Proposed Regulation on European Crowdfunding Service Providers (ECSP) for Business

Position Paper of the European Crowdfunding Network

8 October 2018

We welcome this opportunity to provide comments on the proposed European Crowdfunding Service Providers (ECSP) for Business Regulation (COM(2018)0113 – C8 0103/2018 – 2018/0048(COD)) (the "Regulation").

These comments are based on the text proposed by the European Commission (the "Commission Text"), together with the amendments proposed in the Draft Report to the European Parliament's Committee on Economic and Monetary Affairs (Amendments 1 to 136), the further amendments tabled by members of that Committee (Amendments 137 to 334) (together, the "Amendments"), and compromise amendments as they stand in advance of the meeting on 9 October 2018 (Compromise Amendments A through Y) (the "Compromise Amendments").

We have assumed for purposes of this position paper that no further amendments, beyond the Amendments, may be tabled with respect to the version of the Regulation currently before the European Parliament. Where we believe a change is required that is not reflected in an Amendment, we have noted it in this document in the hopes that it will be reflected as part of the European Council deliberations and Trialogue process.

1. Executive Summary

The European Crowdfunding Network represents 29 crowdfunding platforms from across the European Union (the "EU").

We wholeheartedly welcome the Regulation: believe it has the potential to make pan-European crowdfunding a reality, and that doing so will be of huge benefit to European startups and SMEs and to European investors. However, based on our extensive experience operating in this space, we believe that there are 16 key issues with the Commission Text and/or the Amendments which, if not addressed appropriately, would defeat or undermine the stated purposes of the Regulation.

Our recommendations are in summary the following:

- **Threshold** should be raised to €8 million. (*Article 2(2)*)
- **National licensing requirements** for project owners and investors should not apply, ensuring that the Regulation creates a fully harmonised or 29th regime. (*Article 2(2)*)
- **Definition of "crowdfunding services"** should be modified to align with existing practice, both in view of lending-based and investment-based crowdfunding. (*Article 3(1)(a)*)
- **SPVs** should be permitted to (1) hold multiple assets when professional investors or eligible counterparties are investing and (2) structure as omnibus nominee/trustee arrangements. (*Article 4(5)*)
- **Conflicts of interest** should not prohibit CSPs from having certain types of financial participation in their projects. (*Article 7*)
- **Conflicts of interest** should not prevent employees, managers and shareholders of CSP from investing *pari passu* in projects. (*Article 7*)
- **Payment services** restrictions should be clarified to ensure that CSPs can facilitate payment flows, but that they must conduct AML checks. (*Article 9(2)*)
- **Register of individual projects** should not be required. (*Article 11*).
- **Entry tests** should be based on appropriateness rather than suitability, and the outcome of an investor's simulation should not mandate the investor's exclusion. (*Article 15*)
- **Investment caps** should not be applied. (*Articles 15 and 16*)
- **KIIS** content requirements should differ between platform- and project-focused. (*Article 16*)
- **KIIS** responsibility for correctness should stay with the project owner in case of a project-focused KIIS. (*Article 16*)
- **Bulletin boards** should allow for binding reference prices and, in the case of lending-based platforms, a more comprehensive, platform-managed secondary market structure. (*Article 17*)
- **Marketing and communication restrictions** should be modified to allow general communications about live projects. (*Article 19(2)*)
- **Due diligence requirements** should not specify the information required. (*New*)
- **Default rates** disclosure should apply only to lending-based platforms. (*New*)

This position paper explains each of these 16 points in detail, and it provides our views as to the modifications to the Commission Text that should (or should not) be made in order to achieve the optimal outcomes.

2. Background

The European Crowdfunding Network represents the 29 crowdfunding platforms list on the final page of this paper. Our members are headquartered across the EU.

Together we have led the development of the crowdfunding market in Europe over the past eight years, and through that process we have learned first-hand a substantial amount about how crowdfunding works and should work, where the key risks lie and how to mitigate them, how to provide robust investor protection and maintain effective compliance processes, and what regulatory approaches help or hinder the attainment of crowdfunding's objectives.

We wholeheartedly welcome the Regulation and believe it has the potential to make pan-European crowdfunding a reality. To date, the divergence in the relevant laws between Member States has made crowdfunding a largely national affair. This has meant that the vast potential for cross-border capital flows has not been tapped, leading to substantially less funding and fewer investment opportunities across the EU than would be available under a unified regime.

At the same time, we see a number of challenges with the Commission Text which would significantly undermine—and, in some cases, entirely defeat—the stated purposes of the Regulation. And while some of the Amendments would address certain of these challenges, a number of issues still remain, and indeed some Amendments would exacerbate rather than mitigate the problems.

