

Crowdfunding in the U.S. and Abroad: What to Expect When You're Expecting

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The Jumpstart Our Business Startups Act (JOBS Act), signed into law earlier this year, is part of a bipartisan push to broaden funding opportunities for small business owners in the post-recession economy. Recognizing the limited options available to entrepreneurs short on existing assets and looking to raise early-stage capital, the JOBS Act includes a provision that would allow small business owners to offer a limited amount of equity (stock) to private citizens through online platforms.¹ This concept, popularly referred to as “investment crowdfunding,” is based on the growing practice of benevolent giving or microlending to specific individuals or causes through online platforms like Kickstarter or KIVA.²

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1. See Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306 (2012).

2. See Dave Milliken, *Investment Crowdfunding Analysis: Crowdfunding Soars While a Pioneer Shutters*, CROWDSOURCING.ORG (Feb. 20, 2012), <http://www.crowdsourcing.org/document/investment-crowdfunding-analysis-crowdfunding-soars-while-a-pioneer-shutters/11525>; see also Brigitte Bradford, *Week in Review: The True Power of Crowdfunding*, 46 CORNELL INT’L L.J. 427 (2013)

While these charitable forms of crowdfunding are already legal in the United States, until the passage of the JOBS Act, investment (equity) crowdfunding was next to impossible because of restrictive securities laws established by the Securities Act of 1933.³ In the United States, there is a great deal of uncertainty as to what form legalized equity crowdfunding will take as the new law comes into effect over the next year, and what sort of effects investment crowdfunding might have on the business and finance worlds.⁴ Fortunately, the equity crowdfunding experience abroad (in many other countries it is either legal and regulated, or being tolerated until further notice) serves as an instructive example of the kinds of legal and extralegal tools that can be used to effectively regulate the investment crowdfunding world, and the ways in which that world might grow and change.⁵ As a relatively young phenomenon, it is unclear exactly who will end up using crowdfunding as a means of offering equity, but experiences in places like the U.K. and France have begun to reveal what equity crowdfunding might look like in the United States as the practice matures.⁶

This Note examines the emergence of a global equity crowdfunding landscape and argues that depending on what regulatory limits are put in place, the inherent limits of crowdfunding and the digital medium might ultimately be the determining factors in the scale of growth of equity crowdfunding. Part I explores the global origins of crowdfunding and discusses the challenges associated with developing an appropriate regulatory regime. Part II takes a comparative look at the ways in which the equity crowdfunding arena is developing abroad and the ways in which other nations are responding to the growth of the phenomenon. Part III looks prospectively at the impact of the JOBS Act on crowdfunding in the United States and the ways in which the Securities Exchange Commission (SEC) rules might or might not address some of the more salient issues that have been affecting the crowdfunding movement around the world. Finally, this Note argues that the movement towards equity crowdfunding might have its limits independent of any specific regulatory scheme and may not indeed solve the broader problems that it (in theory) sets out to address.

I. Origins of Crowdfunding and Governing Challenges

A. Origins, The Microfinance Movement

The broader crowdfunding movement has its roots in the microfinance and microcredit trend pioneered by Nobel Prize winner Muhammad Yunus.⁷ The microfinance movement aims to attack poverty by giving indi-

KIVA NEWS (June 8, 2012), <http://kivanews.blogspot.com/2012/06/week-in-review-true-power-of.html>.

3. 15 U.S.C. § 77a (2012); see *infra* Part I.C.

4. See *infra* Part III.A.

5. See *infra* Part II.

6. See *infra* Part II.A–C.

7. Anand Giriharadas & Keith Bradsher, *Microloan Pioneer and His Bank Win Nobel Peace Prize*, N.Y. TIMES (Oct. 13, 2006), http://www.nytimes.com/2006/10/13/business/14nobelcnd.html?_r=0.

viduals who cannot afford the transaction costs of traditional bank-based financing access to cash.⁸ Microfinance has carved out a role in promoting savings among impoverished communities, developing credit records for individuals who live in remote regions, and helping to hedge against income volatility in the developing world (an important feature for microloan recipients who are dependent on seasonal agricultural income).⁹ Beyond that, arguments have been advanced that microlending can actually help broad-scale economic development in developing nations by injecting cash into isolated markets and creating new demand for traditional bank loans and investment.¹⁰ Part of the way that microfinance can help open up broader credit markets is by establishing an aggregation of individual cases in which receiving parties demonstrate creditworthiness to their sponsors, donors, loaners, or financiers.¹¹

Of course, the microcredit boom is not without its detractors, and some of the criticisms that have been directed at microcredit specifically can be generalized to crowdfunding in all of its purposes.¹² The most prevalent criticism is that without a continuing support structure microcredit enterprises typically fail.¹³ Frequent microcredit critic Milford Bateman points out that studies of microcredit programs in “the Indian state of Tamil Nadu found that on average only 1 per cent [sic] of microenterprises were still in operation three years after their establishment.”¹⁴ Still, microfinance seems to have accomplished at least some of its goals in most of the geographic locations and economic arenas that it has reached.¹⁵

A vital feature of microfinance is that it allows the individuals donating or loaning money to develop a more intimate relationship with the beneficiary of their contribution.¹⁶ While the goal of microfinance is primarily to provide resources to the underprivileged, the personal level of connection between individual donors or investors and their loan or dona-

8. See *id.*

9. See Michael S. Barr, *Microfinance and Financial Development*, 26 MICH. J. INT’L L. 271, 280 (2004).

10. *Id.* at 286.

11. See *id.* (citing Thierry Tresselt, *Dual Financial Systems and Inequalities in Economic Development*, 8 J. ECON. GROWTH 223, 225 (2003)).

12. See, e.g., Milford Bateman, *The Illusion of Poverty Reduction*, RED PEPPER (Sept. 2010), <http://www.redpepper.org.uk/the-illusion-of-poverty-reduction/>.

13. *Id.*

14. *Id.*

15. See Craig McIntosh, Gonzalo Villaran, & Bruce Wydick, *Microfinance and Home Improvement: Using Retrospective Panel Data to Measure Program Effects on Fundamental Events*, 39 WORLD DEV. 922 (2011) (pointing out that in microfinance programs across three different continents, the probability of major housing improvement increases from 0.038 to 0.070 in the years subsequent to a first microfinance loan). *But see* Jon Westover, *The Record of Microfinance: The Effectiveness/Ineffectiveness of Microfinance as a Means of Alleviating Poverty*, ELECTRONIC J. SOC. (2008), www.sociology.org/content/2008/_westover_finance.pdf (discussing the scattered and overly case-specific empirical evidence of the successes of microcredit).

16. See, e.g., Steven Kurutz, *An International Financier, on a Teensy Scale*, N.Y. TIMES (Nov. 8, 2012), http://www.nytimes.com/2012/11/09/giving/a-writer-bob-harris-offers-a-personal-view-of-microfinance.html?_r=0.

tion recipients made possible by the Internet is an important draw.¹⁷ This coheres with the more general notion that individualized and direct solutions to finance problems are inherently more efficient than working through intermediaries with seemingly opaque funding pathways.¹⁸

B. Beyond Charitable Giving

Since the 2007 financial crisis, the idea of alternative access to capital (avoiding banks or other financial institutions) has gained traction beyond the world of charitable giving.¹⁹ For example, the art world, where financing has always proven challenging for emerging talents, has rapidly absorbed the idea of crowd patronage.²⁰ Sites like Threadless and CatWalkGenius leverage interest in personal connection to the arts by allowing individuals to pick their favorite artists and fund specific projects.²¹ In return, artists typically reward their benefactors with free merchandise or tickets to shows; this is not typically considered a return on investment by the SEC and is therefore not under its purview.²² Recipients of benevolent crowd funds, however, have to be careful that any gifts or prizes given out to their patrons do not include characteristics of interest or increasing return which might run afoul of the current regulation regime.²³

That is not to say that there are no financial benefits at all for benevolent crowdfunders; some patrons are beginning to use their crowdfunding contributions to qualify for tax deductions by setting up fiscal sponsorship arrangements.²⁴ Depending on the size of the contribution, this can mean significant savings for benefactors.²⁵ This type of arrangement typically involves the establishment of a separate 501(c)(3) entity to oversee the fund transfers, meaning that it is likely limited to individuals with the resources and knowhow to incorporate an organization solely for taxation purposes.²⁶

17. See KIVA, <http://www.kiva.org/lend> (last visited Feb. 19, 2013). KIVA's website and lending program is a good example of the tailored donation experience—individual recipients have profiles that allow donors to choose the end destination of their loans. *Id.* Each profile comes with pictures, a detailed narrative explaining what the loan will be used to accomplish, and a general profile of the individual receiving the funds. *Id.*

18. See Barr *supra* note 9, at 291 (noting that the formal lending practices in developing countries often favor entrenched social elites and operate to benefit the politically connected, and suggesting that direct lending through microfinance can help circumvent these issues).

19. See *infra* Part II.

20. Kristina Dell, *Crowdfunding*, TIME (Sept. 4, 2008), <http://www.time.com/time/magazine/article/0,9171,1838768,00.html>.

21. *Id.*

22. See Daniel M. Satorius & Stu Pollard, *Crowd Funding: What Independent Producers Should Know About the Legal Pitfalls*, 28 ENT. & SPORTS LAW. Summer 2010, at 15, 17.

23. See *id.* (describing the ways that non-equity crowdfunding platforms can avoid claims that their activities involve the sale of securities).

