

The European Crowdfunding Industry Response to:

Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the prospectus to be published when securities are offered to the public or admitted to trading (the “Proposal”).¹ COM/2015/0583 final - 2015/0268 (COD)

A joint response and proposed amendment to the Proposal by the European Crowdfunding Network, the UK Crowdfunding Association and Financement Participatif France (FPF), the French crowdfunding association.²

1. Executive Summary

- 1.1. The European Crowdfunding Network, the UK Crowdfunding Association and Financement Participatif France and their respective members from across Europe welcome the review of the Prospectus Directive. The European crowdfunding industry supports the proposal to allow Member States to introduce exemptions from the requirement to produce a Prospectus for offerings up to €10 million. However, there are serious concerns regarding the proposed limitation of this exemption to “domestic offers” and we ask the Commission to review and amend this aspect of the Proposal. The proposed “domestic offer” exemption is a retrograde step that will adversely impact SMEs’ ability to raise finance in the EU via crowdfunding. The Proposal leaves growth SMEs in a difficult fundraising position once they reach a relatively low funding requirement. Unless the exemption allows cross-border investment, the cost of producing a Prospectus will lead many SMEs to avoid seeking cross-border investment.
- 1.2. To address these concerns, the European crowdfunding industry proposes that the exemption from a Prospectus under Article 3 of the Proposal does not apply as proposed only to offers “made only in that Member State” but applies to offers made across the EU.
- 1.3. The terms “Domestic offers” and “offers made only in that Member State” are not defined in the Proposal which leads to legal uncertainty. The Proposal does not adequately explain or justify the rationale for proposing to limit the exemption to domestic offers. Crowdfunding is an online activity so offers are accessible anywhere and the Proposal should reflect that market development. We ask that European law be made fit for today’s markets and for future generations.
- 1.4. The Proposal’s Impact Assessment appears to base the entire crowdfunding industry legal and market analysis upon the response of a single unsubstantiated respondent to the Prospectus Directive public consultation, ignoring ESMA and European Court of

¹ http://ec.europa.eu/finance/securities/prospectus/index_en.htm#151130

² Please see final page for contacts of each organisation.

Justice legal review and the Commission’s own industry data. The Impact Assessment does not take account of key information or best available legal and industry analysis such that further analysis is required before implementing the Proposal. The problems with the Impact Assessment include an unjustified and arguably incorrect interpretation of the current Prospective Directive in relation to cross-border investment and the use of dated and incorrect data regarding the crowdfunding industry. Current industry data demonstrates that average European equity fundraise size was €450,161 in 2015 and that if current growth rates continue, this average will rise to €618,971 in 2016 and €1,244,245 by 2020. Crowdfunding campaigns that raised over €500,000 in 2015 represent over 80% of the total of €356 million raised via equity crowdfunding in Europe. This data demonstrates that the proposed threshold of €500,000 under Article 1(3)(d), below which the Prospectus Directive will not apply to cross-border fundraises, should be reconsidered and increased and that Member States should be free to apply an exemption up to €10m for offers across Europe. This submission sets out further legal and industry analysis in section 3 below which we ask is used as the basis for reconsidering Article 3 of the Proposal.

- 1.5. Limiting the Article 3 exemption to the proposed “domestic offers” is contrary to the goals of Capital Markets Union and the country-of-origin principle applied in the Prospectus Directive by the identification of an issuer’s home Member State as the appropriate competent authority to rule on the Prospectus Directive. The proposal will lead to less cross-border investment activity than at present.
- 1.6. Allowing exempt offers up to €10m to apply to offers across the EU rather than to domestic offers will not reduce investor protection, which is provided by rules on disclosure and liability outside of the Prospectus Directive and will greatly enhance the proper functioning of the market for investment in SMEs. The twin goals of the Prospectus Directive review process - investor protection and fostering SME investment from across the EU - will therefore be supported to the benefit of European SMEs. Greater harmonization can be achieved by increasing the threshold below which the Prospectus Directive does not apply.

2. Proposed Amendment to the Proposal.

2.1. We propose that Article 3 of the Proposal is amended as follows:

“Article 3(2)

A Member State may exempt offers of securities originating in that Member State, to the public in all Member States, from the prospectus requirement of paragraph 1 provided that the total consideration of the offer is less than a monetary amount calculated over a period of 12 months, which shall not exceed EUR 10 000 000.

