

August 2025 update:

This review is historical. See [What we publish](#) for more information and current views.

A review of the regulatory regime for crowdfunding and the promotion of non-readily realisable securities by other media

February 2015

Introduction

1. Crowdfunding is a way in which people, organisations and businesses, including business start-ups, can raise money through online portals (called crowdfunding platforms) to finance or re-finance their activities. Money is subscribed mainly by individuals but also by institutions. Some crowdfunding activity is unregulated, some is regulated and some is exempt from regulation.
2. We are responsible for regulating:¹
 - loan-based crowdfunding platforms,² on which people lend money to individuals or businesses in the hope of a financial return in the form of interest payments and a repayment of capital over time (this excludes some business-to-business loans)
 - investment-based crowdfunding platforms, on which people invest in unlisted shares or debt securities issued by businesses
3. In March 2014 we set out new rules for this crowdfunding activity.³ This paper looks at the implementation of the new rules so far. We will conduct a full post-implementation review of the rules in 2016.

Loan-based crowdfunding

4. On 1 April 2014, the regulation of the consumer credit market transferred to the Financial Conduct Authority (FCA), including responsibility for regulating loan-based crowdfunding platforms.

¹ We do not regulate other forms of crowdfunding, such as rewards-based or donations-based crowdfunding

² Loan-based crowdfunding is also referred to as peer-to-peer (P2P) lending or peer-to-business (P2B) lending

³ Policy statement 14/4, *The FCA's regulatory approach to crowdfunding over the internet, and the promotion of non-readily realisable securities by other media*, March 2014: <http://www.fca.org.uk/static/documents/policy-statements/ps14-04.pdf>

5. The rules we have applied to protect investors in this part of the crowdfunding market focus on ensuring that consumers interested in lending to individuals or businesses have access to clear information. This allows them to assess the risk and to understand who will ultimately borrow the money. We also applied core consumer protection requirements to firms operating in this market. For example, client money must be protected and firms must meet minimum capital standards. Finally, we require firms running these platforms to have resolution plans in place that mean, in the event of the platform collapsing, loan repayments will continue to be collected so those lending money do not lose out.
6. Firms holding an appropriate Office of Fair Trading (OFT) licence and operating loan-based crowdfunding platforms in March 2014 were able to apply for interim permission to continue conducting the activity. Having an interim permission allows these firms to remain in the market pending application for full authorisation. New firms entering the market after April 2014 must first secure full authorisation from the FCA before they may operate in this market.
7. The FCA's high-level rules took effect on 1 April 2014 for interim permission firms. More detailed rules on the conduct of such firms came into force on 1 October 2014. New firms entering the market after April 2014 were subject to all of the rules from the date they become authorised.
8. The capital requirements for firms running loan-based crowdfunding platforms are being phased in to give firms time to adjust to our regulation. Firms are only obliged to meet minimum capital requirements when they become fully authorised, and there is a transitional period (until 1 April 2017) during which the fixed minimum amount is set at a lower level than will subsequently be the case.
9. In this document, we focus on the investment aspects of loan-based crowdfunding. Where platforms arrange consumer credit, additional rules apply to protect borrowers. We have committed to a separate post-implementation review of the consumer credit rules (including those applicable to loan-based crowdfunding platforms) and will publish further information on this in due course.

Investment-based crowdfunding

10. Crowdfunding already fell within the scope of our regulation – and core FCA consumer protections already applied – where platforms allow people to invest in new or established businesses by buying shares or debt securities.
11. These instruments (which we term 'non-readily realisable securities') are not listed on regulated stockmarkets and carry significant risks. The same securities can be sold over the internet as well as through other media, so we have introduced rules that apply to their distribution whether or not that takes place on an investment-based crowdfunding platform.
12. We introduced new consumer protection rules for the sale of these securities in 2014. These rules include marketing restrictions, so firms may only make direct offer promotions to retail consumers who meet certain criteria:⁴
 - those who take regulated advice
 - those who qualify as high net worth or sophisticated investors, or

⁴ See COBS 4.7.7R to COBS 4.7.10R

- those who confirm they will invest less than 10% of their net assets in this type of security
13. Our rules also require firms to check whether customers understand the risks if they do not take regulated advice.
 14. Firms were required to begin complying with these new rules from 1 October 2014.