In this position paper, we describe and explain our main concerns with the Commission Text and the Amendments, and we propose solutions that would address those concerns. In doing so, we are guided primarily by our experience around three areas of practice:

- **Project Owners**: the practices and structures that have encouraged and helped startups and SMEs (1) to view crowdfunding as an effective and desirable source of financing; (2) to succeed in raising the funds they are seeking; and (3) to thrive and grow as businesses after their funding is completed. It is far from trivial for a business to raise funding from the crowd effectively, and then to benefit from the support of their investors without being overly burdened by the administrative challenges of a wide and disparate financing base. Through our experiences we have learned a tremendous amount about what it takes to get a business onto a platform and funded, and how to optimise for their success after funding.

- **Investors**: the approaches that have proven effective in achieving the key balance between investor protection and investor autonomy. It is essential that investors receive the information, and are subject to the screening, necessary to ensure that (1) they understand the characteristics and risks of what they are investing in; (2) their investments are structured properly; and (3) they do not invest more capital than they can afford to lose. But it is also essential, and indeed a key part of the attraction of crowdfunding for many, that investors be treated as responsible adults who, having received the information and been subject to the screening provided by the platform, are capable of making their own investment decisions. As an industry we have worked hard to strike this balance, and, based on our experiences, we believe we have been highly effective in doing so to date.

- **Platforms**: the importance of scalability to the sustainable operation of a crowdfunding platform. In order to build and maintain the legal, financial and technological infrastructure required to operate a crowdfunding platform in a highly professional and compliant manner—including, among other things, maintaining the highest standards of transparency and risk management, implementing comprehensive business continuity plans and back-up service arrangements, and operating appropriate senior manager qualification regimes—crowdfunding service providers ("CSPs") must incur a meaningful level of capital expenditure and ongoing costs. Most platforms can therefore only be profitable, and therefore operate sustainably in the long term, if they are able to achieve a sufficient level of scale. Measures that limit their ability to do so undermine the health and viability of the crowdfunding market.

We hope our views and recommendations will be seen in light of the above and considered seriously as part of the finalisation of the legislation.

3. Key Issues

We have identified 16 key issues that we believe must be addressed if the Regulation is to succeed in fostering a vibrant pan-European crowdfunding environment.

Issues	Recommendations
a. Threshold (Article 2(2)) The Commission Text would limit offerings to a maximum of €1 million per 12 months. This is highly problematic for project owners, investors and platforms: • The number of crowdfunding deals in excess of €1 million is growing quickly, and platforms across Europe are seeing demand from startups and SMEs to be able to raise larger amounts of money. Indeed, many young businesses feel that crowdfunding is most useful to them when they have already achieved initial growth and are seeking capital to scale up—rather than as a form of seed capital—and for these businesses a higher threshold is critical. • Many investors want the opportunity to invest in larger projects. While some investors are focused on smaller deals or younger companies, others are keen to build a portfolio—or include in their broader portfolio a mix—of larger deals or later-stage businesses which, generally, have a somewhat different risk/return profile. • Finally, crowdfunding platforms will only be able to achieve the scale required for profitability if they can offer larger projects alongside smaller ones. For many platforms, a substantial proportion of their revenue comes from projects that raise over €1 million, and losing the opportunity to offer these would make it very difficult for these platforms to operate sustainably in the long term. We therefore welcome and strongly support Amendments 5 and 152-155 (which are incorporated in Compromise Amendment V, amending Recital 12) and 30 and 191-195 (which are incorporated into Compromise Amendment A, amending Article 2(2)(d)). These would **raise the threshold to €8 million in line with the maximum threshold in the Prospectus Regulation**. We think this is an appropriate level in light of where the market currently stands and platforms' need for scale and sustainability. In addition to these Amendments, we would recommend a further set of amendments to Recital 12 and Article 2(2)(d) to establish that the €8 million threshold is measured based on investment from residents of EU Member States. This would align the Regulation more closely with the Prospectus Regulation, and it would accommodate the needs of platforms that operate both inside and outside the EU.	Amendments • Adopt Compromise Amendments A and V (incorporating Amendments 5, 30, 152-155 and 191-195). Other Changes/Recommendations • Further amend Recital 12 and Article 2(2)(d) to establish that the €8 million threshold is calculated based on investment from residents of EU Member States.

