospectus requirements are limited (no pre-approval for non-listed securities), which allows companies to raise funds at relatively low cost.

Another positive aspect regarding the Swiss regulation is the flexibility it gives. It is advisable also in regard to a possible harmonized European Crowdfunding regulation to retain some flexibility whether and how to regulate Crowdfunding platforms as "institution similar to an exchange". This allows the regulation to be tailored to the size and business model of Crowdfunding platforms.

This flexibility is supported by an open and constructive attitude of regulators, who are open to a dialogue to ensure that Crowdfunding platform are implemented in compliance with applicable laws.

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

We can learn from the Swiss system that the flexibility of the regulatory framework has a downside: the case-by-case approach leads to legal uncertainty and higher costs for platforms, because the authorities as well as the Crowdfunding platform's operators need more time and resources to evaluate the requirements and legality of the operator's activities because there is no standardized procedure.

Moreover, the overall uncertainty and the lack of *de minimis* exemptions or specific exemptions for Crowdfunding prevents further growth in this area.<sup>72</sup> It is regrettable that also the planned bills for an FSMA, an FMIA and a FinIA do not provide any exemptions.

## 5 Conclusion

In 2013, CHF 11.6 million was collected through Crowdfunding in Switzerland. This is more than twice the volume of 2012. Nevertheless, Swiss Crowdfunding market remains rather small in comparison with the USA, Germany, and France.

There is currently no specific legislation or regulation in Switzerland explicitly addressing Crowdfunding platforms in Switzerland. However, there are several laws and regulations which may, under certain circumstances, be applicable to Crowdfunding platforms. Depending on the services provided and on the specific business model, Crowdfunding platforms (irrespectively whether they operate an Equity or Lending Model) may require particular a banking license, a license as securities dealer, a license as an institution similar to an exchange and/or a license under the CISA. Nevertheless, Crowdfunding platforms can be structured with minimal regulatory constraints and some platforms obtained a no-action letters from FINMA, confirming that the platforms as operated do not fall under the scope of application of neither the Swiss Federal Act on Banks and Savings Banks, the Federal Act on Stock Exchange and Securities Trading, the Federal Act on Collective Investment Schemes nor the Swiss Anti-Money Laundering Act.

<sup>72</sup> Cf. SECO, Diskussionspapier, p. 14; HETTICH, PETER, Finanzierungsquellen für KMU im Zeitalter von Crowdfunding, GesKR 2013, 386 et seqq., p. 396.



While Crowdfunding received some media attention, this did not create an impulse for political player to act. Quite to the contrary, three regulatory initiatives, namely the bill for a FMIA as well as the draft bills for a FSMA and a FinIA do not address Crowdfunding in any way, although they may have a material impact on Crowdfunding platforms.

The Swiss regulation contains some positive aspects such as the granting of flexibility to authorities and the Crowdfunding platforms as well as limited prospectus requirements. However, it also bears some negative aspects such as the assessment on a case-by-case basis, which causes higher costs and legal uncertainty. The lack of Crowdfunding exemptions is also a downside. These negative aspects should be handled differently in a possible harmonized European Crowdfunding regulation.

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