24. *Id.*

25. See *id.*

26. See *id.*

Where the line is drawn between what constitutes an investment and what is a charitable contribution seems to be pretty clear. The SEC prohibits any unregistered company from selling stock or other securities unless it is specifically exempt from the normal registration process.²⁷ Because of how arduous and expensive the normal registration requirements can be, very few small businesses opt to offer securities to the public except through certain specific registration exemptions laid out under Regulation D and, in some situations, Regulation A of the United States Securities Act of 1933 (the '33 Act).²⁸ The cost of actually registering (not utilizing these exemptions) would be prohibitively high for any small business.²⁹

C. The Existing Regulatory Regime for Exempt Public Offerings

Regulation D (typically referred to as “Reg D”) contains among the most frequently utilized exemptions to SEC registration requirements.³⁰ Under Reg D, companies have three different routes for exemption from SEC registration, each promulgated under either § 3(b) (Rules 504 and 505), or § 4(2) (Rule 506) of the '33 Act.³¹ Each of the rules has different limitations, and would be difficult to utilize in exempting a crowdfunding operation from SEC registration requirements for a set of reasons—some uniform, and some unique to each rule.³² Even if equity crowdfunding is not possible under Reg D,³³ in thinking about the goals and requirements of a crowdfunding regulation regime, it is useful to look at Reg D along with some other registration exemptions as examples of the difficult balance between an interest in greater disclosure (for purposes of investor protection) and an interest in lessening the burden on small businesses looking to raise capital (by conversely cutting away at disclosure requirements).³⁴

The exemption laid out in Rule 504 covers any private company (except those considered special purpose acquisition companies) that limits offers and sales of securities to \$1 million or less in any twelve-month period.³⁵ Rule 504 places relatively lax limits on the nature of investors or number of investors compared with the two subsequent exemption rules

27. Securities Act of 1933 § 4, 15 U.S.C. § 77d (2012) (noting, for example, Regulation D offerings, which are exempt from full registration).

28. See William K. Sjostrom, Jr., *Going Public Through an Internet Direct Public Offering: A Sensible Alternative for Small Companies?*, 53 FLA. L. REV. 529, 540-41 (2001).

29. See *id.* at 575-76 (demonstrating that the various fees associated with an underwritten public offering can amount to between \$300,000 and \$500,000).

30. 17 C.F.R. §§ 230.500-08 (2012).

31. *Id.* §§ 230.504-06.

32. See *infra* Part I.C.

33. Cf. C. Steven Bradford, *Crowdfunding and the Federal Securities Laws*, 2012 COLUM. BUS. L. REV. 1, 24 (2012) (describing ProFounder's early attempts to offer public rounds under Rule 504 and its subsequent failure); William Carleton, *Equity Crowdfunding Dissected*, COUNSELOR @ LAW (Oct. 23, 2012), <http://www.wac6.com/wac6/2012/10/equity-crowdfunding-dissected.html> (describing Bolstr's efforts to utilize Rule 504 by navigating state-by-state registration exemption rules).

34. See *infra* Part I.C.

35. 17 C.F.R. § 230.504 (excluding from applicability so called “special purpose acquisition companies” or “blank check” companies, which include any “company that

found in Reg D.³⁶ The rule also does not limit investors from reselling their securities after purchase.³⁷ However, Rule 504 offerings typically must be undertaken in a state (or number of states) that independently requires publicly filed registration statements and certain disclosure to investors.³⁸ This independent state registration requirement could be equally as prohibitive as federal registration depending on the size and resources of the startup.³⁹ Rule 504 offerings are also typically subject to the same general solicitation prohibition that holds true for all Reg D-exempt offerings.⁴⁰ However, some Rule 504-exempt offerors are allowed to solicit (advertise to) accredited investors under certain state registration exemptions that make their particular company 504-eligible.⁴¹

Rule 505 is in some ways more restrictive, and in other ways less so, than Rule 504.⁴² It raises the cap on offers or sales of equity from \$1 million to \$5 million in any twelve-month period.⁴³ At the same time though, it limits sales to thirty-five non-accredited investors total, while placing no limit on the number of accredited investors who may invest.⁴⁴ Importantly, general solicitation is prohibited under Rule 505 in all circumstances.⁴⁵ The purpose of the three Reg D exemptions (Rules 504-06), and in fact the whole of Reg D, is to provide a less demanding route for companies looking to offer securities to restricted groups of people in lieu of a traditional public offering.⁴⁶ The disclosure protections that typically come with registration are waived for Reg D offerings under the assumption that equity is only being offered to those who are informed enough to make sound decisions about investing.⁴⁷ Allowing registration-

either has no specific business plan or purpose or has indicated that its business plan is to engage in a merger or acquisition”).

36. 17 C.F.R. § 230.500-08.

37. 17 C.F.R. § 230.504.

38. *See id.*

39. The SCOR is a uniform state small corporate offering registration and is the most common method by which state offering registration takes place in accordance with Rule 504. In some states though, the SCOR process involves submitting very thorough risk assessments for potential investors. *See SCOR Overview*, N. AM. SEC. ADMIN. ASS'N, <http://www.nasaa.org/industry-resources/corporation-finance/scor-overview/> (last visited Feb. 19, 2013).

40. 17 C.F.R. § 230.502(c).

41. 17 C.F.R. § 230.504(b)(1).

42. *See* 17 C.F.R. § 230.505.

43. *Id.*

44. *Id.* Accredited investors fall into eight statutorily defined categories, the most important of which (from the perspective of a prospective crowdfunder) are individuals with a net worth of over \$1 million and individuals with an annual income of over \$200,000 or combined marital income of over \$300,000 as defined in Rule 501. 17 C.F.R. § 230.501.

45. 17 C.F.R. § 230.505.

46. *See Regulation D Offerings*, SEC, <http://www.sec.gov/answers/regd.htm> (last visited Feb. 19, 2013).

47. *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 124 (1953); *see also* Alan J. Berkeley, *Limitations on the Manner of Offering Under Regulation D*, in *REGULATION D OFFERINGS AND PRIVATE PLACEMENTS* (exploring the history of judicial interpretation of Rule 502's general solicitation prohibition—from its beginnings as a strict numerical limit on the number of investors that could be solicited, to a more general rule applied on a case-

exempt companies to advertise offerings to the public would seem to contravene the rationale behind the exemption and might open the door to abuse of Reg D offerings.⁴⁸

The restriction on general solicitation included in Rule 502 that is applicable throughout Reg D (with the exception of the aforementioned Rule 504 carve-out) is the main roadblock preventing equity crowdfunding from fitting into the existing SEC exemptions.⁴⁹ The fundamental innovation of equity crowdfunding is that, with the advent of the Internet, entrepreneurs and startup companies can find diverse groups of investors who are interested in owning stock in their company.⁵⁰ The restriction on advertisement written into Rule 502 is in place specifically to protect unsophisticated investors by prohibiting this type of outreach.⁵¹

Offerings under Rule 506, promulgated under § 4(2) of the '33 Act, are subject to the same solicitation restrictions covering the rest of Reg D.⁵² Companies can offer and sell an unlimited dollar amount in equity, but the Rule 506 exemption only permits companies to offer equity to accredited investors and, at most, thirty-five "sophisticated" individual investors.⁵³ The general test used to determine which investors qualify as sophisticated is whether the issuer "reasonably believes immediately prior to making any sale" that the investor in question has enough knowledge and experience in financial and business matters to enable him or her to properly evaluate the merits and risks of the investment.⁵⁴

Regulation A is another potential avenue for issuers looking to avoid the costs of registration.⁵⁵ The Regulation A exemption is limited to offerings of up to \$5 million in a one-year period and does have more relaxed limitations on general solicitation.⁵⁶ But the exemption comes with a series of disclosure costs that, although they are far lower than standard registration costs, commentators have argued would still prevent most potential crowdfunders from using Regulation A as an offering avenue.⁵⁷

The crowdfunding platforms themselves also run into cost barriers under the current regulatory regime, including the possibility that they would be required to register as brokers (though the cost to the platform itself might be passed on to the companies offering equity or to the inves-

by-case basis and guided by the types of individuals solicited and their connections to the equity offering at hand).

48. See, e.g., Berkeley, *supra* note 47.

49. See, e.g., Bradford, *supra* note 33, at 30.

50. See *supra* Part I.B.

51. See *Ralston*, 346 U.S. at 124-25.

52. See 17 C.F.R. § 230.506 (2012).

53. *Id.*

54. *Id.*

55. 17 C.F.R. § 230.251.

56. See Bradford, *supra* note 33, at 24.

57. See *id.* at 49 (citing Rutheford B. Campbell, *Regulation A: Small Businesses' Search for "A Moderate Capital,"* 31 DEL. J. CORP. L. 77, 111 (2006) for the proposition that small businesses are hesitant to use Regulation A because of the cost and complexities associated with completing the "mini-registration" process associated with Regulation A offerings).

tors by charging fees).⁵⁸ Section 3(a)(4) of the '33 Act defines a broker as "any person engaged in the business of effecting transactions in securities for the account of others."⁵⁹ When broken down into its component parts, this rule seems to apply to most, if not all, of the different possible forms of equity-based crowdfunding platforms. Crowdfunding websites are certainly "engaged in the business," as they are constant conduits for multiple offering ventures, not simply one-off participants.⁶⁰ The real question is whether these platforms are susceptible to being seen as "effecting transactions in securities for the account of others."⁶¹ It seems to be the case that they are: "[the typical crowdfunding enterprise's] receipt of transaction-based compensation, continued involvement in the investor-entrepreneur relationship, public advertising, and for-profit status may cumulatively be too much to allow them to avoid broker status" under the current legal regime.⁶²

D. Regulating Crowdfunding

There is, of course, a set of reasons behind the SEC's registration requirements and the high bar that they set.⁶³ The motivation to keep investors away from public offerings by startup companies is largely driven by the notion that, because of their inherent volatility, small businesses make extremely risky investments and are hard to accurately value.⁶⁴ There are high costs associated with transparency though, and forcing startup businesses to provide extensive information to the public before offering equity can (and does) disincentivize stock offerings.⁶⁵ These disclosure cost issues have contributed to an overall reduction in the number of Initial Public Offerings (IPOs) in general over the past decade.⁶⁶

58. 15 U.S.C. § 78c(a)(4) (2012) (outlining the various types of entities that are considered brokers). For a discussion of the new portal category created under the JOBS Act for crowdfunding platforms in contrast to the existing broker category, see *infra* Part I.D.

