

New Wine into Old Wine Skin: Should Hong Kong legislate on Crowdfunding? If so, How?

“And no one pours new wine into old wineskins. Otherwise, the wine will burst the skins, and both the wine and the wineskins will be ruined. No, they pour new wine into new wineskins.” – Mark 2:22, The Bible (NIV)

I. Introduction

In recent years, crowdfunding, an innovative method of raising capital, has emerged.¹ An increasing trend of small and medium enterprises (SMEs) and internet intermediary platforms engaging into crowdfunding activities is observed.² In need of effective regulation, foreign countries including the United States have enacted specific legislations governing crowdfunding.³ In light of this, it was argued that Hong Kong should follow the global practices in order to enhance its role as a global financial centre.⁴ Therefore, it is crucial for Hong Kong to explore its potential needs and possibilities in legislating on crowdfunding.

This paper, taking equity crowdfunding as an illustration, argues that the current Hong Kong regulatory framework on crowdfunding undermines the crowdfunding's mechanism and rationale, causing an interest-imbalance between its key participants. Hence, a specific legislation on it is preferred. A proposal will be proposed based on the analysis.

¹ Karina Sgar, 'Fret No More: Inapplicability of Crowdfunding Concerns in The Internet Age and The Jobs Acts Safeguards' [2012] 64(2) Administrative Law Review 474-505

² Crowdsourcing.org, 'Global Crowdsourcing' (Www.crowdsourcing.org) <<http://www.crowdsourcing.org/editorial/global-crowdfunding-market-to-reach-344b-in-2015-predicts-massolutions-2015cf-industry-report/45376>> accessed 23 January 2016

³ Deakin.edu.au, 'A Response Policy Submission On Crowd Funding' (Deakin.edu.au) <https://www.deakin.edu.au/__data/assets/pdf_file/0005/401990/Crowdfunding_Submission_IPA_July2015.pdf> accessed 26 January 2016

⁴ Ming Wong, 'A good policy on crowdfunding will enhance Hong Kong's role as global financial centre' (South China Morning Post, 28 July 2015) <<http://www.scmp.com/comment/insight-opinion/article/1844231/good-policy-crowdfunding-will-enhance-hong-kongs-role-global>> accessed 29 January 2016

In Part II, an overview of crowdfunding will be given. In Part III, equity crowdfunding activities in the current Hong Kong context and the Hong Kong current legal landscape will be outlined. In Part IV, the above major argument of this paper will be given. In Part VI, a feasible proposal will be suggested.

II. Overview of Crowdfunding

Crowdfunding is defined as “an umbrella term describing the use of small amounts of money, obtained from a large number of [people in public], to fund a [need] through an online web-based platform”.⁵ It evolves from microfinancing; raising small amounts of money, and crowdsourcing; from a large number of people.⁶ (Since SMEs often represent high risk and low return in the eye of the banks and investors, crowdfunding serves to shrink the SMEs’ finance gap.⁷ Among the various types of donation, reward, lending, and equity crowdfunding,⁸ equity crowdfunding is one of the fastest growing types.⁹ It is also known by the complexity in its regulation due to the involvement of security transaction.¹⁰

Equity crowdfunding, sometimes referred as a mini-initial public sharing (“Mini IPO”),¹¹ involving three key participants, namely the borrowers, the intermediary platform operators, and the investors. Borrowers seeking external funds via internet intermediary platform give contributors stakes into their ventures – in the forms of shares, debts, interest, or income , in exchange for their contributions.¹² Since the raised funds are usually pooled upon its collection, equity crowdfunding possesses the characteristic of being a Collective Investment Scheme (“CIS”). Similar

⁵ E.Kirby, S. Worner 'Crowdfunding: An Infant Industry Growing Fast; staff worker paper [swp3/2014] ' OICU-IOSCO, 22 January 2014) <<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD459.pdf>> accessed 3 February 2016<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD459.pdf>

⁶ CodyR Friesz, 'Crowdfunding & Investor Education Empowering Investors to Mitigate Risk & Prevent Fraud' [2015] 48(1) Suffolk University Law Review 135

⁷ *ibid* 132

⁸ Gabison, Garry A 'Equity Crowdfunding: All Regulated but Not Equal' [2015] 13(3) DePaul Business & Commercial Law Journal 361

⁹ Deakin.edu.au (n 3)