Issues	Recommendations
b. <u>National licensing requirements (Article 2(2))</u> A substantial challenge for many CSPs, including especially those that operate lending-based platforms, has been the licence requirements imposed by some Member States on project owners and investors. In some cases, national law has even required borrowers to obtain licences for deposit-taking and lenders to obtain licences for the provision of credit. If such licence requirements were maintained, they would effectively prohibit the application of this regulation in the Member States in which they apply and therefore undermine the very purpose of an EU-wide regulatory framework. We therefore welcome and strongly support Amendments 190 and 198, which would **add a provision that ensures that national licence requirements do not prevent project owners and investors from using platforms operated by CSPs authorised under the Regulation**. This is an essential change in order for the Regulation to create a truly pan-European framework. Along similar lines, but more broadly, we are conscious that there has been some discussion (if not Amendments) that would change the structure of the regime created by the Regulation from that of a 29th regime to a minimum standards approach. If pursued, this would allow Member States to impose further rules or licence requirements on CSPs (or, indeed, project owners or investors) beyond what is contemplated by the Regulation. We would strongly oppose such a move. In order for the Regulation to be effective in its aims, it is essential that CSPs—many of whom are relatively small businesses—not be faced with the burdens of identifying and complying with different regulations in 28 separate Member States. **It is essential, in our view, that the rules established by the Regulation represent a 29th regime (or else complete harmonisation), and not merely a set of minimum standards to which Member States can make additions.** We therefore oppose these Amendments and any move away from a fully harmonised/29th regime.	<u>Amendments</u> • Adopt Amendment 190 or 198 <u>Other Changes/Recommendations</u> • Maintain the current 29th regime approach, or implement full harmonisation, but do not change to a minimum standards approach.

Issues	Recommendations
c. Definition of "crowdfunding services" (Article 3(1)(a)) The definition of "crowdfunding services" in the Commission Text is the subject of a number of proposed Amendments. We are not commenting on most of these, although we are broadly happy with the basic structure put forth as part of Compromise Amendment B. However, we would highlight four changes that we do think need to be made in order to reflect the realities of how crowdfunding models are intended to, and do, work in practice. • As mentioned below, **we do not think it is appropriate to include "the offer of investment advice"**, as referred to in point 5 of Section A to Annex I to Directive 2014/65, as one of the activities conducted by CSPs. • However, in addition to the two other MiFID activities already described in this provision ("placing without firm commitment" and, added by Compromise Amendment B, "reception and transmission of client orders"), **we think it is essential to add "execution of orders on behalf of clients"**, as referred to in point 2 of Section A to Annex I to Directive 2014/65. This is an inherent part of what most investment-based crowdfunding platforms do, and in the absence of its inclusion, it is not clear that the Regulation will actually most investment-based crowdfunding activity. • With respect to all crowdfunding models, **it will be important to establish that platforms can provide ancillary services related to their main activities**. We would make this explicitly clear, and we also think that the deletion of the parenthetical "(among others)" from Compromise Amendment B, Part I, should be removed. • Finally, it should be clarified that both "Direct" and "Intermediated Crowdfunding Services" includes lending-based crowdfunding. This does not seem clear based on some of the changes in the Compromise Amendments.	Amendments • Reinsert "(among others)" into the text covered by Compromise Amendment B, Part I Other Changes/Recommendations • Exclude "the offer of investment advice" from the definition of "crowdfunding services" • Include "execution of orders on behalf of clients" in the definition of "crowdfunding services" • Include "ancillary services" in the definition of "crowdfunding services" • Ensure that lending-based crowdfunding is appropriately covered by these definitions

d. SPVs (Article 4(5))

The Commission Text contains a set of restrictions around the use of SPVs. We understand and support the Commissions desire to prevent regulatory arbitrage by other types of financial intermediaries, as well as to ensure that crowdfunding is not used to package complex or exotic projects into pooled vehicles that are then offered to retail investors.

However, there are two substantial problems with the current language that would inadvertently restrict important aspects of crowdfunding activity:

- The first issue is that while complex SPVs (i.e. those that invest in multiple assets, where the investor is not making the individual investment decision with respect to each asset) may not be right for retail investors, they can be, and are, used effectively by professional investors and eligible counterparties. Governments, policy banks, investment funds (such as the EIB and the EIF) and other professional investors and eligible counterparties provide finance to small businesses through crowdfunding platforms, and they typically choose to invest through SPVs. A blanket prohibition on all multi-asset SPVs is therefore overly restrictive and undermine the ability of this Regulation to help facilitate access to finance by small businesses. **It is therefore essential that the restriction on multi-asset SPVs be narrowed to apply only to retail investors**.

- Second, the limitation that SPVs may only hold a single asset fails to provide for nominee and trustee structures. We support the idea that where SPVs are used, investors should be the ones making the investment decision with respect to the underlying asset. One way to achieve this is, as envisioned by the Commission Text, to establish a separate legal entity (a "traditional SPV") for each project. However, **another common approach is the use of an "omnibus" vehicle that acts as nominee or trustee for investors (an "omnibus SPV").** As with a traditional SPV, use of an omnibus SPV achieves the crucial objective of ensuring that there is only one legal shareholder or noteholder representing all investors, which allows for greater investor protection and reduced administrative burden. And also as with a traditional SPV, investors under an omnibus SPV retain full control over their investment decisions, as the nominee or trustee only holds the asset selected by each investor on that investor's behalf. However, in some jurisdictions the use of an omnibus SPV can have significant advantages over a traditional SPV, including the passing tax reliefs through to investors and avoiding of the costs of maintaining hundreds or thousands of separate vehicles. As a result, many project owners, investors and platforms have a strong preference for an omnibus SPVs in lieu of traditional SPVs, and so it is essential that their use be permitted under the Regulation.

