Country Crowdfunding Factsheet

United Kingdom

Date: June 2018

EUROPEAN
CROWDFUNDING
NETWORK

EUROPEAN CROWDFUNDING NETWORK

European Crowdfunding Network

The European Crowdfunding Network AISBL (ECN) is the professional network promoting adequate transparency, (self) regulation and governance while offering a combined voice in policy discussion and public opinion building, incorporated as an international not-for-profit organization in Brussels, Czech Republic.

We support our members in carrying initiatives aimed at innovating, representing, promoting and protecting the European crowdfunding industry. We aim to increase the understanding of the key roles that crowdfunding can play in supporting entrepreneurship of all types and its role in funding the creation and protection jobs, the enrichment of European society, culture and economy, and the protection of our environment.

In that capacity we help developing professional standards, providing industry research, as well as, professional networking opportunities in order to facilitate interaction between our members and key industry participants. On behalf of our members, the ECN will maintain a dialogue with public institutions and stakeholders as well as the media at European, international and national levels.

This document has been extracted from Annex II of the study " Identifying market and regulatory obstacles to crossborder development of crowdfunding in the EU", published in November 2017 and funded by the European Commission (DG FISMA).

Contents

United Kingdom

Overview

The United Kingdom dominates the Crowdfunding landscape in Europe in terms of market volume per capita. The country's overall market share in Europe reached 81% with EUR 4.412m in 2015.

A. Role of alternative finance

Market size

1.09m people invested, donated or lent via online alternative finance platforms in the UK.

254,721 individuals, projects, not-for-profits and businesses raised finance via online alternative finance models.[1]

Trend

Donation-based Crowdfunding grew by 507% from GBP 2m in 2014 to GBP 12m in 2015. Equity-based Crowdfunding is the second fastest growing sector - up by 295% from GBP 84m raised in 2014 to GBP 332m (including real estate Crowdfunding) in 2015.[2]

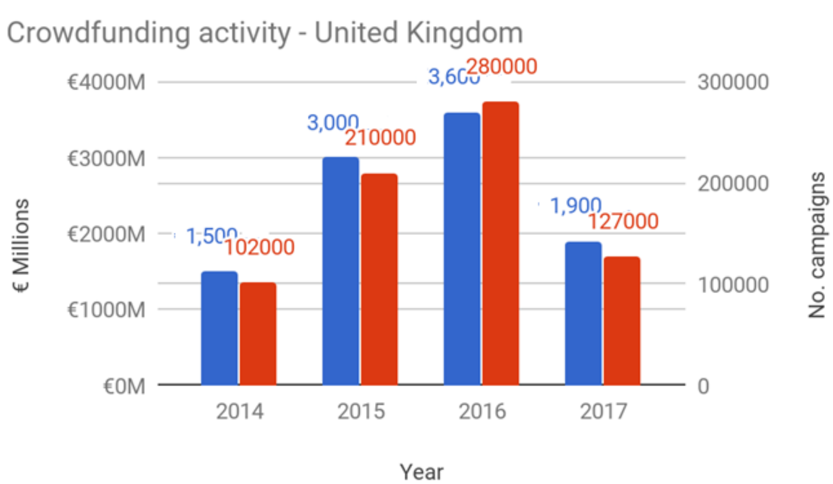

*Figure: Crowdfunding activity in UK from 2014 to 2017,*Source: TAB

[1] Zhang, B. et al (2016): Sustaining Momentum. The 2nd European Alternative Finance Industry Report. Cambridge University (link)
[2] Ibid.

Total Crowdfunding Platforms

In terms of the trends for platforms in the UK, the regulatory environment appears to have begun to act as a barrier to entry for new platforms as the cost of compliance rises and the number of new platforms declined for first time in 2015.