Member States shall notify the Commission and ESMA of the exercise of the option under this paragraph, including the consideration of the offer chosen below which the exemption applies.”

2.2. This amendment deletes the wording that “the offer is made only in that Member State” and the reference to “domestic offers” which we submit are contrary to the

objectives of the Prospectus Directive of investor protection and the proper functioning of markets, for the reasons outlined in this submission.

- 2.3. Recital 13 of the Proposal should be amended accordingly and the recital updated to ensure that the Proposal has an objective of cross-border investment while preserving investor protection.

3. Proposal Impact Assessment Review

- 3.1. We appreciate the Commission's acknowledgement in the Impact Assessment that securities-based crowdfunding has been a particular market development that has led the Commission to consider that "some thresholds [in the Prospectus Directive], including those not amended by the review in 2010, might need to be re-calibrated." This submission represents the views of the leading crowdfunding platforms in Europe and their industry bodies the European Crowdfunding Network and the UK Crowdfunding Association. These industry bodies include platforms from Austria, Finland, France, Germany, Spain, Sweden, the Netherlands, Belgium and the United Kingdom.

- 3.2. The crowdfunding industry does not feel that the Proposal's Impact Assessment is based on the correct interpretation of the current Prospectus Directive's application to cross-border investment and we set out our alternative interpretation below. We also do not believe that the Prospectus Directive consultation response included submissions from enough crowdfunding stakeholders and we wish to remedy this now while the Proposal remains under consideration.

3.3. Legal Analysis

- 3.3.1. The Impact Assessment includes a brief and unexplained interpretation of the application of current Prospectus Directive requirements around Europe for a single issuer as follows:

"Currently, platforms and companies wishing to raise funds via crowdfunding need to consider each Member State as a domestic market in respect of the prospectus requirement and to carry out a country-by-country analysis before addressing investors across borders."

A review of responses to the Prospectus Directive consultation³ shows that this analysis appears to reflect a single respondent's view.

³ <https://ec.europa.eu/eusurvey/publication/prospectus-directive-2015?language=en#>

- 3.3.2. This does not represent a proper legal analysis of the current Prospectus Directive requirements in relation to cross-border investment and the issue of Member States having implemented Article 1(2)(h) with differing Prospectus requirement thresholds ranging from €100,000 to €5,000,000. There is industry and regulator confusion and divergent interpretation and application of Article 1(2)(h) and whether a home Member State exemption threshold applies in host Member States. It will be helpful to finally clarify this in the Prospectus Regulation for the benefit of SMEs and to make it clear that the country-of-origin principle does indeed apply such that home Member States' prospectus exemptions apply in host Member States. The clarification should not be a backwards step for European integration and harmonization which would be the case if the current Proposal Article 3 is not amended to remove the "domestic offer" aspect.
- 3.3.3. ESMA has not provided an opinion or advice on this point⁴ other than to state that the Prospectus Directive may not apply to offers below €5m. The European Court of Justice has not ruled on the divergent implementation of Article 1(2)(h) by Member States. However, there is opinion on the matter from the Advocate General of the ECJ that questioned whether Member States have authority to require a prospectus for an offer below the threshold set out in Article 1(2)(h) at all.⁵ The opinion of Advocate General E. Sharpston in ECJ case C-441/12 casts significant doubt on the legal status of divergent Prospectus exemption thresholds where she states:

“39. If that is indeed the Commission’s view, it seems to me to be mistaken. The Prospectus Directive is a harmonising measure, one of whose fundamental aims is to provide a ‘single passport’ enabling issuers to raise capital in all the Member States. That aim would be set at naught if the threshold for the application of the requirements of the Prospectus Directive — of which the most central, on which all the others are based, is the obligation to publish a prospectus — differed between Member States.

41. If the intention of the legislature had been to require Member States to impose an obligation to publish a prospectus where the total consideration exceeded EUR 2 500 000 (or, subsequently, EUR 5 000 000), to preclude them from imposing that obligation where the consideration was under EUR 100 000 and to allow them the option of imposing it or not where the consideration lay between those two amounts, it seems to me that the intention could have had to be made considerably clearer. As the matter stands, I can find nothing in the language of the preamble or of the enacting terms from which such an intention could be inferred.

