

# EQUITY CROWDFUNDING: TAKING PROFITS FROM THE COLLABORATIVE ECONOMY

Supporting the growth of small and medium enterprises (SMEs) through financial innovation

The use of collaborative platforms to bring investors and SMEs together in small scale is a new trend gaining traction in a number of markets. Specific regulation is gradually evolving. It should improve guarantees to investors while preserving the instrument's innovative and agile features.

## BACKGROUND AND POLICY DEVELOPMENTS

- Crowdfunding is a groundbreaking financial instrument that allows small investors and entrepreneurs in need of funding to interact through online platforms. While it may serve for the intermediation of donations, rewards, peer-to-peer loans, and equity funding, investment-gearred crowdfunding (IGCF) refers to the last two categories, which offer funding opportunities for emerging and growing companies.
- The actual size of the equity crowdfunding niche is unknown, while loan-based crowdfunding operations amount to USD 6.4 billion globally according to the International Organization of Securities Commissions (IOSCO).
- In July 2016, the Brazilian *Comissão de Valores Mobiliários* (CVM) launched a public hearing proposing the creation of specific rules about equity crowdfunding only. Previous regulation allowed only privately-owned companies to raise up to BRL 2.4 million annually without registering the offering with CVM. As equity crowdfunding involves issuing public equity, the new proposal exempts all companies with revenues below R\$10 million from having to register the offering, prepare prospecti, hire intermediates, or incur in issuing costs that are disproportionate to their size.
- The main features of the proposed regulation further include eligibility criteria for issuers, annual funding limits, limitations to retail investors, disclosure requirements, equitable access to information, rules for periodic reporting about the activities of the platforms, and rules for the creation of investment syndicates.

## FURTHER READINGS

- In August 2016, CFASB will host a luncheon for its members to discuss key issues concerning the equity crowdfunding segment. The objective is to open a dialogue about the issue, from a market integrity and best practices perspective, in order to prepare a contribution for the ongoing public hearing.
- CFA Institute Issue Brief: Investment Geared Crowdfunding. Found at <https://www.cfainstitute.org/ethics/Documents/issue-brief-crowdfunding.pdf>
- CVM. Public Hearing on equity crowdfunding (in Portuguese): [http://www.cvm.gov.br/audiencias\\_publicas/ap\\_sdm/2016/sdm0616.html](http://www.cvm.gov.br/audiencias_publicas/ap_sdm/2016/sdm0616.html)
- IOSCO. Statement on Addressing Regulation of Crowdfunding: <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD521.pdf>
- IOSCO. Staff Working Paper SWP3/2014, "Crowd-funding: An Infant Industry Growing Fast". Found at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD459.pdf>

## CFA SOCIETY BRAZIL VIEWPOINT

- In March 2014, CFA Institute published an Issue Brief about debt and equity crowdfunding and its attendant emerging regulatory framework globally. CFA Society Brazil's view is aligned with the recommendations suggested in that issue brief, from which important guidelines may be of use to the now ongoing public hearing in Brazil.
- The consolidation of equity crowdfunding as a viable option for financing of SMEs in Brazil is grounded on the formulation of a modern and well-established regulatory and supervisory framework. As this new type of fund sourcing has yet to prove itself in terms of efficiency and return to investors, it is paramount to prioritize investors' protection mechanisms, while preserving its innovative features.
- The primary issues to be tackled by the new regulation are: transparency, the integrity of platforms operations, and suitable corporate governance practices. The latter must be specific and take into consideration the issue of proportionality, as imposing guidance that is too strict may imply in burdensome costs for issuers. The focus of governance direction should be the development of effective supervision and reporting mechanisms. In order to facilitate that, regulation watchdogs may share the oversight of platforms with self-regulatory organizations.
- As non-professional investors may access equity crowdfunding, special attention is advised on disclosure of information, investors' education, and investment suitability.