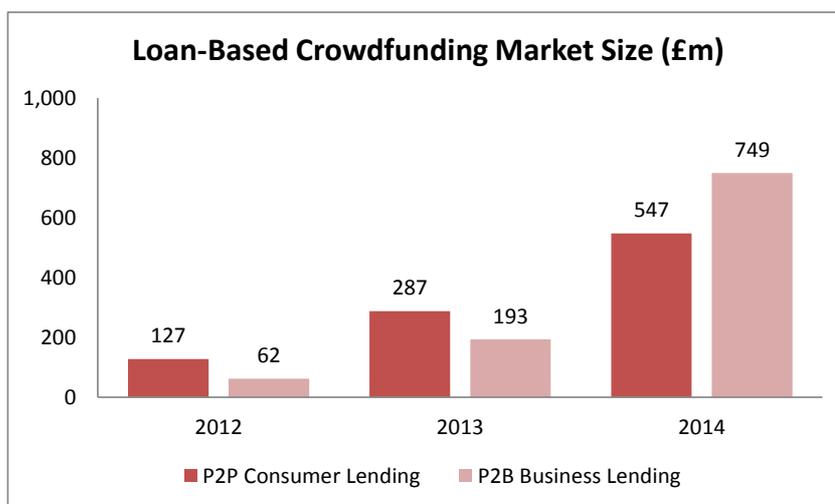
Changes to the market

15. In this section we summarise the development of the UK market in 2014.
16. Unless otherwise stated, data is derived from the Nesta and University of Cambridge 2014 report into the crowdfunding sector.⁵ Supporting information and individual firm information has also been provided by specialist websites www.p2pmoney.co.uk and www.altfi.com. We have also used information from our ongoing supervision of the market.

Market information

Loan-based crowdfunding

17. In the UK, loans made on loan-based crowdfunding platforms in 2014 are calculated by Nesta and the University of Cambridge (Nesta 2014) to be almost £1.3bn. The sector was almost three times larger in 2014 than in 2013 (when it raised around £480m).



18. In 2014, for the first time, business loans (£749m) accounted for a greater proportion of the market than loans raised on consumer-lending platforms (£547m). Nesta and the University of Cambridge (Nesta 2014) also report that around 2% to 3% (approximately £11m to £16m) of borrowers using consumer-lending platforms are borrowing for their businesses.
19. According to data supplied by www.altfi.com, before we began regulating the sector, it took an average of 28 months for new platforms to reach their first £25m in sales. In 2014, it took an average of 17 months for new platforms to achieve the same figure.

⁵ *Understanding Alternative Finance, the UK Alternative Finance Industry Report, 2014* (Zhang, Z., Collins, L., Baeck, P., 2014), <http://www.nesta.org.uk/sites/default/files/understanding-alternative-finance-2014.pdf>

Personal loans

20. The average loan amount borrowed by personal consumers using these platforms in 2014 was £5,471. Over 100,000 loans were arranged on consumer-lending platforms.
21. Of those borrowers surveyed by Nesta and the University of Cambridge (Nesta 2014), more than half reported that they had been offered funding elsewhere and only 15% regarded the inability to get funding elsewhere as a very important factor in their decision to use the platform.
22. The most commonly cited reasons for borrowing money are for buying a vehicle (46%), making home improvements (26%) and consolidating debt (25%).
23. The average rejection rate for borrowers across these platforms is as high as 90%, and the majority of borrowers have strong credit profiles. The average default rate for personal loans is less than 1%.
24. Investors tend to be male and have an average age of 49. On average, they have a portfolio of over £5,600. The wealth profile of investors is mixed, with 37% of investors having an annual income of less than £25,000 and 25% earning more than £50,000.
25. The majority of investors (64%) reported that they use at least some money from their savings budget and 57% reported that they use some money from their investment budget.⁶