59. 15 U.S.C. § 78c(a)(4).

60. Bradford, *supra* note 33, at 24.

61. 15 U.S.C. § 78c(a)(4).

62. Bradford, *supra* note 33, at 66. Professor Bradford further breaks down whether actions like providing advice to investors could tilt the balance further towards broker classification, and runs through the SEC Division of Trading and Market's guide to determine broker status. Ultimately, the question of whether a portal receives transaction-based compensation seems to be the most important determinant of broker status from the perspective of the SEC. See *SEC v. Margolin*, No. 92 Civ. 6307 (PKL), 1992 WL 279735, at *5 (S.D.N.Y. Sept. 30, 1992).

63. See *infra* Part III.A.

64. Timothy Bates & Alfred Nucci, *An Analysis of Small Business Size and Rate of Discontinuance*, J. SMALL BUS. MGMT., Oct. 1989, at 1, 4 (noting that small businesses with low numbers of existing employees [startups] tend to be by far the most volatile ventures in terms of business prospects).

65. IPO TASK FORCE, REBUILDING THE IPO ON-RAMP: PUTTING EMERGING COMPANIES AND THE JOB MARKET BACK ON THE ROAD TO GROWTH 2 fig.B (2011), available at http://www.sec.gov/info/smallbus/acsec/rebuilding_the_ipo_on-ramp.pdf.

66. See *id.* (demonstrating that IPOs, particularly for companies with valuations under \$50 million, have been in drastic decline between the early 1990's and today, falling more than 75% since the high point in 1996).

The valuation-versus-transparency cost conundrum can be described along the lines of the “Gold Ring Problem,” a hypothetical tool used to explain situations in which an unknown asset has to be assigned a value before it can be sold, but there is not enough information available about the asset to come to a straightforward conclusion about its actual worth.⁶⁷ A typical member of the public coming across a small business trying to raise equity online through a crowdfunding website may not be in a measurably better position to assess worth than if he or she had found a gold ring on the street. But the financial risk in picking up a gold ring and having it graded by a jeweler is far less than in sinking large amounts of capital into a startup business. For this reason, the SEC has prioritized investor protection in regulating public offerings, and it will likely continue to do so while putting together the new crowdfunding rules.⁶⁸ Several pundits have made the argument that the risk to consumers in allowing investment crowdfunding is impermissibly greater than the potential reward and the benefits to the small businesses receiving their investments.⁶⁹

Part of the challenge facing an effective crowdfunding regulation regime will be to minimize fraud and maximize transparency while still keeping the transaction costs low for stock-issuing small businesses. In order to meet all of the SEC regulations typically designed to prevent fraud, companies must spend large amounts of time and money carefully filing documents that disclose the operations of their organizations and, to an extent, the methods by which they are already capitalized.⁷⁰ Without this sort of disclosure, it would be hard for prospective investors to get a good picture of how much risk is associated with a particular type of investment.

To combat the prohibitive costs that come along with disclosure, the new JOBS Act regulations amend § 4 of the '33 Act to include a number of substitute measures to lessen the amount of risk inherent in crowdfunding investments.⁷¹ Chief among these measures, listed in Title III of the JOBS Act, are strict limits on the amounts that individuals can invest in any crowdfunded businesses as well as limits on the amount that any business can raise through crowdfunding.⁷² The legislation limits investors who

67. Victor P. Goldberg, *The Gold Ring Problem*, 47 U. TORONTO L.J. 469, 469 (1997).

68. See Daniel M. Gallagher, Comm'r, SEC, Speech at SIFMA Regional Conference: SEC Priorities in Perspective (Sept. 24, 2012), available at <http://www.sec.gov/news/speech/2012/spch092112dmg.htm>.

69. See Edward Wyatt, *Senate Passes Start-Ups Bill, with Amendments*, N.Y. TIMES (Mar. 22, 2012), <http://www.nytimes.com/2012/03/23/business/senate-passes-start-ups-bill-with-amendments.html>; see also *Laws Provide Con Artists with Personal Economic Growth Plan*, N. AM. SEC. ADMIN. ASS'N, (Aug. 21, 2012), <http://www.nasaa.org/14679/laws-provide-con-artists-with-personal-economic-growth-plan>.

70. *Small Business and the SEC: A Guide for Small Businesses on Raising Capital and Complying with the Federal Securities Laws*, SEC, <http://www.sec.gov/info/smallbus/qasbsec.htm> (last modified Dec. 21, 2012) (describing the extent to which small business owners must disclose the same types of information that larger companies must provide).

71. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 302, 126 Stat. 306 (2012).

72. See *id.*

earn less than \$100,000 per year or have a net worth of less than \$100,000 to maximum annual crowdfunding investments of 5% of net worth or \$2,000 (whichever is greater).⁷³ An investor with over \$100,000 in annual income or a net worth above \$100,000 is limited to 10% of their annual income or net worth, whichever is higher, with a maximum cap at \$100,000 per year.⁷⁴ Issuers are not allowed to raise more than \$1 million per year through crowdfunding, and any issuers aiming to raise more than \$100,000 a year are subject to escalated disclosure requirements.⁷⁵ The basic disclosure regime under the JOBS Act requires any crowdfunded company to release ownership structure and the names of directors and certain shareholders; there are further (almost prohibitively extensive) disclosure requirements for any crowdfunded company aiming to raise more than \$500,000 in a year.⁷⁶

In addition to these more conventional regulations, the SEC is also going to rely on the crowdfunding platforms to vet stock issuers and protect investors.⁷⁷ Crowdfunding platforms, which, like Kickstarter or similar charitable counterparts, aggregate different small business offerors and present them to potential investors through a single digital face, would operate under the JOBS Act as intermediaries called “funding portals.”⁷⁸ Registered funding portals must conduct background checks as well as provide a certain uniform depth of information on every issuer that is participating in the market through their website.⁷⁹ Part of the purpose of this requirement is to encourage platforms to stake their reputation on becoming investment intermediaries devoid of fraudulent or even overly risky investments.⁸⁰ Forcing platforms to vouch for the offerings that they host seems to push, in a way, a market solution to the transparency problem.

On a broader scale, proponents of the new regulation also contend that the open nature of social media will also act as a preventative measure and keep risk out of the system.⁸¹ In theory, because of the fact that crowdfunding platforms will be open forums, any bad actors will be immediately spotted and weeded out by the crowd.⁸² There are, of course, some flaws in this approach, the biggest one being that the usefulness of social

73. *Id.*

74. *Id.*

75. *Id.* (including independent review of financial statements).

76. *Id.* (including full audits of financial statements).

77. See Sara Hanks, *Jobs Act Crowdfunding Provisions Await Clarification by SEC*, 44 SEC. REG. & L. REP. 1710 (2012) (describing the role of intermediaries in the JOBS Act).

78. See *id.* Crowdfunding platforms can also elect to meet the intermediary requirements of the JOBS Act by registering as traditional brokers. § 304, 126 Stat. 306. Note that for the purposes of this Note, the term “portal” is used to refer to crowdfunding platforms in general—the phrase “funding portal” is used to refer to the specific JOBS Act-enumerated category.

79. See § 304, 126 Stat. 306; Hanks, *supra* note 77, at 3.

80. See Hanks, *supra* note 77, at 3.

81. Sherwood Neiss & Jason Best, *Why the JOBS Act is a Win for Entrepreneurs and Investors*, INC.COM (Mar. 28, 2012), <http://www.inc.com/sherwood-neiss/why-you-can-feel-good-about-the-jobs-act.html>.

82. See *id.*

networks in combating one-off schemes is limited.⁸³ In a repeat game, however, where small businesses are looking for multiple rounds of funding, the fact that businesses have already been vetted multiple times by the users themselves can be an enormous benefit.⁸⁴ What remains to be seen is how effective crowdfunding platforms can be in encouraging open but fair discourse among end-users.⁸⁵ If platforms allow completely uncensored discussion, they could be introducing incentive to manipulate the market by defaming or unjustly criticizing certain equity-offering companies and not others.⁸⁶ This problem is potentially magnified by the anonymity that the Internet allows.⁸⁷

II. Equity Crowdfunding Abroad

A. The United Kingdom

Probably the earliest example of crowdfunding success in the Internet age comes from the United Kingdom, where rock band Marillion raised over £35,000 in 1997 to bankroll their first tour of the United States.⁸⁸ Crowdfunding through established portals emerged as a phenomenon in Europe more-or-less contemporaneously with the growth of crowd-based websites in the United States.⁸⁹ The United Kingdom, in particular, has been a hotbed of crowdfunding activity over the last two or three years, with at least two portals offering active equity crowdfunding.⁹⁰ While Kickstarter only recently brought its platform to the United Kingdom, the art world has embraced crowdfunding for a number of years already through independent platform sites like Space Hive (which focuses on improving public spaces) and project-specific crowdfund campaigns.⁹¹ As evidence of the successes of crowdfunding in the United Kingdom, mem-

83. See Susan Block-Lieb, *E-reputation: Building Trust In Electronic Commerce*, 62 LA. L. REV. 1199, 1214 (2002) (describing the debate over whether negative feedback on eBay can successfully drive out bad actors and how long that process can take).