¹⁰ C. Steven Bradford, 'Crowdfunding and The Federal Securities Laws' [2012] 2012(1) Columbia Business Law Review 33

¹¹ Gibson (n8) 362

¹² GIULIANA Borello, 'The Funding Gap and The Role of Financial Return Crowdfunding: Some Evidence From European Platform' [2015] 20(1) Journal of Internet Banking and Commerce 4

to other types of investment, equity crowdfunding involve different risks, particularly, risk of default, equity dilution, and fraud.¹³

III. Equity Crowdfunding Activities in the Current Hong Kong Context and the Current Hong Kong Legal Landscape

A. Equity Crowdfunding Activities in the Current Hong Kong Context

In the context of current Hong Kong, equity crowdfunding has gained its popularity evidenced by the blooming of many internet intermediary platforms such as Colony88, Bigcolors, Crowdboron, and Fund2.Me.¹⁴ Apart from SMEs borrowers, crowdfunding has also found its application for individual investors who are lack of capital, wishing to invest in real estates. Crowdbaron, an intermediary platform, allows Individual investors to be collaborating in funding a property and received share of profits upon the sold of the property.¹⁵

Despite the hype, equity crowdfunding in Hong Kong is still falling behind. Particularly, internet intermediary platform operators face difficulties including sustaining its operation due to its underutilization by the borrowers. Fund2.Me and Colony 88, for instance, have eventually shut down after thriving to survive for two to three years.¹⁶

As equity crowdfunding is a comparatively new concept in Hong Kong,¹⁷ Simon Deane, partner for finance and insolvency at Deacons, offered an explanation of this phenomenon. The major reason he suggested was the lack of specific regulations on crowdfunding, causing uncertainty in its regulation, consequently resulting in the reluctance of both the borrowers to adopt the practice and the potential platform operators to launch their platforms in Hong Kong.¹⁸

¹³ E.Kirby, S. Worner (n5)

¹⁴ Iris Leung, '5 Hong Kong Crowdfunding Platforms You Should Know' (StartupsHK, 22 January 2014) <<http://www.startupshk.com/5-hong-kong-crowdfunding-platforms-you-should-know/>> accessed 3 February 2016

¹⁵ *ibid*

¹⁶ Weiteng Luo , 'Not in with the Crowd' (*China Daily USA*, 12 June 2015) <http://usa.chinadaily.com.cn/epaper/2015-06/12/content_20986489.htm> accessed 3 February 2016

¹⁷ *ibid*

¹⁸ Deacons, 'Hong Kong yet to offer attractive playing field for crowdfunding ventures' (*Deacons*, 5 June 2015) <<http://www.deacons.com.hk/zh-hk/news-and-insights/news/hong-kong-yet-to-offer-attractive-playing-field-for-crowdfunding-ventures.html>> accessed 10 February 2016

B. Hong Kong Legal Landscape on Crowdfunding

In the legal context, there is currently no specific legislation on equity crowdfunding. Based on its nature as a Collective Investment Scheme (“CIS”)¹⁹, the Securities and Futures Commission has issued a notice²⁰ in reminding the society that equity crowdfunding is potentially subject to the regulation of two ordinances, namely, the Securities and Futures Ordinance (“SFO”)²¹ and the Companies (Winding Up and Miscellaneous Provisions) Ordinance (“C(WUMP)O”)²² which implies crowdfunding is governed by a general security law in Hong Kong.

As SFO and C(WUMO)O mainly regulate borrowers and internet intermediary platform operators there are three major categories of regulating provisions directly in effect in regulating crowdfunding. This includes, restriction on offering shares or debentures and issuing of prospectus to the public under the C(WUMO)O,²³ prohibition on the issue of unauthorised Invitations to the Public under the SFO,²⁴ and prohibition on carrying on a “regulated activity” under the SFO.²⁵ All three categories of provisions share the same legal nature as they all prescribe statutory offences in requiring the activities participants to comply either the registration (licensing or authorization) requirements. Further they require registration-exemption when engaging the activity. Until now, it was commented that most borrowers and platform operators rely on the “professional-investor-exemption” when engaging in crowdfunding.²⁶

C. Distinct Features of the Current Hong Kong Crowdfunding Regulatory Framework

To analyse, three distinct features of the current crowdfunding regulatory

¹⁹ Part I Schedule 1 SFO,

²⁰ Securities and futures commission, 'Notice on Potential Regulations Applicable to, and Risks of, Crowd-funding Activities' (*Securities and Futures Commission*, 7 May 2014) <<http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=14PR53>> accessed 20 January 2016