⁴ As demonstrated by a review of all of ESMA’s statements on crowdfunding:

<https://www.esma.europa.eu/databases-library/esma-library/crowdfunding> and the ESMA Prospectus Q&A.

⁵ <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:62012CC0441&from=EN>

42. Consequently, I consider that an issuer or offeror would be entitled to rely on the Prospectus Directive as amended if the Netherlands authorities were to require publication of a prospectus where the total consideration for an offer on or after 1 July 2012 was between EUR 2 500 000 and EUR 5 000 000, and that national courts would be obliged to disapply any domestic rule requiring such publication.”

3.3.4. The proposed amended wording of Article 3 in Section 2 above will finally clarify the matter regarding application across Europe of a home Member State’s Prospectus exemption thresholds in a manner that increases cross-border investment and is fit for the future growth of SME investment in Europe, while continuing to protect investors appropriately (please see section 5 below).

3.4. **Industry Analysis**

3.4.1. The Impact Assessment states:

“Respondents to the consultation stated that offers on crowdfunding platforms usually have a total consideration between EUR 50 000 and EUR 1 500 000. Research found that the average fund raising on crowdfunding platforms in the EU was about EUR 250 000. Therefore, raising the lower threshold from EUR 100 000 up to EUR 500 000 would provide a safe harbour for the development of the vast majority of crowdfunding initiatives.”

3.4.2. While the Commission’s goal of providing such a “safe harbor” for a “vast majority” of fund raises is sound, setting the amount of that “safe harbor” should be based on a more up-to-date review of industry data. Such a review demonstrates that the figures above do not take account of the actual average size of raises nor the rapidly growing nature of crowdfunding. A review of responses to the Prospectus Directive public consultation shows that the above statement is taken verbatim from a single response to the consultation and the response is not substantiated or referenced, which is not an adequate market analysis for such an important European policy decision.

3.4.3. Crowdsurfer and Ernst and Young were recently commissioned by the European Commission to produce a report on crowdfunding in Europe during 2013 and 2014.⁶ An up-to-date review of Crowdsurfer data from www.crowdsurfer.com for equity crowdfunding campaigns shows:

- In 2014 and 2015, 37 crowdfunding platforms across the European Union raised a total of €439,179,041 for 1068 successful equity crowdfunding campaigns (this analysis does not include other transferable securities such as crowdfunded bonds or debentures).
- The average successful fundraise size in 2013 was €181,058, rising by 66.7% to €300,006 in 2014 and by 50% to an average of €450,161 in 2015. This represents linear annual growth of average fundraise size. If this trend continues, the average fundraise size will be €618,971 in 2016 (already exceeding the proposed cross-border limit) and will reach €1,244,245 by the year 2020.

⁶ <https://crowdsurfer.com/blog/crowdsurfer-and-ey-release-european-crowd-finance-study/>

- The number of fundraises above €500,000 in 2015 was 157 projects raising €291,930,761 of a total amount raised of €356,077,356 from 791 successful equity crowdfunding campaigns. Campaigns over the €500,000 therefore represented 82% of the total amount raised via equity crowdfunding in 2015.
- 3.5. This average fundraising level is clearly considerably more than the €250,000 estimated in the Impact Review and this data also demonstrates that the average crowdfunding fundraise is growing rapidly and that the proposed €500,000 exemption is not high enough.
 - 3.6. Fundraises above €500,000 account for 82% of European crowdfunding investment demonstrating how important larger fundraises are to the viability of the crowdfunding industry and the support given to SMEs. Therefore, the Prospectus Directive Proposal should be made suitable for the years to come by ensuring that the exemption up to €10,000,000 does not only apply to so-called domestic offers but applies to offers across Europe.
 - 3.7. The Proposal allows SMEs to grow to a small size where they get stranded until they are large enough to bear the costs of a Prospectus. The costs of assessing the level at which countries require a prospectus is much less than preparing a prospectus, so this proposal will without doubt shrink the single market.