Amendments 163 and 222 address the first issue effectively, and we support them. Amendment 223, which has been taken up in Compromise Amendment C, is similar but would only cover eligible counterparties, which is too narrow.

To address the first issue, however, a new amendment to Article 4(5) is needed to establish that omnibus SPVs of the type described above may be used. Amendments 41 and 47 may not make sense in light of that new amendment, so we would recommend their rejection at this stage, although aspects of their content may be sensibly included in the new amendment.

Amendments

- Adopt Amendments 163 and 222.
- Reject Amendments 41, 47 and 223.
- Reject Compromise Amendment C.

Other Changes/Recommendations

- Amend Article 4(5) to allow for nominee and trustee structures (omnibus SPVs) as well as traditional SPVs.

Issues	Recommendations
e. <u>Conflicts of interest—CSPs (Article 7)</u> The Commission Text includes a prohibition on CSPs from having financial participation in the projects they offer through their plaforms. We think this is highly counter-productive: allowing platforms to participate in projects, whether through investing their capital or charging a carry/success fee, does not create a conflict of interest in practice; instead, so long as the participation or fee is disclosed and does not benefit from preferential treatment, it serves to align the interests of the CSPs with its investors. Moreover, a platform may have to invest in projects in order to ensure the integrity of the marketplace, in particular when considering buying back certain investments from investors. A number of the proposed Amendments address in different ways, but the approach that has been put forward as paragraph 1 of Compromise Amendment F, and in Compromise Amendment X for the Recitals, is by far the most sensible. We understand the intent behind the language in some amendments, which would have required that financial participation by CSPs but only if done uniformly across all offers or as a matter of intervention for integrity reasons. The problem is that, in many cases, this would still be too narrow, especially for investment-based crowdfunding. There may be a number of cases in which, for example, the project owner does not want to accept investment from the CSP, or where a different carry fee is negotiated, and these Amendments would deny any flexibility to the CSP or the project owners. Therefore, **the approach of allowing flexible participation, but requiring it to be disclosed and transparent, is the optimal solution, and we fully support it**.	<u>Amendments</u> • Adopt paragraph 1 of Compromise Amendment F. • Adopt the part of Compromise Amendment X covering financial participation by CSPs. • Reject the other Amendments put forward on this subject.

f. Conflicts of interest—employees, managers and major shareholders (Article 7)

The Commission Text also proposes a prohibition on CSPs' employees, managers and major shareholders, along with persons connected to them, investing on projects through their platforms. This is an unnecessary and counterproductive restriction, for much the same reasons as discussed above for the CSPs themselves. So long as the relevant people are investing on the same terms as external investors (*pari passu*), the result will be an alignment, rather than a conflict, of interests.

The alignment of interests between the platforms' management and retail investors can be a very strong protection of the latter, as it is a safeguard against acceptance of low-quality projects in favour of maximising volume. Meanwhile, by allowing people connected with CSPs the opportunity to use the platform as investors, they can better understand the investor experience and help improve the platform for other external investors. Finally, such restrictions would prevent the emergence of new platforms, that rely for the financing of the first projects on managers, employees and their "friends and family" to achieve the required financing as they do not initially have the necessary active investors base.

Again the proposed Amendments take different approaches, but none address the issue satisfactorily:

- Amendments 9 and 54, which are combined in Compromise Amendments F and X, would disapply the restrictions from employees, so that only managers and major shareholders would be restricted from investing. While this is an improvement, we see no more point in restricting managers and major shareholders than in restricting employees: in all cases, their investments align interests rather than create conflicts, so long as they are on the same terms and disclosed. We therefore support these Amendments as a starting point but feel the changes also need to cover managers and shareholders.

- Meanwhile, Amendment 55, which is also included in Compromise Amendment F, would then require that employees who do invest in projects not have any influence over them. This, too, seems counterproductive: employees are often in a position to positively influence projects, such as by recommending vendors or partners to them, testing their products or otherwise bringing value, and such positive influences would be of benefit to all investors in the company. And it is difficult to envision a set of circumstances in which an employee with a financial interest in a project would seek to negatively influence the business. We oppose these Amendments as well.

- Amendments 232 and 233 would each make Article 7(2) even more restrictive than the Commission Text, so for the reasons explained above, we oppose them as well.

Instead we strongly recommend that Recital 19 and Article 7(2) be amended to **remove the prohibition on employees, managers and major shareholders investing through platforms altogether, so long as their investments are disclosed and are made on the same terms as external retail investors**. We would also delete Article 10(2)(j), as it is no longer necessary if these changes are made.

Amendments

- Adopt paragraphs 2 and 3 of Compromise Amendment F.

- Adopt the part of Compromise Amendment X covering financial participation by employees, managers and major shareholders.