Business loans

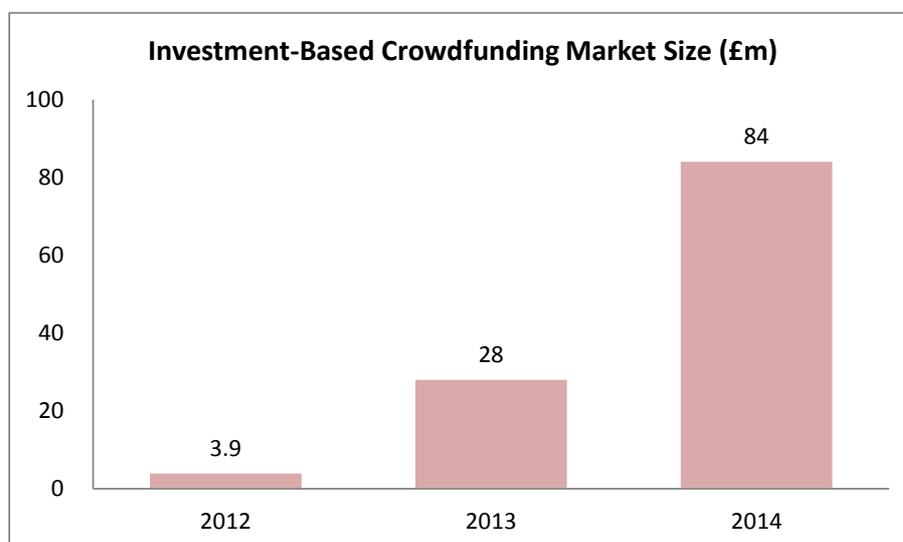
26. The average amount borrowed for business purposes in 2014 was £73,222. A newly emerging trend identified in the Nesta and University of Cambridge report (Nesta 2014) is secured lending for real estate mortgages and developments, with some platforms specialising in this type of business. The average business loan size here is £662,425 with an average term of ten months.
27. 33% of borrowers surveyed by Nesta and the University of Cambridge (Nesta 2014) reported that it was unlikely or very unlikely that they would have been able to secure funding with other sources. 44%, on the other hand, reported that it was likely or highly likely that they would have been able to find funding elsewhere if they had not used loan-based crowdfunding platforms.
28. Default rates for business loans show more variation from platform to platform. With some platforms, the default rates are less than 1%. With other platforms, some of which have now closed to new business, default rates were significantly higher.⁷
29. Investors in business loans are primarily male and aged 55 or over. They also tend to be wealthy, with one-third having an annual income in excess of £50,000. Investors have an average portfolio of over £8,000, spread over a median of 52 business loans.
30. 54% of those surveyed report that they use some money from their investment budget, and 45% from their savings budget.

⁶ Note that the survey allowed for multiple responses to this question

⁷ For more detail, see this page: <http://www.p2pmoney.co.uk/companies.htm>

Investment-based crowdfunding

31. According to the Nesta and University of Cambridge report (Nesta 2014), the amount raised on investment-based crowdfunding platforms in 2014 the UK is expected to be £84m. This is three times the amount raised in 2013 (£28m).



Equities

32. Equity-based crowdfunding grew by 201% in 2014. The average amount raised through equity-based crowdfunding is £199,095. Almost 95% of the funded deals were eligible for the Enterprise Investment Scheme (EIS) or Seed EIS (SEIS) schemes.
33. The average age of investors is 40 and the average portfolio size is £5,414 (with one-third having invested less than £1,000).
34. 38% of investors surveyed by Nesta and the University of Cambridge (Nesta 2014) were classified as professional or high net worth individuals. 62% described themselves as retail investors with no previous investment experience of early stage or venture capital investment. The average portfolio size for high net worth and sophisticated investors is over £8,000. For other retail investors it is less than £4,000.
35. As with loan-based crowdfunding, the primary reason for investment is the hope of financial return. Few investors came to the model to invest in a family member or friend or to support a local business.
36. 68% of those surveyed report that they use money, at least partly, from their investment budget, and 44% from their savings budget.