²¹ (Cap 571)

²² (Cap 32)

²³ C(CWUMP)O s38, s38B, and s38D for a company incorporated in Hong Kong and s342 and 342 C for company incorporated outside Hong Kong

²⁴ s103(1) SFO

²⁵ s114, s115, Schedule 5 SFO

²⁶ Bitquant, 'Barriers to crowdfunding in Hong Kong' (Bitquant, 7 May 2015) <<https://bitquant.wordpress.com/2015/05/07/barriers-to-crowdfunding-in-hong-kong/>> accessed 7 February 2016

regime can be observed.

The first feature relates to the regulatory manner. It involves three limbs. The first limb is the classification of crowdfunding in determining its governing source of law. Secondly, the regulatory categorization of the different activities is involved in crowdfunding. The third limb is the registration-or-exemption requirement in each category of regulated activity.

The second feature relates to the regulatory function. At the core of each category of regulated activity is the stipulated registration (licensing or authorization) requirement that serves to protect the investors' interests. Registration might be seen as a process ensuring material financial information disclosure, being a safeguarding hurdle.²⁷ Provided exemption serves to mitigate the harshness created by the registration requirement.

The third aspect relates to the legal recognition of crowdfunding. There is no explicit legal recognition given to equity crowdfunding, however, the silence of the law in crowdfunding prohibition couples with the provided exemption in the general security law constituting a gray area for the current crowdfunding operation in Hong Kong.

IV. Main Argument For Legislation on Crowdfunding

The major contention for enacting specific legislation on crowdfunding is that the current Hong Kong regulatory framework on crowdfunding undermines the crowdfunding's mechanism and rationale, causing an interest-imbalance between its key participants.

A. The Current Classification of Crowdfunding When Determining Its Governing Source of Law Fails to Take into Account Its Unique Features

As crowdfunding is currently governed by the general securities law of SFO and C(WUMOO) based upon its CIS nature, such classification of crowdfunding in determining its source of law has risks to take into

²⁷ Karina Sgar, 'Fret No More: Inapplicability of Crowdfunding Concerns in The Internet Age and The Jobs Acts Safeguards' [2012] 64(2) Administrative Law Review 483

account its unique features.

Crowdfunding could hardly include a CIS as a part of its nature. A full definition of a CIS is given in Part I Schedule 1 SFO. Three distinct features of crowdfunding, however, including the limited financial capacity of the SMEs borrowers, the many-but-thin-investment slices, and the feature of double information asymmetry, having an implication in the formulation of the overall equity crowdfunding regulation were hardly accepted to be taken into account.

Firstly, regarding the feature of the limited financial capacity of the SMEs borrowers, it is argued that it has an implication in its share registration process, particularly the involved cost. HKCPA SMEs Financial Reporting Framework and Standards claims SMEs shall be strictly defined as a company not exceeding its total annual revenue and total assets of HK\$5m²⁸ that it has a relatively lower financial capacity than the traditional CIS players. Drawing distinction is crucial at this stage of development.

Secondly, regarding the many-but-thin-investment slice, it is argued that it has an implication on both the limit of the type of investors and the limit of the share offering made. Since crowdfunding was originated from the business concept of crowdsourcing and microfinance,²⁹ investment funds are solicited in thinner slices and geared towards more diverse investors³⁰ which distinguishes crowdfunding from the other CIS in the way in which each investment slice is relatively smaller while involving a relatively more types and higher number of investors.

Thirdly, regarding the feature of double information asymmetry, it has an implication on the balancing of interest between borrowers and investors. Crowdfunding differs from the traditional CIS in which it takes place via the internet intermediary platforms. Thus, the traditional information asymmetry is prone to be replaced by a double information asymmetry. In

²⁸ HKCPA, ' Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard ' (HKCPA, February 2011) < http://app1.hkicpa.org.hk/ebook/HKSA_Members_Handbook_Master/volumeII/sme-frf&sme-frs.pdf > accessed 6 February 2016

²⁹ CodyR Friesz, (n 6)

³⁰ Rechman, ' Understanding the Basics of Crowdfunding ' [2015] 84(11) CPA Journal, 30

practices, both the borrowers and investors rely on the disclosure of information from opposing parties to make accurate judgements. Borrowers require information of investor to accurately judge the quality of investors, when there may be limit of the allowed types of investors. Investors require information of borrowers to accurately judge the quality and future prospects of the borrower's project or company,³¹ which crowdfunding is distinguished in terms of the standard of information disclosure.