Other Changes/Recommendations

- Further amend Recital 19 and Article 7(2) to allow managers and major shareholders, and not just employees, of CSPs to invest through their platforms so long as the investments are made on the same terms as external investors and are disclosed.

- Delete Article 10(2)(j).

Issues	Recommendations
g. Payment services (Article 9(2)) The proposed requirement in the Commission Text that crowdfunding platforms obtain a payment services licence in order to handle clients' funds (Article 9(2) is overly broad and fails to reflect the way that crowdfunding operates in practice. While every platform is slightly different, the generally accepted approach taken by investment-based and lending-based crowdfunding platforms is to (1) collect funds from investors via bank transfer, debit card or similar payment mechanism, (2) have those funds held in a segregated account at a deposit-taking bank and (3) either distribute those funds to the project (if an investment is completed), send them back to the investor (if the investor requests) or else have the bank continue to hold them pending investment by the investor. In each part of this process, both the payment services and the holding of client funds are being conducted by authorised payment or credit institutions, but the platform is responsible for the facilitation and instruction of the payment flows and client funds holding. As currently drafted, Article 9(2) could be seen to prohibit this sort of facilitation, which would dramatically limit the ability of CSPs to conduct their business while providing very limited additional protection for clients. We therefore strongly recommend that Article 9(2) be amended to **ensure that such facilitation is permitted**. At the same time, one proposal not included in the Commission Text or Amendments, but which we think would be sensible, would be to **require platforms to conduct anti-money laundering (AML) checks on their users**. This, we believe, would address much of the concern that Article 9(2) is aiming at but would do so in a significantly more practical way and leave the implementation of the Payment Services Directive to the Member States. Finally, some platforms **operate as registered Payment Agents** (in the sense of Article 4(11) and Article 19 of Directive 2015/2366/EU) of payment service providers. This can be an effective approach for certain platforms as well, but the Commission Text does not explicitly allow for it. Amendment 239 would rectify this, and we support it.	Amendments • Adopt Amendment 239. Other Changes/Recommendations • Amend Article 9(2) to ensure that platforms may facilitate payment services in line with current accepted practice. • Amend Article 9(2), or another appropriate provision in the Regulation, to require CSPs to conduct AML checks on their clients.

Issues	Recommendations
h. Register of individual projects (Article 11) The Commission Text contemplates a register of all authorised CSPs (Recital 27; Article 11), and we are supportive of this. However, Amendments 161, 266 and 267 would expand that register to include all live crowdfunding projects on all platforms. **We do not think such an expanded register is advisable,** for three reasons. • First, it would result in projects that are not comparable (due to differences in platform structures and approaches) being presented alongside each other, potentially leading to investor confusion. • Second, it has the potential to undermine the ability of platforms to compete with each other and thereby achieve scale. • Finally, it is likely that maintenance of such a register would impose significant practical and technical burdens on platforms. We therefore oppose these Amendments.	Amendments • Reject Amendments 161, 266 and 267.

Issues	Recommendations
i. <u>Entry tests (Article 15)</u> As discussed earlier in this paper, we think the Commission's approach to investor screening and qualification is a sensible one. We are therefore concerned by, and oppose, certain of the Amendments that have been proposed to it: • Amendments 288 and 291, which are incorporated in Compromise Amendment O, would have the impact of changing the entry test from one of appropriateness to one of suitability. Whereas appropriateness looks at investors' understanding of the investment and its risks, a suitability analysis requires platforms to assess investors' financial positions before allowing them to invest. **This would impose a huge burden both on platforms and on investors (the latter of whom often view it as highly intrusive to be required to provide detailed financial information or documents), and it is substantially disproportionate to the approach taken to most other forms of self-directed financial services.** In general, a suitability analysis is thought necessary only where the financial services provider is offering advice as to whether or not an investor should make a particular investment, and that is not something that crowdfunding platforms, as a matter of practice, do (as a result, and as discussed above, we think the inclusion of investment advice in the definitions section is inappropriate, and that it should be removed). Crowdfunding platforms act as brokers for one specific asset class only. They do not give any investment advice based on the individual circumstances of a certain investor. Other forms of online investment platforms much more commonly use an appropriateness analysis, and this is the approach taken by Member States that have made such test mandatory. We think that is exactly what should be done here. • Amendment 289, which is also incorporated in Compromise Amendment O, would require platforms to enquire about the investor's professional experience in crowdfunding (rather than the Commission draft, which makes such an enquiry optional). **The whole purpose of this Regulation is to help expand crowdfunding across the EU, and so in many cases investors will inherently not have had previous experience with crowdfunding. A requirement to include such an enquiry in the entry test is therefore misguided and may have the effect of excluding many of the investors whom this Regulation is specifically intended to reach.** • Finally, while we support the idea of offering simulations whereby investors can assess the financial impact of losses, **we are very concerned about the idea contained in Amendments 295 and 296 that, if the simulation yields certain outcomes, the platform should prevent the investor from investing.** We think that will significantly deter investors from using the simulation and therefore be contrary to the educational purpose the simulation is meant to serve; it would also raise problems where investors wish to run multiple scenarios through the simulation, which in many cases may be a valuable thing for the investor to do.	<u>Amendments</u> • Reject Amendments 288 and 291, together with the parts of Compromise Amendment O that incorporate them. • Reject Amendment 289, together with the part of Compromise Amendment O that incorporates it. • Reject Amendments 295 and 296.