Debt securities

37. The Nesta and the University of Cambridge report (Nesta 2014) focused on the use of debt security crowdfunding platforms that finance renewable energy projects. This part of the market grew by 63% in 2014.
38. The average amount raised is £730,000. The average investment in debt securities on these platforms is £1,243.
39. The opportunity to make a positive social impact was an important factor for 86% of investors in debt securities issued in support of renewable energy projects.

40. 62% of those surveyed report that they use money, at least partly, from their investment budget, and 55% from their savings budget.

Authorising new firms

Loan-based crowdfunding

41. 50 firms operating loan-based crowdfunding platforms in March 2014 applied to us for interim permission.
42. Since then we have authorised one firm, which entered the market after April 2014, to operate a loan-based crowdfunding platform, and we are presently reviewing a further eight applications. With three interim permission firms leaving the market, this means that the number of firms operating in this sector, or seeking to enter it, has increased from 50 in April 2014 to 56 by the end of 2014.

Investment-based crowdfunding

43. By April 2014 we had authorised ten firms to conduct regulated activity in relation to investment-based crowdfunding. At present, there are 14 firms authorised to conduct regulated activity in relation to investment-based crowdfunding, and we are currently considering the applications of another ten firms. We have identified another 11 firms that act as appointed representatives and conduct regulated activity in relation to investment-based crowdfunding. This brings the total number of firms in this part of the market, or seeking to enter it, to 35.

The authorisations process

44. We have been asked what our expectations are when we receive applications for the authorisation of crowdfunding businesses. With reference to our threshold conditions, we encourage firms to take the following steps.
- Submit a suitable and detailed regulatory business plan setting out the planned activities (and related risks), budget and resources (human, systems and capital) – i.e. not a funding pitch.
 - Have adequate non-financial resources (i.e. the management board has adequate knowledge and experience of financial regulation).
 - Have adequate financial resources when submitting their application (i.e. not looking at future fundraising to reach the requirement).
 - Have a website that is either up-and-running or at a suitably advanced stage (including a test site or app, or screen shots of a planned website or app, that would demonstrate the user interface and functionality available to users) to demonstrate how it will operate should the firm be authorised.
 - Understand the requirements for FCA authorisation and the permission profile for which they wish to apply, then submit a complete application (including an outline of which regulated activities the firm plans to conduct).
45. Particularly for investment-based crowdfunding applications for authorisation, in 2014 we have seen that, where applicants submit high quality applications (making sure to include all of the above), we have been able to make more timely decisions. In the past we have

encountered problems where firms have submitted almost blank application forms or applied for regulated activities that are unnecessary for their business model.

Project Innovate and the Innovation Hub

46. We have set up an Innovation Hub offering support to innovator businesses that are looking to introduce ground-breaking or significantly different financial products or services to the market, including when they need assistance with an application for authorisation or a variation of permission.⁸
47. To help firms running loan-based crowdfunding platforms we have produced a quick guide to the areas of our Handbook that are relevant to them.⁹

FCA supervision of the market

48. Supervising investment-based crowdfunding platforms in 2014 included engaging with firms' senior management, monitoring their websites and reviewing monthly management information (MI). This approach has resulted in a number of regulatory interventions that have been mainly to ensure the proper protection of consumers. For example, this means ensuring that only appropriate types of customers were allowed to invest, and that financial promotions are clear, fair and not misleading, with regards to both the nature and performance of the assets invested in and the exit opportunities for investors. In addition, there have been a small number of reactive prudential events where firms were not meeting the expected capital requirements.
49. A similar approach was also taken with loan-based crowdfunding platforms. However, additional forward-looking supervisory visits were undertaken to assess the governance, management and controls of five market participants to understand the risk that the sector poses to our statutory objectives. Overall, we were encouraged by what we found during our visits, including a good understanding of credit risk and robust anti-money laundering (AML) and Know Your Customer (KYC) checks. The firms visited all placed an emphasis on ensuring that consumers interested in lending to individuals or businesses had access to clear information, which would allow them to assess the risk and understand who will ultimately borrow the money.
50. We are particularly looking to see that platforms are disclosing all relevant information to enable potential investors to make informed decisions on whether or not to invest. This information should not be misleading. So, for instance, claims that shares offered on a platform are the same as shares held by venture capitalists should be true: we would be concerned if these claims were not being verified and firms were, therefore, promoting the shares with misleading information. This becomes significant if venture capitalists are able to profit from successful investment opportunities but crowdfunding investors find, when an investment succeeds, that equity dilution means they do not share in the profits to the same extent.
51. For people to share knowledge, platforms often allow investors to comment on investment opportunities. Some market intelligence suggests that negative comments are being deleted from these forums on some sites, which may lead to situations where relevant risks are overlooked.