B. The Over Complexity of the Categorical Regulatory Framework

There is criticism that the categorically regulating manner is overly complex and stringent.

When crowdfunding is subject to the general securities law of SFO and C(WUMMO), the whole process of crowdfunding is dissected and categorically governed by the different provisions. Such regulating manner creates a wide net and is potentially overlapped. In such case, it creates multiple hurdles for both borrowers and platform operators to pass in order to conduct the whole crowdfunding process. To extent, such regulatory manner increases the level of regulatory complexity.

C. The Stringent Requirements and the Limited Facilitation of the Provided Exemption Under Regulatory Category

As mentioned, all three categories of regulated activity prescribed a registration (licensing or authorization) requirement or provided exempted conditions. Arguably, the category of prospectus issuing and the category of investment advertising involve stringent registration requirements while the provided exempted condition is in limited facilitation as it contravenes the crowdfunding mechanism.

Regarding the category of restriction on offering shares or debentures and issuing of prospectus to the public under the C(WUMMO),³² it stipulates that the issuing must comply the registration requirement and the relevant disclosure requirement.³³ Exemptions conditions are provided in the 17th

³¹ Deakin.edu.au (n 3)

³² C(WUMMO) s38, s38B, and s38D for a company incorporated in Hong Kong and s342 and 342 C for company incorporated outside Hong Kong

³³ Detailed disclosure requirement listed in Third Schedule

Schedule.³⁴

Regarding the second category of prohibition on the issuing of unauthorised invitations to the Public under the SFO,³⁵ the law stipulates an authorization requirement and provided exemption conditions. The exempted conditions include the abovementioned conditions, listed in the 17th Schedule of C(WUMP)O. An implicit exempted condition is suggested when the offers are not made to the public.³⁶

1. Stringent Registration (Authorization) Requirement

It is argued that the registration is stringent since it involves high costs and lengthy procedures. In Hong Kong, the cost for prospectus registration is HK\$1415, which seems to be little in amount.³⁷ In order for the whole crowdfunding to be processed, it requires different registrations in the different regulatory categories. There are other involved accessory costs, such as accounting fees and legal fees, resulting in an aggregation of high amount of cost.³⁸

2. Exemption Condition

As mentioned, since registration involves high amount of cost, many current intermediary platforms rely on the registration exemption to the internet intermediary platform operators.³⁹ However, the exempted condition is problematic as it undermines the crowdfunding mechanism.

The exemptions listed in the 17th of C(WUMP)O are of the following:

- (i) The offers must be made to no more than 50 persons
- (ii) The offers must be made only to professional investors
- (iii) The offers for which the total consideration payable does not exceed HK\$5 million
- (iv) The offers where the minimum consideration payable or the

³⁴ 17th Schedule

³⁵ s103(1) SFO

³⁶ Charlton, 'Hong Kong Regulation on Crowdfunding' (Charlton, June 2015) <<http://www.charltonslaw.com/legal/compliance/Hong-Kong-regulation-of-crowd-funding/index.html>> accessed 24 January 2016

³⁷ Companies registry, 'Major Fees under the Companies Ordinance' (Companies Registry, 3 March 2014) <<http://www.cr.gov.hk/en/public/fees.htm>> accessed 14 February 2016

³⁸ Karina Sigar, 'Fret No More: Inapplicability of Crowdfunding Concerns in The Internet Age and The Jobs Acts Safeguards' [2012] 64(2) Administrative Law Review 483

³⁹ Bitquant, 'Barriers to crowdfunding in Hong Kong' (Bitquant, 7 May 2015) <<https://bitquant.wordpress.com/2015/05/07/barriers-to-crowdfunding-in-hong-kong/>> accessed 7 February 2016

minimum principal to be subscribed does not exceed HK\$500,000

Regarding condition (i), it is criticized that the limitation of 50 is not referring to offers accepted but the number of offers made.⁴⁰ Since borrowers via the internet platform can potentially make unlimited offers, this exemption would be hardly applicable for borrowers to rely on.