Issues	Recommendations
j. Investment caps (Articles 15 and 16) The approach taken the Commission Text to investor screening and qualification (Article 15) is a sensible one. It reflects well-established best practice for investor protection: it ensures that that investors understand the nature and risks and of the investments they are making, and that they are provided guidance on the maximum proportion of their wealth that they should invest; while at the same time, these provisions preserve investor autonomy by allowing investors who have received this information and screening to make their own decisions. We therefore strongly oppose Amendments 156, 296 and 298. These **hard caps on the amount an investor can invest through a crowdfunding platform would substantially undermine the purpose and efficacy of the Regulation in two ways**: • First, they would make it significantly more difficult for startups and SMEs to raise funds. Most successful crowdfunding campaigns consist of investments of a range of sizes, from very small to ones that are well in excess of the proposed caps. These larger investments, which are generally made by high-net-worth investors, are nearly always essential to the successful completion of a campaign, and in their absence, crowdfunding simply does not work. • Second, these caps would discourage many investors from participating in crowdfunding. One of the main attractions of crowdfunding to many investors is the independence it gives them to make their own investment decisions. And for higher-net-worth investors, crowdfunding is often only appealing if they can allocate amounts of capital (often well in excess of any proposed caps) that are meaningful to them in light of their overall portfolios. Caps on the amount that they may invest take away their autonomy and, in the case of higher-net-worth investors, make crowdfunding an impractical and unattractive way in which to allocate capital. We also question Amendments 294 and 305, which would reduce the recommended maximum investment through crowdfunding from 10% to 3% of the investor's net worth. While this is a less significant concern than hard caps, it is not in line with **common practice or advice, which tends to view 10% as a reasonable proportion of an investor's capital to be allocated to higher-risk investments**. And given that many crowdfunding investments, particularly lending-based ones and later-stage equity ones, are not in fact higher-risk, a 3% recommended maximum seems unduly conservative and unnecessary. We therefore oppose these Amendments.	Amendments • Reject Amendments 156, 296 and 298. • Reject Amendments 294 and 305.

Issues	Recommendations
k. KIIS—content (Article 16) We are supportive of the principle of the Key Investment Information Sheet (KIIS) as the way to provide investors with the necessary information to make informed investment decisions. However, we think certain changes need to be made with respect to its content. First, we would stress that the **distinction between a project-focused information sheet and a platform/performance-focused information sheet is crucial** in order to provide a framework that works both for lending-based and investment-based crowdfunding services. With regard to many lending-based crowdfunding models, investors need to learn about the platform, the performance of the loans it has generated and the credit assessment in place rather than granular project information for an informed investment decision. Amendments 98 and 307, which are combined in Compromise Amendment P) create this distinction, and we support their adoption. While we agree with and support the concept and content of the proposed platform-focused information sheet, we think the content of the project-focused information, as set out in Annex I, requires two changes: • First, in Part A(c), there is a requirement to provide a hyperlink to the most recent financial statements of project owners. This is problematic because, in many Member States, business below a certain threshold of turnover do not have the obligation to publish their financial statements. Where this is the case, and financial statements are not otherwise in the public domain, many businesses consider them highly confidential. **We therefore recommend that platforms have the option to provide key financial figures and ratios in lieu of financial statements if they so choose**. • Second, in Part B(d), there is a requirement to state the maximum offering amount if different from the target. In our experience, **many businesses do not want to define a maximum amount ahead of time**, for two reasons. One is that, if they do not raise the maximum, they worry they may be perceived as having "failed", notwithstanding that they hit or exceeded their target. The other is that, as in any fundraising round, circumstances may change while the round is ongoing: a business that intends to raise a particular amount may find that, due to new opportunities arising or a desire to accept investments from certain investors or groups of investors, it ultimately is willing to accept more. This happens all the time in a traditional, or offline, fundraising context, and it is equally common in crowdfunding. Amendment 334 would aim at the first issue, but instead of giving the option to provide either financial statements or figures and ratios, it only allows for the provision of figures and ratios. We therefore support the adoption of Amendment 334 so long as it is amended to allow for either option. We would also support the removal of Part B(d) from Annex I.	Amendments • Adopt Amendment 98 or 307, or paragraph 4a of Compromise Amendment P. • Adopt Amendment 334, but modify it to allow a choice between providing financial statements and providing figures and ratios. Other Changes/Recommendations • Delete Part B(d) from Annex I.