Crowdfunding models

Equity-based Crowdfunding	Equity-based Crowdfunding is one of the fastest growing models, up by 295%, to GBP 332m raised in 2015, compared to GBP 84m in 2014. A sizeable part, GBP 87m of the total Equity-based Crowdfunding volume, is from real estate Crowdfunding, wherein a syndicate of individuals receive a legal share of a property, typically through equity into a registered security in a special purpose vehicle (SPV) that is operated by the online platform.[3]
Lending-based Crowdfunding	Peer-to-Peer Business Lending remains the largest model by volume in the UK online alternative finance market. In total, nearly GBP 1.49bn was lent to SMEs in the UK. This represents a 99% year-on-year growth rate and 194% average growth rate between 2013-2015. Peer-to-Peer Consumer Lending reached GBP 909m in 2015, compared with GBP 547m in 2014. With a 66% year-on-year growth rate and a 78% average growth rate for the period 2013-2015, the Peer-to-Peer Consumer

[3] Ibid.

	Lending sector is growing fast and continues to provide efficient consumer credit to UK borrowers.
Other	In 2015, community shares reached GBP 61m with a 79% year-on-year growth rate, whilst pension-led funding was almost flat with GBP 23m for the year. Debt-based Securities, which allow investors to invest in both short-term and long-term renewable energy initiatives, achieved a very respectable GBP 6.2m with a 52% three-year average growth rate.[4]

B. Regulatory context

Country / Summary	United Kingdom
Recent developments in Crowdfunding regulation	• The FCA is currently in the process of concluding a post-implementation review of its Crowdfunding rules which commenced in July 2016. The interim report published at the end of 2016 focused principally on loan-based Crowdfunding and how investor protections could be strengthened but also considered the content and timing of disclosures in investor communications for both loan and investment-based Crowdfunding. Further changes are likely when the review concludes mid-2017. • From 21 March 2016, advising on P2P agreements became a regulated activity and from 6 April 2016, the FCA's client money rules were simplified for firms that that operate electronic systems in relation to lending and

[4] According to desk research of European Crowdfunding Network, referencing the state of the market in 2016, (link)

	hold money in relation to both regulated and unregulated P2P. • In January 2016, HM Treasury amended secondary legislation so that firms performing the activity of operating an electronic system in relation to lending (i.e. operators of loan-based Crowdfunding Platforms) are not regarded as operating collective investment schemes (though they may still be AIFs under the AIFMD). • On 29 March 2017, the UK government triggered the process for exiting the EU. The ramifications for the cross-border development of Crowdfunding into and out of the UK will largely depend on the basis of any transitional arrangements following Brexit as well as the outcome of the negotiations on the UK/EU relationship which will determine what arrangements apply in relation to EU legislation in future once the UK has left.
Current/planned Crowdfunding regulation	
General regulation	The Securities Model generally entails conducting a regulated securities business • FCA authorisation required For the Lending Model, the regulated activity of "operating an electronic platform in relation to lending" was introduced in April 2014 • FCA authorisation required. Donations/Rewards-based Model is not subject to financial services regulation. For the Securities Model, FCA rules restrict the promotion of "non-readily realisable securities" to certain categories of retail investor.
Prospectus requirement	Prospectus requirement for offering of transferable securities (such as shares): • Threshold: EUR 5m per issuer within 12 months. Proposed EU Commission changes will permit Member States to impose an exemption from the requirement to produce a prospectus for domestic offers of up to EUR 10m, and for non-domestic offers, a maximum raise of EUR 500,000 – although this may be subject to change given the European Parliament's current agreed position. For the Securities Model, where profit share is not channelled through a standard corporate issuer/shareholder relationship, investment may be characterised as collective investment scheme.
AIFMD regula-	For the Securities Model, to the extent that an investment