Regarding condition (ii), professional investors include both the high net worth investors, whose portfolio of no less than HK\$8 million, and institutional investors. This exemption, although the majority in crowdfunding is mostly relying on, serves limited facilitation. First, since crowdfunding intends to source funds from the general public, this exemption largely restrains the scope of legitimate investors, undermining the original rationale of crowdfunding. As it has been mentioned previously, crowdfunding is an innovative means for SMEs borrowers to shrink the finance gap caused by the investors' reluctance in investing and the banks' reluctance in borrowing. Therefore, this exemption of limit share to professional investors does not reflect the reality.

Regarding condition (iii), although the limit of HK\$5 million can be understood as to purposely assist the needs to SMEs, it is criticized that the limit is on the number of offers made rather than the offer accepted.⁴¹ Hence, the similar loophole of condition (i) appears in which the borrowers via the internet platform can potentially make unlimited offer that makes this exemption inapplicable.

D. The Ambiguity Lies in the Category of “Regulated Activity” and Its Failure in Addressing the Legal Role of the Intermediary Platform Operator

Apart from the regulatory categories of restricting securities offering and investment advertising, the regulatory category for prohibiting internet platform operator in carrying on a “regulated activity” under the SFO⁴² is ambiguous and not promising to address its legal role played in the crowdfunding process.

⁴⁰ Charlton (n37)

⁴¹ Charlton (n37)

⁴² S114, s115, Schedule 5 SFO

In the category of prohibiting internet platform operators in carrying on a “regulated activity” under the SFO, the law prescribes a licensing requirement. The types of “regulated activity” are listed in Schedule 5 SFO. The most relevant types include, dealing in securities,⁴³ advising on securities,⁴⁴ providing automated trading services,⁴⁵ and asset management.⁴⁶ Among the different types, the type of “dealing in securities” is ambiguous. Although the term “dealing” has a wide definition, as examples, makes or offers to make an agreement, or induces or attempts to induce another person to enter into or offer to enter into an agreement,⁴⁷ it requires scrutiny of the act and the role of the platform operators itself in order to decide whether it will amount to “dealing”. In this case, since platform operators may engage into multiple acts and roles in which there is no bright line test in differentiating it, it creates difficulty in determining whether the platform operator will be deemed as “dealing in securities”, hence, a licence will be required.

Unfortunately, the current law fails to properly address the legal role of the intermediary platform operators. Apart from the abovementioned licensing requirement, the platform operators are also required to comply with the Code of Conduct issued by the Securities and Futures Commission.⁴⁸ Requirements such as the duty to ensure the suitability of the recommended investment products for particular client are prescribed in the Code of Conduct. In this case, it is questionable if the law is simply imposing duty requirements on the platform operator or if the law intends the role of platform operators to be in equivalent to the role of the brokers.

E. The imbalance of Interests Between the Key Participants in Crowdfunding

Due to the abovementioned problems, it is argued that the interests between the three key participants, borrower, platform operators, and

⁴³ Type 1, Schedule 5

⁴⁴ Type 4, Schedule 5

⁴⁵ Type 7, Schedule 5

⁴⁶ Type 9, Schedule 5

⁴⁷ Schedule 5 SFO

⁴⁸ Securities and futures commission, 'Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ' (Securities and Futures Commission, 2015) <http://en-rules.sfc.hk/net_file_store/new_rulebooks/h/k/HKSFC3527_1868_VER60.pdf> accessed 14 February 2016

investors, are imbalanced.

1. Investors' Interest

The main interest of investors, apart from the actual investment profit made, is the protection of risk. As mentioned, equity crowdfunding associates with high level of risk, such as risk of default, equity dilution, and fraud.⁴⁹ For example, Eurostat data shows that by 2010, only 46% of businesses which started five years before have survived in the market.⁵⁰ It was pointed out that moral hazard may potentially increase the level of risk exist, therefore it is critical for the regulatory to safeguard the associated risk in order to protect the interest o investors.

Having examined the current regulatory framework, it is argued that the current regulatory framework of equity crowdfunding succeeded in offering protection for investors. First, the categorically regulatory manner places multiple hurdles for the setting up of the whole crowdfunding process. Second, the stringent registration requirements couples with the limited applicability of the exempted conditions elevate the level of set hurdle. The level of difficulty for borrowers and platform operators to conduct crowdfunding activities therefore is high. Hence, the interest of investors is safeguarded.