4. Other Challenges and conflicts arising from a “domestic offer” exemption

- 4.1. The terms “Domestic offer” and “offer [that] is made only in that Member State” are not defined in the Proposal which leads to considerable uncertainty. With freedom of movement across Europe, any attempt to artificially impose national borders has both legal and practical challenges. This would become evident if the exemption under Article 3 is not extended to offers across Europe. Our review of the responses to the Prospectus Directive consultation demonstrate that only three respondents suggested a potential “domestic offer” exemption but the responses did not provide a conclusive position or clear analysis as we provide here.
- 4.2. Questions that must be answered before a “domestic offer” exemption could be introduced include:
 - 4.2.1. Is a “domestic offer” open to EU foreign nationals who are resident, on business trips or on holiday in that Member State at the time of an offer or are they restricted from investing?
 - 4.2.2. Are nationals of a home Member State allowed to invest in domestic offers while they are in other EU countries while an offer in their home Member State is open?
 - 4.2.3. Do domestic offers include offers in a foreign language made initially in another Member State?
 - 4.2.4. If an issuer uses a platform domiciled in another member state, will the offer be “domestic” in the home member state of the issuer or the platform?
- 4.3. As a minimum, offers made under home Member State exemptions should be open to residents of all other Member States as long as the offer does not specifically state that it is targeting other Member States.

- 4.4. Crowdfunding is by its nature an online activity. It is not possible for crowdfunding platforms to limit access to offers to national borders. It would be a considerable burden to require that issuers or crowdfunding platforms apply different rules for different EU nationals. The Electronic Commerce Directive⁷ applied the country of origin principle for online information society services and given the online nature of crowdfunding the same principle should apply here. As the data for growth and crowdfunding fundraise size above demonstrates, it is important to ensure that any proposed amendment to the Prospectus regime is grounded in the reality of the internet era of investment.
- 4.5. The European crowdfunding industry believes that the proposed “domestic offer” exemption will not lead to greater harmonisation or flexibility for crowdfunding markets but rather will continue the current lack of regulatory and industry harmonisation. The United Kingdom accounts for a large percentage of European crowdfunding and this is likely to be one of the jurisdictions that becomes inward looking, but adopting the €10m level. SMEs based in smaller EU territories or where host Member States have a low threshold above which a Prospectus must be produced will be disadvantaged. There will be incentive for SMEs and crowdfunding platforms to adopt models that fall outside of the Prospective Regulation (as ESMA have observed as a risk in its Opinion on Crowdfunding) or to relocate.
- 4.6. The proposal to limit the Article 3 exemption to “domestic offers” is also contrary to the goals of the Capital Markets Union. Council conclusions on the CMU action plan has clearly stated:
- “the CMU is an important pillar of the Commission Investment Plan to promote jobs and growth in Europe ... by removing unjustified barriers to cross-border investment and diversifying the sources of funding, thus supporting notably the financing of infrastructure and SMEs.”⁸
- 4.7. Permitting domestic offers of €10m whilst restricting cross-border offers to €500,000 is likely to make issuers and crowdfunding platforms in certain countries look outside their borders for investment. This is the opposite of one of the key concepts of CMU and it is ironic that cross-border offers, which are typically more cost-intensive than domestic ones, should be restricted to such a low threshold.
- 4.8. The Proposal itself includes in its objectives as “an important step to build Capital Markets Union” such that encouragement of cross-border investment without unjustified barriers should be a goal. This therefore requires consideration of amendment of Article 3 of the Proposal as we set out.

5. Investor Protection

- 5.1. The European crowdfunding industry agrees that investor protection is key and that the proper functioning of SME investment markets is enhanced by the involvement of trusted intermediaries that carry out due diligence and ensure proper disclosure to investors. The industry is of the opinion that amending the proposed Article 3 €10,000,000 exemption to apply to offers across the EU, will not have a negative

⁷ Directive 2000/31/EC

⁸ <http://www.consilium.europa.eu/en/press/press-releases/2015/11/10-capital-markets-union/>

impact upon investor protection due to regulations and industry measures that are already in place.