Issues	Recommendations
I. KIIS—responsibility (Article 16) With respect to responsibility for preparing the KIIS, we believe the Commission Text strikes the right balance. By placing responsibility for the accuracy or correctness of the KIIS on the project owner, these provisions ensure that the person or people who are closest to the details of the project bear responsibility for the information about it. Meanwhile, it is right that the CSP be responsible for the completeness and clarity of the KIIS, as they will be the ones most familiar with the applicable legal requirements and most capable of ensuring that the drafting of the KIIS is done in a way that will be clear to investors. Several of the proposed Amendments modify these responsibilities slightly and are sensible. The wording change in Amendment 18 is an improvement. We also support the principle of Amendment 97 (which is incorporated into Compromise Amendment P), which changes the wording from the terms "clear, comprehensible and correct" to "fair, clear and not misleading", but the limitation set forth in that Amendment to three sides of A4 paper is too restrictive. However, a number of Amendments, together with much of Compromise Amendment P, would shift responsibility for the accuracy or correctness of the KIIS onto the CSPs themselves. Amendments 99, 173, 309 and 310 all place the burden of ensuring that the information is correct on the CSP. **In the case of project-focused information sheets (as opposed to platform-focused ones), this is a very significant and problematic shift. It would effectively turn CSPs into auditors, raising the costs of—and increasing the time involved in—crowdfunding substantially**. Meanwhile, it is fully in the CSPs best interests, without this additional obligation, to ensure that they are sufficiently comfortable with the information provided by project owners to publish the project on their platform. We therefore oppose all of these amendments.	Amendments • Adopt Amendment 18. • Reject amendments 99, 173, 309 and 310. • Reject Compromise Amendment P (except part 4a). Other Changes/Recommendations • Amend Article 16(3) to replace the term "clear, comprehensible and correct" with "fair, clear and not misleading".

Issues	Recommendations
m. Bulletin boards (Article 17) The provisions set forth in the Commission Text with respect to secondary trading (Article 17) are largely sensible with respect to investment-based crowdfunding platforms. Our one concern is around the requirement set forth in Article 17(2) that any suggested reference price for a trade be non-binding (Article 17(2)). Small companies are often keen to ensure that their valuation does not swing wildly, and if a highly motivated seller chose to sell investments for significantly less than they were worth—or indeed a surge of buyers led the price to go significantly above what the company thinks it should be—that can cause significant problems for the company in future fundraising rounds. There is, therefore, value to be had in facilitating certain trades only at a fixed price, and while a fixed price should by no means be mandatory, prohibiting it does not seem sensible either. It is worth noting that our understanding is that the use of a fixed price would not render such a bulletin board a "multilateral system" for purposes of Directive 2014/65/EU, so long as each transaction is an individual one between buyer and seller, rather than a matched bargain system or similar arrangement). We therefore support Amendment 315, which has been incorporated into Compromise Amendment Q, **establishing that platforms must notify clients *whether* a reference price is binding or not binding, rather than that the reference price is non-binding**. **With respect to lending-based crowdfunding platforms, the bulletin board structure is impractical and does not reflect market practice of leading platforms**. Given the nature and structure of the investments on many lending-based platforms—and the market expectation of relatively complete secondary liquidity for those investments – these platforms need to be able to conduct a more comprehensive facilitation of the purchase and sale of loan agreements under a set of defined rules. This requires a platform-managed secondary market that allows platforms—in a fully transparent manner—to determine binding prices and to match sellers and buyers under certain non-discretionary rules which ensure liquidity and rule out the possibility of abuse, for example due to a pressure to sell or due to better information about a certain loan. Such platform-managed secondary markets are in the interests of retail investors, as they add flexibility and reduce the risk of abuse. We therefore support the adoption of Amendment 314, which provides for this sort of facilitation.	Amendments • Adopt Amendment 315 or Compromise Amendment Q. • Adopt Amendment 314.