2. Borrowers' and Platform Operators' Interest

The main interest of borrower is to seek external funds while the main interest of platform operators is to attract establish successful securities transaction in order to further its platform operation.⁵¹ Therefore both borrowers and platform operators share the common interest of being able to access to the equity crowdfunding market. As discussed, since the current regulatory framework for crowdfunding creates a high level of hurdle for borrowers and platform operators to access to the equity market. Therefore the interest of borrowers and platform operators is undermined.

F. The Rationale of Crowdfunding Is Undermined and the Preference of Enactment of Specific Legislation on Crowdfunding

⁴⁹ Eleanor Kirby, Shane Worner (n 5)

⁵⁰ Deakin.edu.au (n 3)

⁵¹ ibid

It is argued that the current regulatory framework undermines the crowdfunding mechanism and places a high hurdle for borrowers and platform operators to access to the equity crowdfunding market. Hence the rationale of crowdfunding to shrink the finance gap of borrowers is undermined. In order to maintain the current regulatory system for traditional CIS while promoting efficient equity crowdfunding system, a specific enactment of legislation on crowdfunding is preferred.

V. Suggested Proposal

Based on the comparative legal analysis, a proposal of Hong Kong equity crowdfunding legislation will be suggested. Focus will be placed on the role of the platform operators, the limit of the investment size, the limit of investors, and limit of the borrowers.

A. Proposal Objective

The proposal seeks to rectify the current imbalance of interest between the key participants on crowdfunding. In other words, it seeks to balance the dilemma between maintaining regulatory constraints for investors' protection and loosening bureaucratic barriers for crowdfunding activities.⁵²

B. Survey of Regulation on Crowdfunding from Different Jurisdictions

The chosen countries include U.S., U.K., and Italy. The former two countries are chosen due to the resemble similarity between their regulatory regime and the Hong Kong law. The latter two countries were chosen due to its early enactment of equity crowdfunding legislation.

1. U.S.

The U.S. crowdfunding legislation involves both the federal level and the state level. The Securities and Exchange Commission ("SEC") implements the federal regulations on Equity Crowdfunding via the Jumpstart Our Business Starts Acts ("JOBS").⁵³ It focuses on limiting the investing crowd.⁵⁴ It stipulates that offering of prospectus must be made through an intermediary, who may either follow the traditional

⁵² Deakin.edu.au (n 3)

⁵³ Gibson (n 8)387; SEC Rule Interpretation – Crowdfunding Proposed Rules, Securities Act Release No. 9470, Exchange Act Release No. 70741, 78 Fed Re. 66,427 (proposed Oct.23, 2013)

⁵⁴ Gibson (n 8) 387

broker-dealer registration⁵⁵ or the crowdfunding platform⁵⁶.

The investment size is limited USD 1m (EUR750K) per 12 months. Equity Crowdfunding for Borrowers are limited to local U.S. corporation. The limit of the investment size is USD 1m (EUR750K) per 12 months. The company borrowers must disclose information such as its name, legal status, organization, physical and website address.⁵⁷

The intermediary platform operators must be register as a broker or crowdfunding platform. Particularly, Due Dilligence to investors and to offering are emphasized for the platform operators to comply in tackling fraud. Due Dilligence to investors include requirement of disclosure of information 21 days prior launching the pitch⁵⁸ and requirement of ensuring information is not misleading. Due Dilligence to investors include requirement of ensuring all investors positively affirm with the risks involved and qualify to make the investment according to the regulation.⁵⁹

Investors are limited in their investment size in accordance with their net-worth and income. Investors whose net worth and income being less than USD\$40K (EUR 30K) are only allowed to invest up to USD\$2000 (EUR EUR1500). Investors whose income and net worth being less than \$100K (EUR 75K) are allowed invest up to their 5%. Investors whose net-worth and income is more than \$100K (EUR75K) can invest 10%. All individual can annually invest up to a tiered threshold.⁶⁰

2. U.K.

The UK “Aims to make investment-based crowdfunding more accessible to a wider, but restricted, audience of consumers”.⁶¹ The United Kingdom’s Financial Conduct Authority (“FCA”) affirmed that investment-based crowdfunding platforms were regulated like any

⁵⁵ 15 U.S.C. s78c(a)(23) (2015)

⁵⁶ Rules Governing the Limited Offer and Sale of Securities Without Registration under the Securities Act of 1933, 17 C.F.R. s230.506 (2015)

⁵⁷ SEC Rule Interpretation 66428

⁵⁸ SEC Rule Interpretation at 66,468

⁵⁹ SEC Rule Interpretation 66,471

⁶⁰ 15 USC s77d(a)(6)(B) / SEC Rule Interpretation, 66430

⁶¹ Gibson (n 8) 394

broker-dealer.⁶² It focuses on extending the investment crowd by extending the definition of qualified investors.⁶³ It requires prospectus must be submitted to authority to approve before its issuing.