84. See *id.* at 1210–12, 1216 (demonstrating that even imperfect e-market feedback can be an effective fraud deterrent when enough individuals participate).

85. See *id.* at 1208.

86. *Id.* (discussing the chilling effect of retaliatory negative feedback in online marketplaces).

87. See Christine Souhrada, Note, *Securities Fraud, Market Manipulation, and the Internet*, 2002 UCLA J.L. & TECH. NOTES 28 (2002) (noting that the SEC has already begun to examine the problem of individuals disseminating false information over the Internet in order to manipulate stock prices).

88. Even though their lead singer once acknowledged that they were the “least hip” band in the world, a dedicated U.S. fan base and the advent of the Internet helped revitalize the band in the late 1990s. Jake Wallis Simmons, *Crowdfunding: How the Kindness of Strangers is Changing Business*, TELEGRAPH (Oct. 24, 2012), <http://www.telegraph.co.uk/culture/9599846/Crowdfunding-how-the-kindness-of-strangers-is-changing-business.html>.

89. See *id.*

90. Mike Wendling, *Crowdfunding Start-Ups Show How to Sidestep Bank Loans*, BBC NEWS (Aug. 22, 2012), <http://www.bbc.co.uk/news/business-19286163>.

91. Patrick Hussey, *Crowdfunding: What You Need to Know*, GUARDIAN (Aug. 16, 2012), <http://www.guardian.co.uk/culture-professionals-network/culture-professionals-blog/2012/aug/16/kickstarter-uk-launch-crowdfunding-culture>.

bers of the arts and entertainment worlds and the interactive gaming industry have recently come together from across the United Kingdom to deliberate on and disseminate a series of proposals to facilitate crowdfunding for both commercial and cultural purposes.⁹²

Securities offerings in the United Kingdom are mainly governed by the Financial Services Authority (FSA) under the guidance of the Financial Services Markets Act of 2000 (FSMA).⁹³ Though the FSMA became law fairly recently, it does not specifically contemplate crowdfunding; however, it does contain a number of regulations that have been loosely adapted to crowdfunding (at least for the time being, until the United Kingdom passes explicit equity crowdfunding laws).⁹⁴ Under the FSMA regulatory system, any invitation or inducement to engage in investment activity is considered a “financial promotion.”⁹⁵ Similar to the prohibition on general solicitation laid out by the SEC, the regulatory scheme surrounding financial promotions seeks to prevent unauthorized or nonexempt individuals or organizations from advertising equity offerings to the public.⁹⁶ The FSA does, however, include carve-outs for seeking investment from friends and family or other “connected persons” in pre-incorporation stages.⁹⁷ Any other form of financial promotion conducted by an equity crowdfunding portal must be conducted by either an FSA-authorized entity or under a specified exemption.⁹⁸

The exempted groups of investors to whom securities can be offered look very similar to the SEC’s groups of accredited or sophisticated investors who are allowed to invest in equity offerings under the various rules in Reg D.⁹⁹ Two of the more important exempt classes are “high net worth individuals”—persons with income of €100,000 or assets of €250,000 excluding their pensions and any insurance policies—and “sophisticated investors”—persons with a connection to the financial industry, such as members of angel networks,¹⁰⁰ or individuals employed by financial institutions.¹⁰¹ Importantly, any of these exempted persons must file a certifi-

92. ASS’N FOR U.K. INTERACTIVE ENTMT, UKIE CROWD FUNDING REPORT: A PROPOSAL TO FACILITATE CROWD FUNDING IN THE UK 2 (2012), available at http://media.sponge.com/ukie_crowd_fund_feb_2012.pdf.

93. See London Funding Conference, *Crowd Funding, Staying on the Right Side of the FSA Part 2*, YOUTUBE (Apr. 6, 2011), <http://www.youtube.com/watch?v=qWgKbewv7FY>; Financial Services and Markets Act, 2000, c. 8, § 1 (Eng.).

94. Financial Services and Markets Act, ch. 8, § 1.

95. *Id.* § 21.

96. *Id.*

97. *Id.* ch. 8, § 1.

98. *Id.*; London Funding Conference, *supra* note 93.

99. See *id.*

100. Angel investors are wealthy individuals who invest their own capital in small businesses, typically in return for equity or convertible debt. See Greg Novak, *Angel Networks Are Local and Global*, WALL ST. J. (Jan. 17, 2013, 2:25 PM), <http://blogs.wsj.com/accelerators/2013/01/17/angel-networks-are-local-and-global/> (describing how networks of angel investors form and pool together funds to invest in early-stage businesses).

101. Financial Services and Markets Act, § 21; see also London Funding Conference, *supra* note 93.

cate in compliance with the FSMA standards certifying that they are qualified to receive financial promotions under one of the exempt categories before they actually receive any financial promotion.¹⁰² What this essentially means is that any crowdfunding portals operating along the lines of these specified FSMA exemptions would have to prevent users from viewing the various funding opportunities that are being hosted on the site until the users have completed a thorough certification process.¹⁰³ If this provision is actually enforced stringently, it could become a major obstacle to portals looking to attract users, even those who actually qualify for financial promotion. A London-based software vendor that has independently begun to crowdfund in order to raise money has taken this approach by hiding their crowdfunding activities behind a “restricted page” that requires users to certify that they meet one of the exempt categories (which are laid out in clickwrap).¹⁰⁴ Whether this approach would work for a crowdfunding portal is yet to be seen, but it would seemingly be a major deterrent to potential end-users (members of the public) who might be hesitant to commit to signing certificates or waivers before actually accessing websites.

The FSMA also places limits on the number of people who can invest under exempt categories as well as the total amount of equity that can be offered under the exemptions. The total number of individuals who can take equity in an exempt offering was originally 100, but has moved to 150 over the past year.¹⁰⁵ And the total amount of equity that can be offered was €2.5 million, but has risen to €5 million over the past year.¹⁰⁶

In addition, the FSA also lays out a set of rules governing so-called “arranging,” or making arrangements which introduce investors to investees.¹⁰⁷ Similar to the question of whether a crowdfunding platform would need to register as a broker in the United States under the Securities Exchange Act, it is an open question whether crowdfunding platforms in the United Kingdom would need to register with the FSA under the “arranging” provision.¹⁰⁸ The “arranging” provision has “always been viewed as being a little ambiguous” by the lawyers who most frequently encounter it in securities cases, and the case law surrounding the issue is

102. See London Funding Conference, *supra* note 93.

103. See *id.*

104. See *Trampoline Crowdfunding Full Details*, TRAMPOLINE SYS., <http://crowdfunding.trampolinesystems.com/fulldetails> (last visited July 24, 2013) (showing that users certify that they meet the requirements through clickwrap agreements). Clickwrap agreements are computer-based agreements typically found in the software installation context where users must acknowledge the terms of an agreement by clicking “I Agree” before the installation process can go forward. See Kevin W. Grierson, *Enforceability of “Clickwrap” or “Shrinkwrap” Agreements Common in Computer Software, Hardware, and Internet Transactions*, 106 A.L.R. 5th 309, 317 n.1 (2003) (outlining the evolution of the legal landscape surrounding clickwrap).

105. See London Funding Conference, *supra* note 93.

106. *Id.*

107. Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, art. 14, S.I. 2001/544.

108. See London Funding Conference, *supra* note 93.

fairly light.¹⁰⁹ The FSA does offer interpretation guidelines for judges (PERG guidance (2.7.7B)), but has recently stated that it will seek to refresh those guidelines since, in the opinion of the FSA, they are currently being interpreted too narrowly.¹¹⁰ Still, current interpretation of the “arranging” rules seems to favor crowdfunding portals, as they are not actively persuading individuals to invest in certain offerings.¹¹¹ As long as the portals do not offer specific advice on which projects to invest in, they can probably narrowly avoid the “arranging” label by claiming that they are only acting as passive conduits between investors and equity offerings.¹¹²

Another important consideration in the context of U.K. crowdfunding regulation is the “collective investment scheme” model.¹¹³ This ordinarily occurs when funds from large numbers of individuals are pooled into a joint account for the purpose of investing in a variety of forms of investment.¹¹⁴ This type of arrangement, similar to an “investment contract” under the Securities Act and the Exchange Act in the United States, is regulated even more strictly than typical FSA-regulated offerings.¹¹⁵ Promoting collective investment schemes is particularly difficult, and there are additional requirements limiting the types of securities that collective investment schemes can invest in, as well as limits on who can manage authorized collective schemes.¹¹⁶

Whatever form crowdfunding portals may take, there are hints that the FSA will tighten the reins for compliance with the FSMA.¹¹⁷ In August of 2012, the FSA gave its first public notice about crowdfunding sites, saying that they should only be “targeted at sophisticated investors who know how to value a start-up business, understand the risks involved and that investors could lose all of their money.”¹¹⁸ The FSA also recognized that some firms involved in crowdfunding might currently be operating without authorization, but, importantly, did not give any hint as to how this would

109. Jake Green, *The Regulated Activities Order: Arranging Deals in Investments*, NABARRO LLP, 2 (June 17, 2009), <http://www.nabarro.com/downloads/the-regulated-activities-order-arranging-deals-in-investments.pdf>.