Issues	Recommendations
n. <u>Marketing and communication restrictions (Article 19(2))</u> The Commission Text contains restrictions on the marketing and communication of crowdfunding campaigns (Recital 37; Article 19(2)) that are out of line with market practice and are overly restrictive and unnecessary. While every crowdfunding platform conducts its marketing and communication efforts differently, a common approach is to use communications to notify investors about new or popular campaigns and to highlight campaigns that are likely to be of interest to a wide range of investors. Doing so helps attract the most investors to the platform, where they can then see the campaign that was advertised along with all the other campaigns on the platform. **By prohibiting crowdfunding platforms from marketing or communicating about individual live campaigns, the Regulation will make it much more difficult for platforms to attract investors. This harms not only the campaigns that would otherwise have been advertised but all campaigns on the site, and it therefore has the opposite impact of what we understand the Commission to have intended.** At the same time, we think the risk of platforms unfairly discriminating between campaigns is very low. It is in the interest of all platforms to maximise the likelihood that each campaign it hosts will get funded, and so no platform is likely to engage in activities that would hurt or other reduce the funding chances of any of its campaigns or the trust it has worked to build with its investors. Amendments 107 and 320, which would amend Article 19(2) by prohibiting platforms from "disproportionately target[ing]" individual campaigns, rather that barring outright any mention of them, would be an improvement on the Commission Text, but they still impose a restriction that is unnecessary and unhelpful. Instead, we think Amendment 318, which would delete the restrictions in Article 19(2) altogether, is the only sensible approach here, and we think Recital 37 should similarly be deleted. Amendments 21 and 174-176, which make wording changes to Recital 37, and Amendment 319, which modifies Article 19(2), do not improve the situation and so should be rejected. As a separate point, we agree with the language in Article 19(4) that prohibits national competent authorities from requiring ex ante notification and approval of marketing communications, and we support Amendment 322, which would **extend this prohibition to ESMA as well**. Finally, we would note for purposes of later discussion that a sensible alternative approach to marketing and communications restrictions would be to separate the two concepts. To the extent that "marketing" is defined as actively promoting and encouraging investment in a particular project, whereas a "communication" about the project merely announces its existence and contains information about (and link to) it, it could make sense to apply a set of restrictions to "marketing" but not to "communications".	<u>Amendments</u> • Adopt Amendment 318. • Adopt Amendment 322. • Reject Amendments 21, 107, 174-176, 319 and 320. <u>Other Changes/Recommendations</u> • Delete Recital 37. • Consider defining "marketing" and "communications" separately, with restrictions imposed on marketing but not on communications.

Issues	Recommendations
o. <u>Due diligence requirements (New)</u> The Commission Text does not propose a defined set of due diligence requirements that platforms must conduct on project owners. We think this is sensible**: in our experience, defined due diligence requirements tend to be counterproductive, as they turn due diligence into a "tick-box" exercise rather than the subjective evaluation that it is intended to be**. Instead, we think platforms should each determine what due diligence they feel appropriate for their particular projects and then be transparent with their clients about the process they conduct. We therefore oppose Amendments 226 and 282, each of which would impose a specific set of checks each platform needs to conduct. While most of the checks identified are ones that platforms would be likely to conduct anyway, we think the impact of these lists will be to narrow rather than broaden what platforms do in practice. We are also particularly concerned by point 3 of Amendment 282: while transparency with respect to process is important, the need to disclose the exact checks conducted on individual projects could have significant privacy and data protection implications. In any crowdfunding exercise, the project owner is likely to disclose significantly more information to the platform than it wants in the public domain; if the platform then has to pass much of this information on to all investors, it is likely that project owners will either be less forthcoming in the information they provide or eschew crowdfunding altogether.	<u>Amendments</u> • Reject Amendments 226 and 282.

Issues	Recommendations
p. Default rates (New) The Commission Text does not include any reference to disclosure of investment performance, but Amendments 279, 283 and 284, which are combined into Compromise Amendment N, would require platforms to disclose default rates. We fully support this approach in the context of lending-based crowdfunding platforms (and, in the case of the platform-focused KIIS, would expect the default rates to be an inherent part, among other performance indicators), **but in the context of many investment-based platforms a focus on default rates as the relevant measure does not make sense**. Platforms which offer the equity of early-stage businesses are, due to the nature of this asset class, likely to see a high proportion of those businesses fail. These platforms will therefore have high "default rates". However, the objective in making investments early-stage equity is for those businesses that succeed to return many multiples of capital invested, so that the investor's overall portfolio has a strongly positive return. As a consequence, default rates on their own do not tell investors very much about their likely returns from an investment-based platforms. We are not convinced that there is a need to require investment-based platforms to make disclosures about performance at all, because most platforms will do so anyway as a result of market demand. However, if there is a desire to mandate performance disclosure, we would be supportive of that, but we would strongly recommend that it be done by requiring platforms to disclose the full performance picture, including returns realised, implied performance (of investments that have not yet been realised) and defaults or failures.	Amendments • Reject Amendments 279, 283 and 284, but modify them to cover only lending-based platforms. • Revised Compromise Amendment N to cover only lending-based platforms. Other Changes/Recommendations • Consider a requirement around broad performance disclosure for investment-based platforms.

4. Conclusion

We reiterate that we welcome the Regulation and are enthusiastic about the positive impact it will have on European startups and SMEs and on European investors. A harmonised regime will at last make it possible for CSPs to provide their services on a fully cross-border basis within Europe, and with this will come an increase the volumes, quality and professionalism of crowdfunding across the continent.

However, the 16 issues we have discussed in this paper are critical ones, and in the absence of satisfactory solutions to them, the impact of the Regulation will be significantly less, and in the case of some of these issues, the Regulation will not serve its intended purposes at all. We are therefore very hopeful that our recommendations above will be adopted.

We are available at any time to discuss the contents of this paper or any related matters.

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Respectfully submitted by:

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