tion	amounts to a collective investment scheme: • categories of investors to which unregulated collective investment schemes are narrower than for other non-readily realisable securities. A Crowdfunding structure could constitute an AIF if it includes profit share arrangements. Light-touch regime for managers with management assets under EUR 100m: • FCA authorisation/registration and reporting requirements, but Directive marketing restrictions not applied.
Payment service regulation	• The transmission of funds between the investor and the crowdfunded business may involve the platform operator providing "credit transfer" or "money remittance" services under the Payment Services Regulations 2009 (as amended) (PSRs) implementing the Payment Services Directive in the UK. A platform operator will require separate FCA authorisation if it is conducting payment services. • Operators have historically relied on the exemption for 'commercial agents' but this is unlikely to be possible post 13 January 2018 when PSD2 takes effect. The FCA has published draft guidance on this point which, although not yet final, may mean that loan and investment-based Crowdfunding Platforms would not be considered to be providing payment services as a regular occupation or business activity, such that separate authorisation would not be required.
Further possible requirements	Money Laundering Regulations 2007: • platform operator has to verify the identity of clients. Note that the Money Laundering Regulations 2007 will be repealed from 26 June 2017 and new regulations will apply in order to implement 4MLD. From 25 May 2018, the General Data Protection Regulation will replace the UK's existing Data Protection Act 1998 and will impose wide-ranging requirements on platform operators in relation to their processing of personal data. The consequences of breaching the GDPR can be significant.
Regulatory barriers	
Inbound	**Foreign Crowdfunding Platform addressing UK investors:** • Financial Services and Markets Act 2000: Platforms carrying on a "regulated activity" in the UK will be required to

	obtain FCA authorisation as an "authorised person". The scope of the FCA authorisation required will depend on the regulated activities being carried on by the platform. Platforms based in Member States other than the UK and authorised under MiFID may be able to exercise passport rights under MiFID without having to obtain authorisation on a country by country basis. Financial promotions directed at UK recipients will also likely be subject to additional conduct of business obligations under the UK financial promotion regime. **Crowdfunding Platform from another EU country addressing companies/projects in the UK:** • Companies seeking to raise finance through issuing debt or equity securities must satisfy themselves that they are meeting any requirement to publish a prospectus (or fall within an available exemption). Contravening the prohibition in the FSMA of dealing (and other activities) in transferable securities without an approved prospectus is a criminal offence. The Companies Act 2006 also prohibits the offer of shares in a private limited company to the public.
Outbound	**UK Crowdfunding Platform addressing foreign investors:** • UK platforms targeting non-UK investors only would not be subject to UK licensing requirements or conduct of business rules provided that the fundraising activity is also taking place outside the UK (i.e. the companies or projects seeking to fundraise through the platform are non-UK based). The FCA would consider a number of different factors in determining that this would be the case. UK platforms are likely to be subject to local licensing and conduct of business requirements (depending on the scope of their activities) and so should carry out due diligence on the regulatory regime of any EU country in which they are targeting investors or investment companies/fundraising opportunities prior to launch. • As mentioned above, UK platforms seeking to passport into other EU jurisdictions under their MiFID platform would not need to obtain additional licences, but may be subject to additional conduct of business rules under the host state's regulatory regime. UK platforms should be aware of EU-based regulation including in relation to data protection, AML and consumer protection, which set out common standards which UK platforms will be expected to comply with under local implementing legislation. Similarly, companies seeking to raise finance should be aware

	of any local requirements to issue a prospectus (or conditions which must be met in order to issue shares to the public).
Impact of EU regulation	
Prospectus regulations	As a result of implementing the Prospectus Directive in the UK, the FSMA requires a prospectus to be published where transferable securities are offered to the public. Contravening the prohibition in the FSMA of dealing (and other activities) in transferable securities without approved prospectus) is a criminal offence. In addition, under the UK corporate regime, the Companies Act 2006 prohibits the offer of shares in a private limited company to the public. It is possible to structure the involvement of the platform so as to reduce the risk of breach.
AIFM Directive	A Crowdfunding structure could constitute an AIF if it includes profit share arrangements. Light-touch regime for managers with management assets under EUR 100m which is applicable to most UK-based platforms: • FCA authorisation/registration and reporting requirements, but Directive marketing restrictions not applied.
MiFID/MiFID II	The key impact of MiFID (and MiFID II from July 2018) is whether securities in question are those that fall within the MiFID definition of 'financial instrument' and, if so, the ability of the platform in question to passport their activities across Europe. There is substantial overlap between the UK regulatory regime and MiFID as you would expect but each platform needs to identify and confirm that their UK regulated activities fall within the scope of MiFID and can therefore be passported.
PSD/PSD II	The reduction in scope of the 'commercial agent' exemption under PSD2 is likely to mean that many platform operators will need to be authorised to provide payments services on the basis that the transmission of funds between the investor and the crowdfunded business can involve the platform operator providing "credit transfer" or "money remittance" services.