110. *Id.* (noting that the examples laid out in the current guidelines are being treated by judges as if they were an exhaustive list of all of the possible “arranging” scenarios, while the FSA had intended the examples to merely be instructive in assessing unique situations).

111. *Id.*

112. *See id.*

113. Financial Services and Markets Act, 2000, c. 8, § 21 sched. 2.8 (Eng.).

114. *See* Justin Aronson, Note, *Lessons For The United Kingdom: How Registration And Prospectus Requirements Have Inhibited Condo-hotel Investment Offerings*, 35 SYRACUSE J. INT'L. L. & COM. 95, 114 (2007).

115. *Id.*

116. *See id.*; *see also* FSA, THE COLLECTIVE INVESTMENT SCHEME INFORMATION GUIDE 4, available at www.fsa.gov.uk/pubs/foi/collguide.pdf.

117. *See* James Hurley, FSA: ‘Crowdfunding’ for Sophisticated Investors Only, TELEGRAPH (Aug. 17, 2012, 9:57 AM), www.telegraph.co.uk/finance/yourbusiness/9482082/FSA-Crowdfunding-for-sophisticated-investors-only.html.

118. *Id.* (internal quotations omitted).

be handled.¹¹⁹

The two main U.K.-based equity crowdfunding entities that have emerged to date are Crowdcube and Seedrs, and each has taken a somewhat different approach to operating within the current legal arena.¹²⁰ Seedrs has actually become the first crowdfunding portal to receive FSA approval and is operating as fully registered and authorized, but is limiting itself to investors who are deemed knowledgeable enough to pass a discretionary vetting process.¹²¹ Presumably it is doing this to protect itself from future regulatory attacks (hedging against the enormous uncertainty facing crowdfunding portals), but in doing so it could be keeping out a very large number of potential users. On the other hand, Crowdcube, a slightly better known portal, has been presenting equity opportunities without FSA approval.¹²² Instead, Crowdcube currently operates more like an open forum where would-be investors can view pitches from individual companies and then engage in nominally independent equity purchases.¹²³ Whether this work-around will result in some form of action by the FSA is yet to be seen, but Crowdcube may already be in hot water after allegations that it misled investors by manipulating, or allowing the manipulation of, one of the offerings hosted on its site.¹²⁴

B. Italy

Perhaps a more accurate parallel for the crowdfunding phenomenon in the United States (though less predictive of things to come than illustrative of the current path) is the Italian experience.¹²⁵ While active equity crowdfunding is much less widespread in Italy than in the United Kingdom, Italy seems to be on a more similar course to the United States in terms of the general regulation and management of equity crowdfunding activities.¹²⁶

The few existing surveys of the entire crowdfunding industry in Italy (equity, charitable, and otherwise) seem to paint a similar picture to the one emerging in the United States.¹²⁷ Of the prominent crowdfunding por-

119. *Crowdfunding: Is Your Investment Protected?*, FSA, http://www.fsa.gov.uk/consumerinformation/product_news/saving_investments/crowdfunding (last updated Oct. 8, 2012).

120. ASS'N FOR U.K. INTERACTIVE ENTMT, *supra* note 92, at 7.

121. *Id.*

122. *Id.*

123. *See How Does Funding Work?*, CROWDCUBE, <http://www.crowdcube.com/pg/crowdcube-faq-20#howfundingworks> (last visited Oct. 10, 2012) (describing that the firm Ashfords LLP actually completes the arrangement).

124. James Hurley, *Peer-to-Peer Website Accused of Misleading Investors*, TELEGRAPH (May 8, 2012, 11:40 AM), <http://www.telegraph.co.uk/finance/businessclub/9251891/Peer-to-peer-website-accused-of-misleading-investors.html>.

125. *See infra* Part II.B.

126. *Id.*

127. *See* DANIELA CASTRATARO & IVANA PAIS, ANALYSIS OF ITALIAN CROWDFUNDING PLATFORMS 3 (2012), available at <http://twintangibles.co.uk/wp-content/uploads/2012/12/CrowdfundingInItaly1.pdf>; see also Giancarlo Guidici et al., *Crowdfunding: The New Frontier for Financing Entrepreneurship?*, POLITECNICO DI MILANO: DIPARTIMENTO DI INGEGNERIA GESTIONALE (Oct. 5, 2012), available at <http://papers.ssrn.com/sol3/papers.cfm?abstract>

tals in Italy, only one is currently operating to provide any sort of equity for investors, and it is doing so only by directly connecting investors with entrepreneurs, not by offering actual open investment portal services.¹²⁸ The rest are either operating as purely charitable enterprises, or are encouraging users to invest set amounts of money in return for gifts or awards.¹²⁹ But, by far, the most common form of crowdfunding activity in Italy is microlending, with an estimated 78% of all money raised through crowd portals in the country moving through microlending avenues.¹³⁰ Microlending in Italy has accounted for about €10 million in successfully funded projects to date.¹³¹ Equity-based portals (not true equity crowdfunding portals, but networks of angels organized to directly connect investors with projects) account for about €2 million of funded projects, and gift or reward-based programs account for about €1 million.¹³²

The average size of funding rounds for lending and gift-based projects in the Italian crowdfunding marketplace is several thousand euros (€2,600 for gift-based and €4,500 for lending), while equity projects in the country typically tend to raise money at greater orders of magnitude, the average equity project bringing in close to €250,000 per round.¹³³ However, this noticeable gap in funding size (with the average equity offering bringing in one hundred times more capital) is probably not entirely indicative of how equity crowdfunding rounds will look in the future, in Italy and elsewhere.¹³⁴ Because the forms of equity crowdfunding occurring in Italy right now look more like website-based incarnations of angel networks, the rounds being raised by each project look, in size, like angel network investments.¹³⁵ True equity crowdfunding portals would likely host a range of projects looking for funding at levels far below the amounts that angel investors typically seek to invest.¹³⁶ In fact, a 2011 study of the various equity crowdfunding efforts globally demonstrated that almost half of the projects raised only between \$50,000 and \$250,000 per round, and a full

_id=2157429 (highlighting Eppela, SiamoSoci, Boomstarter, Starteed, Kapipal, ProduzioniDalBasso, FundForCulture, Crowdfunding Italia, De Revolutione, and Zummolo, among others).

128. Guidici et al., *supra* note 127, at 9 (discussing SiamoSoci, which behaves more like a network of angel investors than a crowdfunding portal in comparison to the other crowdfunding portals currently in operation in Italy, which all either operate on a purely charitable basis or on a gift basis).

129. *See id.*

130. CASTRATARO & PAIS, *supra* note 127, at 9.

131. *Id.*

132. *Id.*

133. *Id.* at 10.

134. *See id.*

135. *See* Scott Shane, *The Size of Angel Investments*, SMALL BUS. TRENDS (Nov. 3, 2008), <http://smallbiztrends.com/2008/11/the-size-of-angel-investments.html> (highlighting that in 2008 the average amount of angel investment received per company was around \$370,000).

136. *See* CROWDSOURCING, CROWDFUNDING INDUSTRY REPORT: MARKET TRENDS, COMPOSITION AND CROWDFUNDING PLATFORMS (2012), available at <http://www.crowdsourcing.org/document/crowdfunding-industry-report-abridged-version-market-trends-composition-and-crowdfunding-platforms/14277>.

quarter of all projects raised less than \$50,000.¹³⁷

Italian crowdfunding portals, besides taking a number of different approaches to fundraising, are also legally organized in a number of different ways.¹³⁸ The majority are organized as Srl organizations (similar to the United States Ltd.), with only two registered as Spa (the Italian equivalent of a public corporation).¹³⁹ A small few are not legal entities at all, but most seem to be at the very least listed in the publicly available nationwide Company Register.¹⁴⁰ It is important to note though, that just because a portal is itself a registered company, its actions are not necessarily condoned by the Commissione Nazionale per le Società e la Borsa (CONSOB), the Italian equivalent of the SEC.¹⁴¹

Until recently, the CONSOB did not have any official position on crowdfunding, but in October of last year the Italian legislature passed the second Decreto Crescita, a decree that “among other things, legalizes equity crowdfunding.”¹⁴² In much the same way that the SEC needs to go through the rulemaking process to refine the JOBS Act before it comes into effect, the CONSOB will need to review this section of the Decreto Crescita to determine exactly how it will shape Italy’s crowdfunding future.¹⁴³ However, it is already clear that crowdfunding under the Decreto Crescita will have at least one key difference from the crowdfunding regime in the United States: only “high-tech businesses” will be authorized in Italy to offer equity through crowdfunding portals.¹⁴⁴ How exactly the CONSOB will define and give shape to the term “high-tech” remains to be seen since the Decreto only specifies that crowdfunding should be available to companies active in the “development and commercialisation of high-tech value products or services.”¹⁴⁵ The fact that the Italian legislature has prioritized the technology industry in opening up avenues for crowdfunding does not necessarily mean that the law will not eventually be adapted to include other forms of business venture though.¹⁴⁶ There is a general sense that this first step is designed to allow the Italian equity market to slowly develop a taste for crowdfunding that can later be expanded upon if demand presents itself and if the first portals and first rounds of funding

137. *Id.*

138. CASTRATARO & PAIS, *supra* note 127, at 10.

139. *Id.*

140. *Id.*; see also *Services: For the Public Administration*, ITALIAN CHAMBER COM. REGISTRY, <http://www.registroimprese.it/en/per-la-pubblica-amministrazione#page=registro-imprese-pa> (last visited Apr. 27, 2013).