⁸ Please see our website for more information: <http://www.fca.org.uk/firms/firm-types/project-innovate>

⁹ The guide is available here: <https://innovate.fca.org.uk/innovation-hub/summary-rules-loan-based-crowdfunding-platforms>

52. We are also investigating a number of firms that conduct regulated investment business without being appropriately authorised to carry on regulated activities in the UK.

Website and financial promotion reviews

53. Over the course of 2014 we proactively monitored crowdfunding financial promotions and took action where firms do not meet our standards. In addition to this business-as-usual supervision, we conducted a specific review of crowdfunding websites last year. Between April and October 2014, 25 websites (including both loan-based and investment-based platforms) were reviewed against the financial promotions rules and the requirement to be fair, clear and not misleading.
54. With regard to the investment-based platforms we considered, we identified problems with most of the websites in the review. The common issues identified were:¹⁰
- A lack of balance, where many benefits are emphasised without a prominent indication of risks.
 - Insufficient, omitted or the cherry-picking of information, leading to a potentially misleading or unrealistically optimistic impression of the investment.
 - The downplaying of important information. For example, risk warnings being diminished by claims that no capital had been lost or the relevant risk warnings being less prominent than performance information.
55. This is of particular concern for us given that 62% of equity crowdfunding investors surveyed by Nesta and the University of Cambridge (Nesta 2014) described themselves as retail investors with no previous investment experience of early stage or venture capital investment. Firms need to provide investors with appropriate information, in a comprehensive form, so that they are reasonably able to understand the nature and risks of the investment and, consequently, to make investment decisions on an informed basis.
56. Our review of loan-based crowdfunding identified similar issues but also:¹¹
- promotions comparing crowdfunding investing to savings accounts and banking and, in doing so, creating the impression that the lender's capital was secure
 - insufficient information in promotions about the taxation of investments
 - from the perspective of the borrower, the omission or lack of prominence of the Representative Annual Percentage Rate (APR), and
 - promotions having a lack of balance by giving prominence to the benefits of borrowing without a prominent indication of risk in relation to the borrower's financial circumstances
57. Of the investors surveyed by Nesta and the University of Cambridge (Nesta 2014), a majority of those investing in personal loans said they use at least some money that would otherwise be saved. We are, therefore, particularly concerned about promotions in this sector that encourage investors to see loan-based crowdfunding as being equivalent

¹⁰ Requirements in COBS 4.5.2R call on firms to meet these standards

¹¹ See COBS 14.3.2R, COBS 14.3.7A G, CONC 3 and CONC 4.3

to holding money on deposit. Investors should understand that there are greater risks involved and they may lose some or all of their money.

58. Following our review, we contacted all the relevant firms and told them to make the necessary changes to their websites to ensure they were fair, clear and not misleading and fully compliant with our rules. All the firms we wrote to were keen to comply and most made the required changes with immediate effect.
59. We will continue to monitor financial promotions in this sector and to take action where firms do not meet our standards.