C. Disclosures & safeguards

Fundraisers are protected by the Consumer Credit sourcebook (CONC) and the Conduct of Business Sourcebook (COBS). A platform should consider highlighting key risks to the borrower including the consequences of missing payments or underpaying, including, where applicable, the risk of repossession of the borrower's property.[5]

Before a P2P agreement is made, the platform must grant that the agreement is adapted to the borrower's needs and financial situation.[6]

Both, the UK Crowdfunding Association and the Peer-to-Peer Finance Association have published a code of practice. Members of the associations agree with the principles laid out in the Code and the adherence of those principles is required for membership.

D. Support policies

Overview

The UK Crowdfunding sector is subject to specific regulation in the equity-based and P2P lending field. The regulatory body is the Financial Conduct Authority (FCA), which introduced a wholly new set of regulations for the P2P sector in April 2014 and, at the same time, some additional requirements for equity-based Crowdfunding Platforms. Prior to this, the P2P sector was not formally regulated, as it was not considered to fall under any existing regulatory regime. The regulations require that platforms operating in the sector must be authorised (Licensed) and conform to standards set out by the FCA.

The equity-based sector has always been regulated, however additional regulations dealing specifically with Crowdfunding activities were also introduced in April 2014. These will be reviewed and amended if deemed necessary. Primarily, the regulations require platforms to be authorised (Licensed) or to have regulated activities managed by authorised parties, and a screening process must be in place to sort sophisticated and non-sophisticated investors. If an investor is deemed a "non-sophisticated" investor, constraints are placed on how much they are permitted to invest, in that they must not invest more than 10% of their net investable assets in investments sold via what are called investment-based Crowdfunding Platforms.[7]

Additional regulations concern the communication of the offers, the fairness, language and clarity of description used to describe these offers and the awareness of the risk associated with them.

Whilst most offerings are small enough to take advantage of the exemptions offered by the EU Prospectus Directive, there are examples where Crowdfunding activities have been conducted with properly prepared

[5] Further explanations: P2P agreements Article 4.3.3 (CONC).
[6] Further explanations: P2P agreements Article 4.3.4 (CONC).
[7] Zhang, B. et al (2016): Sustaining Momentum. The 2nd European Alternative Finance Industry Report. Cambridge University (link)

prospectuses thereby permitting higher raises to be transacted, notably the Brewdog Equity For Punks IV offer.

Whilst often viewed as a good regulatory regime, there are those that contend that they are founded in an "old world understanding of finance and motivation" and so are not sensitive to the distinctiveness of Crowdfunding models and the philosophy behind them. Survey data suggests that most platforms are reasonably comfortable with these arrangements, however, as the intention is to protect the consumer from inappropriate behaviour by platforms and those they permit onto them, this metric of acceptability to platforms may not be a good indicator of the appropriateness of the existing regulatory framework.[8]

Market Supervision

FCA - Financial Conduct Authority.[9]

State initiatives

Matching funds initiatives	SME P2P lending match funds by the British Business Bank (link). Local Business Lending Partnership Newcastle City Council and Funding Circle (link). Crowdfund Plymouth by Plymouth City Council (link). The Mayor of London Crowdfunding programme. This initiative by the Mayor is aimed at helping Londoners to crowdfund innovative project ideas that boost quality of life and the economy (link).