141. See *Intermediaries - Register of Investments Firms*, CONSOB, http://www.consob.it/mainen/intermediares/investments_firms/index.html (last visited Mar. 8, 2013) (listing all CONSOB-approved intermediaries).

142. Anton Root, *A Closer Look at Italy’s Crowdfunding Law*, CROWDSOURCING (Oct. 10, 2012, 6:12 PM), <http://www.crowdsourcing.org/editorial/a-closer-look-at-italys-crowdfunding-law/20096>; see Decreto Legislativo 83/2012, in G.U. 187/2012.

143. See Root, *supra* note 142.

144. *Italy’s Crowdfunding Law Has Many Similarities to the JOBS Act*, CROWDFORCE (Oct. 19, 2012), <http://crowdforce.co/italys-crowdfunding>.

145. *Id.* (internal quotations omitted).

146. See *id.*

run smoothly.¹⁴⁷ Limiting the first equity rounds to one specific industry also allows the CONSOB to focus more explicitly on investor education.¹⁴⁸

Besides this industry-based limitation, the Decreto also lays out a number of more general guidelines for CONSOB rulemaking.¹⁴⁹ In order to limit crowdfunding efforts to the small businesses that need it the most, companies that have been in existence for longer than forty-eight months will be ineligible for equity crowdfunding, and companies with total yearly outputs of over €5 million euros (by the second year of operation) cannot offer equity through crowdfunding portals.¹⁵⁰ Importantly, crowdfunding rounds will have to be co-signed (in a way) by seasoned investors.¹⁵¹ Any company looking to offer equity through a crowdfunding portal will be required to first raise money through offerings to traditional sophisticated investors or venture capitalists.¹⁵² This provision is designed to protect less knowledgeable shareholders from potential abuse and unexpected changes to their rights in future funding rounds involving sophisticated investors (a problem that will be explored further in this Note).¹⁵³

C. France

After the United States (191) and the United Kingdom (44), the nation with the largest number of active crowdfunding platforms is France (28 as of 2012).¹⁵⁴

The French phrase “finance participative” has been adopted as a parallel to “crowdfunding,” and the idea has grown strong roots, especially in the arts world.¹⁵⁵ It is unsurprising that crowdfunding has taken hold in France, where a similar system of community-style investing and lending has already been in existence for more than twenty years: the “club d’investisseurs pour une gestion alternative et locale de l’épargne solidaire” (CIGALES) movement.¹⁵⁶ In the pre-internet era, CIGALES investment

147. *See id.*

148. *See id.*

149. *See id.*

150. *Id.*

151. *See id.* (explaining that a professional investor or venture capitalist will have to anchor any crowdfunding offering).

152. *See Root, supra* note 142.

153. *See id.*; *infra* Part III.B.

154. CROWDSOURCING, *supra* note 136, at 17.

155. *See France Crowd Funding Restorations*, UNITED PRESS INT’L (Jan. 11, 2013, 8:45 AM), http://www.upi.com/Top_News/World-News/2013/01/11/France-crowd-funding-restorations/UPI-42581357911935 (describing efforts by the French National Monuments Agency to raise money from the public to dedicate to restoration of cultural centers and national monuments); *see also* KISSKISSBANKBANK, <http://www.kisskissbankbank.com/en> (last visited Jan. 2, 2013) (providing descriptions of various arts-based crowdfunding projects based in France).

156. *See generally* Arvind Ashta et al., *Social Innovation Lessons from Microangels? An Institutional Entrepreneurship Case Study of the CIGALES Movement in France*, 3 (Burgundy Sch. of Bus., Working Paper No. 25, 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2031732 (describing the emergence and growth of the CIGALES movement).

clubs were the ideological forerunners for the crowdfunding movement.¹⁵⁷

CIGALES operates as a federation of democratically governed local clubs in which individual investors pool together their savings to support small businesses or other microenterprises.¹⁵⁸ Individual contributions to a CIGALES club can be anywhere from €7.50 to €450 per month, and each club is comprised of between five and twenty members.¹⁵⁹ Most clubs invest solely in ethically operated local small businesses or businesses with particular social or cultural goals, and they do not generally expect returns on their investment.¹⁶⁰ Importantly though, as an incentive to participate in investment in local or socially conscious businesses, club members receive a 25% income tax deduction on any sums invested (through the Madelin law), as well as a 50% wealth tax deduction on any of their investments in small and medium-size enterprises (through the TEPA law).¹⁶¹ All clubs are organized centrally under the federation, which acts less as a governing body than a flag-bearer for the movement, but does collect subscription fees which are for the most part redistributed to the local clubs (as is the case with many crowdfunding portals, these fees are also used in part to support the federation staff and its day-to-day operations).¹⁶²

CIGALES clubs operate legally in France under the provision in the civil code allowing for “indivisions.”¹⁶³ Indivisions are similar to tenancies in common under English law, and in France major financial institutions have been using indivisions since the 1970s as vehicles to collectivize investments for large institutional clients under the Monory law (a law originally established to allow employees to own shares in the companies that employ them).¹⁶⁴ The founders of the CIGALES movement seized the opportunity to use these indivision-based investment pools, which, by championing small business and taking into account specific ethical and social responsibilities, they believed could have a net positive impact on both the French economy and French society as a whole.¹⁶⁵

The CIGALES movement has stagnated a bit due to changes in the tax structure governing small business investments and flagging interest in the broader social investment idea; however, it does provide some important lessons for the fledgling equity crowdfunding industry in France.¹⁶⁶ In a series of interviews asking members of CIGALES clubs to identify key problems with the club-based investment system, one of the issues that

157. *See id.*

158. *See Ashta et al., supra* note 156, at 15.

159. *Id.* at 14.

160. *Id.*

161. *Id.* at 24.

162. *See id.* at 15.

163. *See id.* at 19.

164. *Id.*

165. *Id.*

166. *Id.* at 24–27 (exploring the reasons behind the slowing growth of CIGALES clubs and the dissolution of certain local chapters).

arose most frequently was the limited opportunity for exit.¹⁶⁷ Many club members reported that it is too difficult to successfully take money out of a CIGALES club after periods of funding.¹⁶⁸ Even though CIGALES investors are content to make no profit on their investments (save for their tax-exempt status), they still enter into the various arrangements expecting to be able to get back at least some of the capital that they put in and say that they would be less likely to participate if they are not guaranteed some form of exit opportunity if needed.¹⁶⁹ If difficulties pulling out money can disincentivize even members of this type of altruistic club, then the exit expectations of individuals looking for returns through equity crowdfunding portals need to be carefully considered.¹⁷⁰

Fortunately, a French portal called WiSeed, which does offer equity investment, has provided what might be the first answer to the exit question.¹⁷¹ In October of 2012, a pharmaceutical development company called Antabio, which had raised early stage funding on WiSeed, became the first company to reach an important milestone in the development of equity crowdfunding—over two hundred crowd investors received a profitable return in an exit event.¹⁷² In fact, not only did the investors make a return, some made as much as 70% on their initial investment when a larger pharmaceutical development company bought out all of Antabio's existing shares.¹⁷³ Of course, one successful buyout does not mean that the marketplace has figured out how to absorb crowdfunded businesses; profitable exits are few and far between for seed stage investors, and exits at a loss in equity crowdfunding environments would seem to present a host of unanswered problems.¹⁷⁴ Members of the French crowdfunding world have put forward regulatory suggestions that hit on some of these problems, but in a less than fully fleshed out marketplace it is difficult to make precise recommendations.¹⁷⁵

167. *Id.* at 35.

168. *Id.*

169. *Id.*

170. Long-term capital lock-in is a significant feature of venture capital, and one that has only become more pervasive with the recent decrease in IPOs. See Darian M. Ibrahim, *The New Exit in Venture Capital*, 65 VAND. L. REV. 1, 12 (2012). Considering the limitations on transferability that the JOBS Act imposes, crowdfunding investments will likely be even more illiquid than traditional venture capital investments. See Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 302(b), 126 Stat. 306 (2012); see also *infra* Part III.A.

171. See *World-Premier Successful Exit in Equity Crowdfunding!*, SEEDING FACTORY (Oct. 18, 2012), <http://seedingfactory.com/2012/10/world-premier-equity-crowdfunding-exit>.

172. *Id.*

173. *Id.*

174. Recent research suggests that in more than a third of traditional venture capital investments, investors eventually lose all of their money, and further, more than 95% of investors earn less than their projected returns. See Deborah Gage, *The Venture Capital Secret: 3 Out of 4 Start-Ups Fail*, WALL ST. J. (Sept. 19, 2012, 9:32 PM), http://online.wsj.com/article/SB10000872396390443720204578004980476429190.html?mod=WSJ_article_comments#articleTabs%3Darticle (discussing unpublished research and commentary by Harvard Business School lecturer Shikhar Ghosh).