The investment size is limited to EUR 5m per issuer within 12 months. Borrowers must comply with the existing regulations on prospectuses. Particularly, disclosure of information must include a declaration of accurate information, the borrowers' financial information, the investment objective, organizational structure, and risk factors. More specifically, borrowers must disclose any criminal conviction record of its managers⁶⁴

The intermediary platform operators must be licenced to FCA.

The definition of investor is expanded to a bigger but restricted crowd including certified or self-certified sophisticated investor, retail clients who are certified as high net worth investors, and retail clients who confirm they have received investment advice. Investors are allowed to invest up to 10 per cent of their net investible portfolio.

3. Italy

Italy is one of the earliest countries enacting legislations on crowdfunding.⁶⁵ Although it mainly regulates intermediary platform operators and investors, the legislation specifies type of legitimate borrowers.⁶⁶

The limited investment size is EUR 5m per issuer within 12 months. Borrowers are mainly restricted to innovative start-ups. Definition of innovation start-ups is defined as a company owned or controlled by a natural persons, established less than forty-eight months, subject to Italian tax or has its headquarters in Italy. Its turnovers must be lower than EUR5 million and does not distribute profits. It produces and innovative

⁶² Gibson (n 8) 392

⁶³ Financial Conduct Authority, 'The FCA's Regulatory Approach to Crowdfunding (and Similar Activities)', Consultation Paper ' (Financial Conduct Authority, October 2015) < www.fca.org.uk/static/documents/consultation-papers/lcp13-13.pdf> accessed 14 February 2016

⁶⁴ Gibson (n8) 394

⁶⁵ Commissione Nazionale per le Società e la Borsa Reg. 26 giugno 2013 n. 18592 (CONSOB Reg.)

⁶⁶ Gibson (n8) 390

products in the high technological sector.

The intermediary platform operators must be a professional platform operator. There is no licence requirement if the platform operator is a financial intermediary.

The only limit for investors is that 5% of the equity offer must be taken by professional investors before offer completion.

C. Lessons Learnt

The above all countries adopt a 12 months period for the issuing of prospectus. Both U.S and Italy restrict on the type of legitimate borrowers. U.S and U.K requires platform operators to be broker. Both U.S and U.K requires a high standard of information disclosure from the borrowers. Particularly, UK requires disclosure of previous criminal conviction record. U.S places an emphasis on the platform operators' in acting due diligence. U.K expands the scope of qualified investors within its current limit. U.S adopts a proportional approach in limiting the investors' investment based upon their investment portfolio.

D. Proposal

As mentioned, crowdfunding involve three distinct features, namely, the limited financial capacity of SMEs, the many-but-thin-slices of investment, and the the double information asymmetry. These features will be taken into account in the proposal.

Furthermore, the role of intermediary platform operators will be ascertained. The limited number of shares made to people will be removed. The scope of legitimate investor will also be expanded.

Based on the survey the proposal is suggested in the following terms:

- (i) All equity crowdfunding must be performed through a licensed platform.
- (ii) Investment limit should remain in the current 5m, based on offer accepted, in a period of 12 months. The limit of 5m can be an aggregated investment size, aggregated from multiple investing projects, per issuer.
- (iii) Borrowers must disclose all material financial information

- including previous criminal convictions of its managers.
- (iv) Platform operators must be a licenced broker from SFC and be acting in Due Dilligence.
 - (v) There is no specific requirement to the legitimate type of investors. There will be a limited-financial-information-disclosure. There will be different limits for investors based upon their size of investing portfolio

VI Conclusion

In conclusion, the current regulatory framework fails to take into account the unique features of crowdfunding. The current categorical regulatory manner is complex and creates high hurdles for borrowers and platform operators to access to the market. The stringent registration requirement and the limited facilitation of the provided exemption enhance the hurdle level. The mechanism of crowdfunding and its rationale is undermined and the interests of the key participants are imbalance.