[8] Expert opinion of Tim Wright in CrowdfundingHub - The Current State of Crowdfunding in UK (link)
[9] FCA - Financial Conduct Authority (link)

State-aid	Department for International Development funded Crowdpower programme. GVEP international launched a three-year initiative that looks to stimulate, develop and learn from Crowdfunding into renewable energy enterprises in sub-Saharan Africa and Asia (link).
Tax benefits	There are two widely mentioned tax incentives which have been associated with Crowdfunding in the UK. The first is the Enterprise Investment Scheme (EIS), which was started in 1993 to help small, high risk companies raise capital. This plan actually replaced a previous plan, the Business Expansion Scheme (BES), which had been somewhat poorly written as many investors used it purely for tax relief and not necessarily to fund solid business operations. The EIS program allowed for investors to reclaim 30% of income tax by an approved offering. So, within the limit of GBP 1m, the 30% could add up to returning potentially GBP 300,000 of income tax to a UK investor. The Seed Enterprise Investment Scheme (SEIS) was introduced as a new programme. The SEIS was created to provide tax relief to private investors who invested in early-stage companies. Viewed as complementary to the EIS programme, SEIS is for very early-stage companies. SEIS has an annual limit of GBP 150.000 raised but this may be used in

	conjunction with EIS. The company may not have more than GBP 200.000 in assets when shares are issued, must have fewer than 25 employees, must not be listed, cannot have existed for more than 2 years and must not have received investment from a Venture Capital Trust (link).
Crowdfunding guidelines for entrepreneurs/investors	E.g. the FCA provides some guidelines for consumers (link).

E. Additional insights

Best practices

Best Practice 1 - The UK government is the most progressive with the introduction of requirements for banks to be obliged to offer alternative finance options to clients to whom they refuse loans.

Best Practice 2 - The Government created a GBP 2 Million Peer-to-Peer Impact Fund which will help people make social investments through peer to peer and Crowdfunding Platforms

Best Practice 3 - Plymouth University, The University of Surrey and Nottingham Trent University have all partnered with Crowdfunder to facilitate and fund Crowdfunding projects in the cities surrounding their campuses – enabling economic regeneration, community partnerships and business development (link).

Policy measures

The UK's government is known for its support of the online alternative finance market. The government has supported the growth of this market through direct investments (such as the more than GBP 60m lent to SMEs by the British Business Bank via peer-to-peer lending platforms) to the application of tax incentives, such as the EIS and SEIS60 which have been used by a large proportion of investors using alternative finance platforms particularly within Equity-based Crowdfunding.

In 2016, the government introduced the Innovative Finance Individual Savings Account (IFISA). This allows for peer-to-peer loan agreements to be included within the tax-free ISA tax wrapper.[10]

More information on the Innovative Finance Individual Savings Account (IFISA).

Jones, R. (2015), 'Savers could unlock GBP 300m in extra interest with IFISA Financial Reporter.

Other

Set against a period of continued subdued demand from businesses for bank finance, it is apparent that Crowdfunding is beginning to be an important source of finance to businesses. The UK government is introducing requirements for banks to be obliged to offer alternative finance options to clients to whom they refuse loans. This is likely to increase pressure on banks to engage more fully with the sector. It is worth noting that in a survey of 200 international delegates attending the University of Edinburgh Business School's Credit Risk and Credit Control conference, three-quarters felt alternative lenders now pose a threat to banks and traditional lenders. There is some way to go before this happens, but even Ian McCafferty, External Member of the Monetary Policy Committee of the Bank of England acknowledges, "we may well be seeing the early stages of some important changes to the architecture of business finance."

The generally positive stance towards Crowdfunding from the UK Government is also helpful to the sector. This encouragement can be seen through the Government's use of the British Business Bank to place funds on to a number of alternative finance platforms, the maintenance of the SEIS and EIS tax incentive scheme for investors in start-ups, and with introduction of the new P2P ISA provisions.[11]

12

[10] Zhang, B. et al (2016): Sustaining Momentum. The 2nd European Alternative Finance Industry Report. Cambridge University (link)
[11] Expert opinion of Tim Wright in CrowdfundingHub - The Current State of Crowdfunding in UK (link)
[12] Expert opinion of Tim Wright in CrowdfundingHub - The Current State of Crowdfunding in UK