175. See FINPART, LIVRE BLANC: FINANCE PARTICIPATIVE, PLAIDOYER ET PROPOSITIONS POUR UN NOUVEAU CADRE RÉGLEMENTAIRE (2012), available at <http://finpart.org/down>

D. Elsewhere in the European Union and the Rest of the World

In 2011, with respect to all forms of crowdfunding, an estimated €300 million moved through crowdfunding portals based in the European Union or on EU web domains.¹⁷⁶ This represented a quarter of the €1.2 billion global crowdfunding marketplace, which has grown so rapidly that it has nearly doubled in size every year since 2009 and is estimated to have almost doubled again between 2011 and 2012 to €2.2 billion.¹⁷⁷ Driven almost entirely by the European market, equity crowdfunding in particular has demonstrated a tremendous capacity for growth, with a compound annual growth rate (CAGR) (in market size measured by number of campaigns) of 114% since 2009.¹⁷⁸

Still, crowdfunding laws throughout much of the European Union are unclear, and, in most cases, equity crowdfunding is being conducted without explicit regulatory approval or disapproval.¹⁷⁹ In Germany, for instance, the basic assumption until recently was that crowdfunding platforms could only raise as much as €100,000 per project.¹⁸⁰ The founder of equity platform Seedmatch challenged this paradigm though, by drawing up arrangements between investors and equity-offering companies based on “a so called ‘partiarisches Darlehen’ or a profit participating loan” contract.¹⁸¹ The German financial authority recognized and accepted this bit of innovation, and Seedmatch can now raise equity rounds above the €100,000 limit, but it faces an uncertain future with regards to laws governing the screening of potential investors and fundraisers.¹⁸² Recently, the German financial authority BaFin offered an advisory note outlining several important considerations for prospective crowdfunding portals, but instead of outlining any new or developing regulatory program specifically tied to crowdfunding, simply made note of the existing regulations that might restrict or prohibit certain types of crowdfunding platforms or activity.¹⁸³ For the most part though, this is how equity crowdfunding portals across the rest of the European Union are operating—by assessing the current legal landscape in each specific coun-

load/plaidoyer-juin (describing the limited existing regulatory framework for crowdfunding in France and suggesting that the current laws are too tied to pre-internet investment realities).

176. KRISTOF DE BUYSERE ET AL., A FRAMEWORK FOR EUROPEAN CROWDFUNDING 21 (2012), http://www.europecrowdfunding.org/Resources/Documents/Framework_EU_Crowdfunding.pdf.

177. *Id.*

178. CROWDSOURCING, *supra* note 136, at 17.

179. *See supra* Part II.A-C.

180. Raf Weverbergh, *Crowdfunding: Seedmatch is Going Where No Kickstarter Has Gone Before*, WHITEBOARD (last visited Jan. 2, 2013), <http://www.whiteboardmag.com/crowdfunding-kickstarter-seedmatch> (explaining that crowdfunding in Germany was originally understood as falling under the ‘silent partner’ (stille Beteiligung) laws, which place a \$100,000 cap on investment activity).

181. *Id.* (emphasis omitted).

182. *Id.*

183. Jörg Begner, *Crowdfunding and Supervisory Laws*, BaFin Q., 3Q 2012, at 8 available at http://www.bafin.de/SharedDocs/Downloads/EN/Mitteilungsblatt/Quarterly/bq1203.pdf?__blob=publicationFile.

try and attempting to retrofit an equity-offering platform to the existing set of regulations.¹⁸⁴

Beyond Europe, the crowdfunding landscape is even more embryonic, and while there is a large amount of capital and willingness to participate, less than 5% of all active crowdfunding platforms are based outside the United States or Europe.¹⁸⁵ The one notable equity-based platform in Asia is GrowVC, a Hong Kong-based organization with ties to the crowdfunding community in Finland.¹⁸⁶ It operates somewhat differently than most other equity portals though, in that instead of hosting projects that individual investors can choose among, it pools capital from all of the site's users and invests in selected companies as a fund.¹⁸⁷ Users still have a say in which companies receive funding, but this setup allows for more streamlined funding processes and has the added benefit of aligning the interests of the portal and investors in certain cases.¹⁸⁸

By far the most distinctive and developed crowdfunding system is the Australian Small Scale Offerings Board (ASSOB).¹⁸⁹ Organized like a typical stock market, the ASSOB hosts unlisted Australian companies looking to offer freely transferrable equity in compliance with § 708 of the Australian Corporations Act.¹⁹⁰ While it limits each equity offering to twenty non-sophisticated investors per year and requires listed companies to offer disclosure through "sponsors" (typically professionals experienced in securities offerings), it still presents an interesting example of an effective crowdfunding regime, if one that looks very different than what crowdfunding will likely look like in the United States.¹⁹¹

Equity crowdfunding has also reached the Middle East, with one particularly notable effort in Egypt to develop a crowdfunding portal that adheres to Islamic banking law.¹⁹² Because Islamic law circumscribes certain lending practices and interest-bearing investment, the developers of Shekra.com have devised a way to incorporate the developed principle of

184. See Eze Vidra, *Startup Equity Crowdfunding Grows in Europe (NESTA Report)*, VC CAFE (July 4, 2012), <http://www.vccafe.com/2012/07/04/startup-equity-crowdfunding-grows-in-europe-nea-report> (comparing WiSeed, Crowdcube, and Seedrs with Symbid in the Netherlands and MyMicroInvest in Belgium, and exploring the different investment vehicles and post-investment rights of investors in each country).

185. CROWDSOURCING, *supra* note 136, at 18.

186. Mike Butcher, *Grow VC Launches, Aiming to Become the KIVA for Tech Startups*, TECHCRUNCH (Feb. 15, 2010), <http://techcrunch.com/2010/02/15/grow-vc-launches-aiming-to-become-the-kiva-for-tech-startups>.

187. *Id.*

188. *Id.*; see *Users*, GROWVC, <http://www.growvc.com/main/about/users/> (last visited Jan. 4, 2013).

189. *About ASSOB*, AUSTRALIAN SMALL SCALE OFFERINGS BOARD, <http://www.assob.com.au/about.asp?page=1> (last visited Jan. 10, 2013).

190. *Id.*

191. Jonathan Sandlund, *Exploring ASSOB: A \$130 Million Crowdfunding Model that Works*, THECROWDCAFE (Nov. 12, 2012), <http://www.thecrowdcafe.com/exploring-assob-a-crowdfunding-model-that-works>.

192. Ahmed Lofty, *Islamic Crowd Funding Portal Launched in Egypt*, REUTERS (Nov. 12, 2012, 7:26 AM), <http://www.reuters.com/article/2012/11/12/islamic-finance-egypt-idUSL5E8MC7FN20121112>.

'mudharabah' (profit sharing) into the crowdfunding formula.¹⁹³ Rather than taking a commission on each investment, Shekra will co-invest in each enterprise and generate income by sharing in a portion of the profits with other investors according to a specific formula.¹⁹⁴

III. The JOBS Act and the Future of Crowdfunding in the United States

A. Proposals and SEC Rulemaking

The various provisions of the JOBS Act were advocated for at length in the months and years before the passage of legislation; often in more-or-less stringent terms than those that the bill ultimately laid out.¹⁹⁵ But while the Act itself might not have provided exactly what crowdfunding advocates were looking for, the actual equity crowdfunding regime in the United States may depend more on the rulemaking of the SEC and FINRA (as the SRO)¹⁹⁶ than the contents of the Act itself.¹⁹⁷ The SEC rulemaking process was supposed to come to a close before January 1, 2013, but the SEC has yet to publish any rules, and conservative estimates say that rules will not likely be promulgated until the start of 2014, at the earliest.¹⁹⁸

While the process of receiving comments and rule proposals has begun, the sheer volume of work that the SEC needs to complete before regulations can be announced (both on this piece of legislation and others in the queue) is enormous.¹⁹⁹ Before completion, any published rules must be justified according to a series of SEC priorities including economic efficiency, economic impact, and impact versus alternative rules or solutions.²⁰⁰ Importantly, due to a series of recent court decisions, the SEC must perform economic cost-benefit analyses on every rule in order to determine what effects implementation would have on "efficiency, compe-

193. *See id.*

194. *Id.*

195. *See, e.g., Crowdfund Investing—A Solution to the Capital Crisis Facing our Nation's Entrepreneurs: Hearing Before the Subcomm. on TARP, Fin. Servs. and Bailouts of Pub. & Private Programs of the H. Comm. on Oversight*, 112th Cong. (2011) (statement of Sherwood Neiss, Entrepreneur, The Startup Exemption) (advocating for, among other things, a hard limit of \$10,000 per year for any investor in crowdfunding efforts regardless of income).

196. A self-regulatory organization (SRO) is responsible under § 6 of the Exchange Act for maintaining industry standards and sharing some of the burden of enforcing compliance with rules; FINRA has been the SRO of choice for the SEC since the 1930s. *See Tanya Prive, Inside the JOBS Act: Equity Crowdfunding*, FORBES (Nov. 6, 2012, 11:57 AM), <http://www.forbes.com/sites/tanyaprive/2012/11/06/inside-the-jobs-act-equity-crowdfunding-2>.

197. *See Robb Mandelbaum, 'Crowdfunding' Rules Are Unlikely to Meet Deadline*, N.Y. TIMES, Dec. 27, 2012, at B1 (noting how significantly the rule-making process will shape the law).