Mini-bonds

60. In essence, a mini-bond is a type of debt security, typically issued by small businesses. Such securities run for around three to five years, in general, and offer an interest rate of between 6% and 8% a year. We have seen an increase in the number of small companies issuing mini-bonds on crowdfunding platforms to raise capital for their business. Such businesses may have found it difficult to secure a loan from a bank or could be start-up companies looking for funding.
61. Mini-bonds are also becoming increasingly popular with investors, attracted by the interest rates on offer. However, it is important for prospective investors to understand the risks. Mini-bonds are illiquid and can be high risk, as the failure rate of small businesses is high. There is no protection from the Financial Services Compensation Scheme (FSCS) if the issuer fails. Firms promoting these securities to the public must make the risks clear to prospective investors.
62. We have reviewed the financial promotions of a number of mini-bonds (both those on crowdfunding platforms and in direct marketing). We have the following concerns:
 - Firms are failing to make clear that mini-bonds are investments that place investors' capital at risk, and are not deposit-based or capital-protected products. While the returns on mini-bonds can appear competitive in the current low interest environment, it is misleading to compare their interest rates with those obtainable from savings accounts where investors' capital is not at risk.
 - It is important that the promotion is balanced; in particular, the risks to capital and the lack of FSCS cover should be highlighted.
 - Comparisons are sometimes made to retail bonds (such as corporate bonds listed on the stock market) but there are important differences. For example, mini-bonds are generally not traded, so investors' money is effectively locked in until maturity as the mini-bond cannot be sold on before the end of its term. This should be made clear to prospective investors.
 - Where a firm is asked to approve a financial promotion on behalf of an unauthorised firm, the firm must satisfy itself that the financial promotion is fair, clear and not misleading. It must not approve the promotion if it does not comply with our rules.

Social media

63. In August 2014 we published a consultation on our supervisory approach to financial promotions in social media.¹² In light of the internet-based nature of crowdfunding platforms, that consultation is likely to be of particular interest to firms running such platforms.
64. The consultation outlines our approach to supervising consumer communications made via digital media. We noted that our rules are intended to be media-neutral to ensure that consumers are presented with certain minimum information, in a fair and balanced way, at the outset of firms' interaction with them. Our rules include sector-specific requirements, but in each case there is an overarching principle that any communication should be fair, clear and not misleading.
65. One issue that we know is of particular concern to the crowdfunding sector is the extent to which the use of social media amounts to making a 'financial promotion' within the scope of the Financial Services and Markets Act 2000 and, therefore, subject to our financial promotion rules. What is or is not a 'financial promotion' is a matter of interpretation of the legislation, not of our rules. One key aspect to consider is whether the communication is made 'in the course of business'. We have set out our view of what 'in the course of business' means in Chapter 8.5 of the Perimeter Guidance Manual (PERG). In particular, PERG 8.5.3G considers the position of individuals promoting a small private company in its pre-formation stage, or when seeking to raise additional capital for such a company, which is a common situation in crowdfunding.
66. We expect to publish the final guidance on social media and consumer communications, following this consultation, in the first quarter of 2015.

Co-operative and community benefit societies

67. In October 2014 we consulted on guidance on the FCA's registration function under the Co-operative and Community Benefit Societies Act 2014.¹³ This may be relevant to firms running crowdfunding platforms.
68. The promotion of withdrawable shares issued by societies registered by the FCA under the Co-operative and Community Benefit Societies Act 2014 and arranging deals in these shares are not regulated activities under the Financial Services and Markets Act. So a crowdfunding platform which promotes these shares does not need to be authorised to conduct that part of its business.
69. Societies that use crowdfunding platforms to market their withdrawable shares are required to continuously meet the condition for registration under the Co-operative and Community Benefit Societies Act 2014 that was met when the issuing society was registered (i.e. that it is either a co-operative or its business is conducted for the benefit of the community). This includes the requirement at s.2(3) of the Co-operative and Community Benefit Societies Act 2014 that a society cannot be registered as a co-operative society if it 'carries on, or intends to carry on, business with the object of making profits mainly for the payment of interest, dividends or bonuses on money

¹² Guidance consultation 14/6, *Social media and consumer communications*, August 2014:

<http://www.fca.org.uk/static/documents/guidance-consultations/gc14-06.pdf>

¹³ Guidance consultation CP14/22, *Guidance on the FCA's registration function under the Co-operative and Community Benefit Societies Act 2014*, October 2014: <http://www.fca.org.uk/static/documents/consultation-papers/cp1422.pdf>

invested or deposited with, or lent to, the society or any other person.’ As explained in CP 14/22, we expect that a society’s purpose is not to make a return to investors.¹⁴

70. We have been told that some platforms encourage societies to offer high interest rates on their shares in order to improve the prospects for a successful launch. The competitive effect of interest rates which are published by the platform for comparison purposes provides an added incentive to offer high returns; and for the platform, its remuneration model, where this is commission-based, may be an influential factor.
71. The holders of shares in a society are known as its ‘members’. In the case of a community benefit society, the interests of the members must be subordinated to the interests of ‘the community’ served by the society and so we would expect the society’s rules not to allow either profits or the society’s assets to be distributed to the members.
72. In the case of a co-operative, we would expect that persons who acquire shares will do so because they intend to participate in the business of the society by trading with it, or otherwise using its facilities. The exception to this principle would be where a society’s rules make specific provision for a class of ‘non-user investor members’, which may represent up to 25% of the society’s total share capital.
73. We are not suggesting that societies should not use platforms to promote their share offers. But, where they do, they must take steps to ensure that they continue to comply with the requirements of the Co-operative and Community Benefit Societies Act 2014.
74. Finally, we would encourage platforms to consider whether there are alternative models for remuneration and comparison that are more suited to the particular characteristics of shares in businesses registered as co-operative or community benefit societies.

International action

75. In early 2014, a staff working paper was published by the International Organization of Securities Commissions (IOSCO), which discusses how the crowdfunding sector is growing globally.¹⁵ The report notes that the global market for investment-based and loan-based crowdfunding has doubled year-on-year in recent years to an estimated US\$6.4bn in 2013, driven by annual growth of 90% in peer-to-peer lending. The global equity crowdfunding market is more modest in size and has grown at a slower pace.
76. IOSCO’s report also summarises how the national regulators in different jurisdictions choose to regulate crowdfunding. Given its relative infancy, crowdfunding is not present in every country. Of those jurisdictions where the activity takes place and is regulated, we consider that the UK regulatory regime provides a favourable framework. Contrary to some suggestions, our approach to regulation has not ended the UK market or even slowed its growth, as the above data demonstrates. We consider that our regulation provides a proportionate set of rules, under which the market can develop and consumers are appropriately protected.
77. We are involved in initiatives by the European Banking Authority (EBA) and European Securities and Markets Authority (ESMA) that are considering the regulation of

¹⁴ See paragraph 6.35 of CP14/22

¹⁵ *Crowdfunding: an infant industry growing fast*, IOSCO, February 2014:
<http://www.iosco.org/news/pdf/IOSCONEWS319.pdf>

crowdfunding in the EU.¹⁶ The European Commission has set up a stakeholder forum on the topic and is also looking at the issue. We will continue to engage in all international workstreams that may have an impact on the regulation of crowdfunding in the UK.

Conclusion

78. In the months since we introduced our rules, we have seen the crowdfunding market continue to grow rapidly. We recognise that it is still early but, at present, we see no need to change our regulatory approach to crowdfunding, either to strengthen consumer protections or to relax the requirements that apply to firms. We plan to carry out a full post-implementation review of the crowdfunding market and regulatory framework in 2016 to identify whether changes are required at that stage.
79. We will continue to monitor the market in addition to the formal review process and will take any appropriate action. If, for example, the risks to which investors on loan-based crowdfunding platforms are exposed increase to mirror those seen in investment-based crowdfunding platforms, we will consider applying a similar approach as for non-readily realisable securities.
80. It may be that there are changes to the regulatory framework for crowdfunding as a result of future EU work.

If you have any comments on this document you can send them in writing to:

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¹⁶ ESMA has published an analysis of how typical investment-based crowdfunding business models map across to existing EU legislation. The report is available here: <http://www.esma.europa.eu/content/Opinion-Investment-based-crowdfunding>