5.2. ESMA state in each of their Opinion and Advice on Crowdfunding:

“Even where there is no obligation to publish a prospectus under PD, where MiFID applies there would still be disclosure requirements under MiFID in relation to financial instruments. These obligations would apply to the platform as the authorised investment firm, rather than directly to the issuer of the securities.”⁹

5.3. While there are different national regulatory regimes in place, national regulators have already reported to ESMA that platforms are regulated under MiFID or AIFMD such that there are already disclosure requirements.¹⁰ Investors may also benefit from the European Union’s Unfair Terms in Consumer Contracts Directive to protect against unfair non-negotiated consumer contracts and the application of inappropriate national courts. There may also be classic legal protections and remedies in the case of fraud, misrepresentation etc.

5.4. In addition, market forces dictate that crowdfunding platforms build trust with their users which requires attention to detailed due diligence and full disclosure. The Proposal Impact Assessment gives weight to this view and states:

“It is, however, open to what extent such investor protection concerns would actually materialise as, even without an EU or national requirement to draw up a prospectus, issuers would still need to provide appropriate information to attract and convince investors.”

5.5. Member States legal regimes and consequent investor protection levels, perceived or actual, also play a role in determining whether overseas investors from host Member States have the confidence to invest outside of their home Member State into other countries’ SMEs. Therefore, market forces can encourage the alignment of investor protection regimes. For example, the United Kingdom’s Financial Services Ombudsman accepts complaints from all nationalities, regardless of domicile, against home Member State companies while the European Commission’s consumer financial complaints network (FIN-NET)¹¹ provides a hub for cross-border complaints. FIN-NET states on its homepage:

“Out-of-court complaint schemes normally cover service providers which operate in and from the country where the scheme exists.”

5.6. The European crowdfunding industry represented by this response supports a level playing field across borders and is available for further consultation on national and European level. We applaud and encourage the continued work of ESMA in bringing together regulators from across Europe and encouraging the convergence of investor protection and crowdfunding regulation.

⁹ https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1378_opinion_on_investment-based_crowdfunding.pdf

¹⁰ https://www.esma.europa.eu/sites/default/files/library/2015/11/esma-2015-856_ann_1_esma_response_to_ec_green_paper_on_cmu_-_crowdfunding_survey.pdf

¹¹ http://ec.europa.eu/finance/fin-net/how_en.htm

5.7. The requirements under Article 15 of the Proposal for a minimum disclosure regime may also have an impact upon crowdfunding and could improve investor protection by making Prospectuses more retail investor friendly. We welcome the opportunity for further consultation on the content to ensure this is achieved. Any Prospectus approval and notification process applying to prospectuses under Article 15 for fundraises below €10 million will significantly reduce the number of issuers adopting this regime.

6. Conclusion

6.1. The European crowdfunding industry is of the firm view that the Member States should be free to set an exemption from the requirement to produce a Prospectus for offers up to €10,000,000 across Europe. The crowdfunding industry does not believe that this should be limited to “domestic offers” but asks the Commission to ensure that the exemption under the proposed Article 3 applies to offers anywhere in Europe. This will ensure that the new Prospectus regime is appropriate for offers via the internet from regulated platforms.

6.2. The crowdfunding industry does not believe that issuers should be subject to multiple prospectus exemption regimes (or Directive disapplication under Article 1(2)(h)) under the current Prospectus Directive). Allowing host Member States to require an issuer to issue a prospectus where that issuer is not required to produce a prospectus in its home Member State will introduce market inefficiencies, increase a lack of harmonisation and severely restrict the potential for cross-border investment into SMEs via crowdfunding.

6.3. The European crowdfunding industry’s aim to promote access to finance for SMEs and a Prospectus regime that facilitates cross-border investment for larger offers will ensure that growth companies can be effectively supported with their investment needs. Average investment raised through successful crowdfunding campaigns is growing rapidly and over 80% of the total investment amount raised via equity crowdfunding came from the campaigns above €500,000. The proposed €500,000 threshold in Article 1(3)(g) should therefore be increased.

6.4. The European crowdfunding industry supports investor protection and is subject to disclosure requirements under MiFID and other local legal requirements that will ensure that allowing the proposed €10,000,000 Article 3 prospectus exemption to apply to offers across the EU should not have a negative impact upon investors.

6.5. The industry welcomes the opportunity to be consulted further as part of the legislative process regarding Article 3.

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