198. *Id.*

199. *See id.*

200. Memorandum from SEC Div. of Risk, Strategy, & Fin. Innovation & Office of Gen. Counsel to the Staff of the Rulewriting Divs. & Offices 3 (Mar. 16, 2012) [hereinafter SEC Memorandum], available at http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.

tion, and capital formation.”²⁰¹ When dealing with a tool as potentially potent as equity crowdfunding, these considerations cannot be taken lightly, especially with regard to regulations that attempt to accurately forecast the risks of allowing volatile small businesses to collect capital from unsophisticated investors.²⁰² And comparing the future of a market under a rules regime to the “baseline . . . economic attributes of the relevant market and existing regulatory structure” will be extremely difficult in this case because the baseline is an economy completely without equity crowdfunding and without any regulation that is specific to the crowdfunding movement.²⁰³

The rulemaking process must also identify and consider any potential “reasonable alternatives” to the proposed regime.²⁰⁴ While it is not likely that this will result in changes to the few explicit provisions of the JOBS Act related to crowdfunding,²⁰⁵ it does signal that the SEC has some degree of latitude in concluding exactly how the aims of the JOBS Act should be accomplished.²⁰⁶ Some of the key pieces of the legislation are unlikely to change, such as the limits on amounts of equity that individuals can acquire through crowdfunding in a single year and the income scale on which that metric is based (mentioned earlier in this Note).²⁰⁷ The overall caps on how much each project can raise per year are also unlikely to change (also mentioned earlier).²⁰⁸

An important directive that could end up changing, if not through SEC rulemaking then through later legislative action, is the limit on transferability.²⁰⁹ Securities that are issued through crowdfunding portals under the JOBS Act cannot be transferred for a year after acquisition to anyone except back to the original issuer, to an accredited investor, family, or through a registered offering.²¹⁰ It is hard to imagine though, especially considering the inherently social nature of crowdfunding networks and the liquidity problems already associated with venture capital, that trading or transferring interests acquired through portals will remain limited to longer-term

201. *Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 178 (D.C. Cir. 2010).

202. *See supra* Part I.D.

203. SEC Memorandum, *supra* note 200, at 7.

204. *Chamber of Commerce v. SEC*, 412 F.3d 133, 144 (D.C. Cir. 2005).

205. *See supra* Part I.D.

206. As long as the SEC provides thorough, though not necessarily empirically supported, justifications for their rule proposals and adheres to the larger notice and comment process, it has a great deal of influence over the final content of rules. *Chamber of Commerce*, 412 F.3d at 142-43. For a more detailed look at the ways in which SEC rulemaking authority has been affected by recent court decisions and evolving interpretation of the Administrative Procedure Act, see James D. Cox & Benjamin J.C. Baucom, *The Emperor Has No Clothes: Confronting the D.C. Circuit's Usurpation of SEC Rulemaking Authority*, 90 TEX. L. REV. 1811, 1824 (2012).

207. *See supra* Part I.D.

208. *See id.*

209. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, § 302(b), 126 Stat. 306 (2012).

210. *Id.*

equity holdings.²¹¹

The question of how exactly the states will receive crowdfunding portals is also not entirely answered in the JOBS Act itself.²¹² The law does allow states to impose filing fees on portals that issue equity and enforce laws concerning fraud (Blue Sky Laws), but limits the ability of states to enforce security registration and offering laws against funding portals.²¹³ By allowing states to impose filing fees but not giving any guidelines, the JOBS Act could prompt a race to the bottom that sees certain states become destinations for crowdfunding portals looking to open up shop.²¹⁴

Most important among the various provisions of the JOBS Act though, are those that relate to investor protection.²¹⁵ Beyond the disclosure requirements and the requirement that crowdfunding platforms register with the SEC as either a broker or a “funding portal,” each individual investor must be vetted before they can invest in any crowdfunded offerings.²¹⁶ Individuals must demonstrate an understanding of the risk of loss and must also demonstrate that they are aware of the heightened risk involved in investing in startup businesses.²¹⁷ It is unclear if this will require some form of simple clickwrap term sheet that investors can simply read and approve, or come closer to a form of quiz that tests financial understanding.²¹⁸ If the latter is implemented, then the SEC rules will be very important in dictating exactly how much risk comprehension is expected of prospective crowdfund investors.²¹⁹

Pricing disclosure is another important component in investor protection that will have to be addressed during the rulemaking process.²²⁰ Because the investors that will have access to crowdfunding portals will be “unsophisticated” for the most part, there is a tremendous amount of room for questionable share pricing to go unnoticed.²²¹ And because the cap for each project is effectively \$500,000 (the point at which fuller disclosure akin to full SEC registration kicks in), prosecuting disputed pricing practices might be too trifling for the SEC to pursue and too unprofitable for class action lawyers.²²²

211. See *Crowdfunding: Is Your Investment Protected?*, *supra* note 119. For a brief note about capital lock-in in traditional venture capital, see *supra* note 170.

212. Importantly, the JOBS Act exempts crowdfunded offerings from state securities registration as “covered securities” under § 18(b)(4) of the ’33 Act. See § 302(b), 126 Stat. 306; see also Stuart R. Cohn, *The New Crowdfunding Registration Exemption: Good Idea, Bad Execution*, 64 FLA. L. REV. 1433, 1443–44 (2012).

213. § 305, 126 Stat. 306.

214. See *id.*

215. See *id.* § 302.

216. *Id.*

217. *Id.*

218. See *id.*

219. See *id.*

220. See Alan R. Palmiter, *Pricing Disclosure: Crowdfunding’s Curious Conundrum*, 7 OHIO ST. ENTREPRENEURIAL BUS. L.J. 373, 374 (2012) (discussing in depth the importance of pricing disclosure and the potential for fraud inherent in equity crowdfunding).

221. See *id.* at 375.

222. See *id.*

B. The Extra-Regulatory Limits of Crowdfunding, and the Future of Crowdfunding in the United States

These clear concerns about investor protection, and the experiences of equity crowdfunding portals elsewhere in the world, raise questions about whether everyday individuals are really ready to act as venture capitalists. The first round of funding for any project is usually not the last,²²³ and while individual investors represent enormous amounts of capital,²²⁴ they operate within a larger system that might have a difficult time accommodating them. “Unsophisticated” individuals who are acquiring equity in growing companies are likely unaware of the fact that their ownership stake in a successful company can, and probably will, be quickly diluted during successive fundraising rounds. What was once 2% ownership with limited voting rights in a burgeoning biotechnology company can quickly become a fraction of that without voting rights at all; partly because this is the way that venture capital works, but also because of the immense sophistication gap between established venture capitalists and at-home investors. It remains to be seen what sorts of contractual provisions become the norm in equity offerings through crowdfunding portals, but they will very likely be geared towards the best interests of the startup businesses and venture capitalists they will hope to attract, not the multitudes of seed-round investors.

From the crowdfund offeror’s perspective, this disconnect between their initial crowd of investors and the greater world of venture capital can also cause problems. Having “too many hands in the pot” so early in a company’s life can create myriad problems when looking for new investments.²²⁵ Raising subsequent funding rounds during which hundreds or thousands of existing equity holders have to be contacted would create

223. Normally, startup financing is accomplished over several rounds, from seed stage to Series A, B, C, and so forth depending on how long a project survives. Lately, though, a so-called “Series A crunch” has begun to emerge as a glut of seed financing and has met stagnating availability of next-step funding. This crunch is projected to leave many startups scrambling for funds and many current seed-stage investors without anything to show for their early faith. See *Seed Investing Report - Startup Orphans and the Series A Crunch*, CB INSIGHTS (Dec. 19, 2012), <http://www.cbinsights.com/blog/trends/seed-investing-report>. The question remains whether crowdfunding can help to solve this problem by providing a new source for second-stage funding, or if crowdfunding will simply further the growth of available seed-stage funding and subject members of the general public to the Series A crunch. See Ryan Caldbeck, *Crowdfunding Won’t Solve the Venture Capital Series A Crunch*, FORBES (Jan. 23, 2013, 12:39 AM), <http://www.forbes.com/sites/ryancaldbeck/2013/01/23/crowdfunding-wont-solve-the-venture-capital-series-a-crunch> (predicting that crowdfund investors would be at a major risk in picking up the Series A rounds that are currently being vetted and left behind by experienced venture capitalists).

224. J.J. Colao, *Fred Wilson and the Death of Venture Capital*, FORBES (May 8, 2012, 12:47 PM), <http://www.forbes.com/sites/jjcolao/2012/05/08/fred-wilson-and-the-death-of-venture-capital> (“[I]f U.S. families devote just 1% of their assets to investing in startups via crowdfunding, that would unleash a torrent of \$300 billion annually.”).

225. See Kathryn Hough, *New York Legal Experts Warn Against Dangers of Crowdfunding for Startups*, TECHLI (June 24, 2012), <http://techli.com/2012/06/crowdfunding-for-startups>.

aggravation and a degree of legwork that growing companies can ill afford and might also stand to make them less attractive to potential investors.²²⁶

Which sorts of projects will ultimately be attractive to investors and form the basis of the equity crowdfunding movement in the United States is yet to be seen. Particularly in these types of investments though, individual investors tend to prefer projects with well-thought-out business plans and transparent, understandable risk.²²⁷ Experienced and thoughtfully composed boards of directors are also important factors in determining which crowdfunding projects will be successful and attract attention.²²⁸ Ultimately though, the size and shape of equity crowdfunding in the United States will be determined by the crowd. While the SEC and FINRA might shape the crowdfunding movement by being more permissive of smaller funding rounds, or favoring certain forms of disclosure or investor education, in a marketplace with unprecedented social oversight the most important market constructors might just be the end users themselves—and that is the idea.

226. *See id.*

227. Gerrit K.C. Ahlers et al., *Signaling in Equity Crowdfunding* 3 (York Univ., Working Paper No. 21, 2012), available at <http://ssrn.com/abstract=2161587> (utilizing signaling theory to assess how investors act when faced with equity opportunities through crowd portals).

228. *Id.*

