Legal problems of crowdfunding.
Crowdfunding and Competition Law in the United Kingdom

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«I shall be telling this with a sigh
Somewhere ages and ages hence:
Two roads diverged in a wood, and I—
I took the one less traveled by,
And that has made all the difference. »

The Road Not Taken
Robert Frost
Abstract

Crowdfunding introduced a new digital age in the financial market and has become an important online financial alternative, in which promoters have the possibility to raise money for their projects, through the use of appropriate technologies (online platforms). Crowdfunding has on its basis the concepts of share and collaboration and seems to improve competition, making the market more dynamic, ensuring a better match between supply and demand.

This new online financial alternative was an essential tool to support crowd in the post-crisis period, which started with the global economic crisis in 2008. At the time, across the world, people were dealing with liquidity problems, the level of indebtedness of people was too high and the access to funds was extremely difficult to get in the common markets.

The United Kingdom is a leader in the European market in this kind of funding and that is the reason why this work analyses the existing models and types of crowdfunding in this country.

This work involves a general study of competition law of the United Kingdom, in order to recognise the concerns of competition law in the market.

Competition law has the aim of ensuring the organization and efficient distribution of resources in the market by increasing economic efficiency.

In short, this work tries to assess if crowdfunding developed in the United Kingdom can pose some concern to competition law, through restrictive practices of competition.

Note the following: Crowdfunding in the United Kingdom refers to the research taken over during the Program Erasmus+ which took place in London, at Centre of Commercial Law Studies, Queen Mary University of London, between February 1st and April 4th 2019. Thus, according to the submitted schedule, available data reported until the year of 2017.

Key-words: Crowdfunding; United Kingdom; Competition Law; Restrictive Practices of Competition; Two-sided Markets; Ecosystem Products; Consumption Synergies; Network Effects; Asymmetric Prices; Single-homing; Multihoming; Bundling; Tying.
Resumo

O crowdfunding introduziu uma nova era digital no mercado financeiro e tornou-se uma importante alternativa financeira online, na qual os promotores têm a possibilidade de arrecadar dinheiro para seus projetos, através do uso de tecnologias apropriadas (plataformas on-line). Tendo por base os conceitos de partilha e colaboração, o crowdfunding parece melhorar a concorrência, dinamizando o mercado, garantindo uma melhor correspondência entre oferta e procura.

Esta alternativa financeira online foi uma ferramenta essencial para apoiar as “massas” no período pós-crise, iniciado com a crise econômica global no ano de 2008. Na época, verificou-se um problema generalizado de liquidez, o nível de endividamento das pessoas era muito alto, e o acesso a fundos era extremamente difícil de obter nos meios tradicionais.

O Reino Unido é líder no mercado europeu do financiamento colaborativo, motivo pelo qual este trabalho analisa os modelos e tipos de financiamento coletivo existentes neste país.

Realizou-se um estudo geral sobre o direito da concorrência no Reino Unido, a fim de reconhecer as preocupações do direito da concorrência no mercado.

O direito da concorrência tem como objetivo garantir a organização e a distribuição eficiente de recursos no mercado, aumentando a eficiência econômica.

Em síntese, este trabalho tenta avaliar se o financiamento coletivo desenvolvido no Reino Unido pode causar alguma preocupação à concorrência no mercado, por meio de práticas restritivas à concorrência.

Nota: Crowdfunding no Reino Unido se refere à pesquisa realizada durante o Programa Erasmus+, em Londres, no Centro de Estudos de Direito Comercial da Universidade Queen Mary de Londres, entre o dia 1 de fevereiro e 4 de abril de 2019. Os dados disponíveis relatados na tese reportam-se ao ano de 2017.

Palavras chave: Crowdfunding; Reino Unido; Direito da Concorrência; Práticas Restritivas à competição; Mercados Bilaterais; Ecossistema de Produtos; Sinergias de Consumo; Efeitos de Rede; Assimetrias de Preços; Single-homing; Multihoming; Bundling; Tying.
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List of abbreviations

B.C. - Before Christ.
CASS - Client Asset Sourcebook.
CAT - Competition Appeal Tribunal.
CC - Competition Commission.
CD/DVD - A digitally encoded recording on an optical disk that is smaller than a phonograph record; played back by a laser.
CDOs - Collateralised debt obligations.
CIS - Collective Investment Scheme.
CMA - Competition and Markets Authority.
CMVM - Portuguese Securities Market Commission.
COBS - FCA Handbook Conduct of Business Sourcebook.
ERRA - Enterprise and Regulatory Reform Act 2013.
ESMA - European and Securities Market Authority.
FCA - Financial Conduct Authority.
FCA PS14/4 - The FCA’s regulatory approach to crowdfunding over the internet, and the promotion of non-readily realisable securities by other media, Policy statement 14/4.
ISA’s - Individual Savings Accounts.
MiFID - Markets in Financial Instruments Directive.
OFT - Office of Fair Trading.
PSRs 2017’ - Payment Services Regulations 2017.
PSD2 - Second Payment Services Directive 2015/2366/EC.
P2P - Peer-to-Peer.
RAO - Regulated Activities Order.
SME - Small and medium-sized enterprises.
SPV - Special Purpose Vehicle.
TFEU - Functioning of the European Union.
UK - United Kingdom.
«There is nothing that man fears more than the touch of the unknown […] even in sleep, when he is far more unguarded, he can all too easily be disturbed by a touch. It is only in crowd that man can become free of his fear of being touched».

Elias Canetti

1. Crowd

1.1. Historical background

Along this work, one word assumes and will keep assuming relevant interest: Crowd. If we observe the meaning of the word crowd in the dictionary, we conclude that is defined as: «[…] an assembly of persons or things in close proximity or densely packed together and may suggest lack of order, loss of personal identity», 2 or «a large group of people in a public place», 3 or even «heterogeneous group of people reacting to the same stimulus in a similar manner». 4

What if crowd means more than that?

If we return to history with the purpose to observe a rich past of facts, events, we can ascertain where the first crowds were found, and how they branched out. As Gabriel Tarde mentioned: «crowd is the group of the past; after the family, it is the oldest of the social groups». 5

Looking at history, ancient Greece emerges as a primordial example, with regard to the first crowds. Athens in the fifth century B.C., presents itself as a democratic city, as a result, of the profound reform to its political basis by Cleisthenes, 6 which broke with all the existing paradigms at the time. According to Aristotle, the author of the Constitution of Athens, Cleisthenes was responsible for «returning the Politeia to the crowd (plíthos)». 7

The crowd which Aristotle refers to are the Athenian citizen: (i) men; (ii) majority age; (iii) children of Athenian father; (iv) subsequently, in the time of Pericles, sons also of Athenian mother. 8 These Athenian citizens enjoyed the right of freedom (equal rights of speech and vote

6 See topic 4.3.
in the Assembly – Isegoria), and the right of equality before the law (all persons are governed by the same laws without distinction or exclusion – Isonomy). This human gathering occurred in the public square, in the city centre, specifically at the Agora, subsequently, in view of the high attendance of the crowd, the assembly began to take place on the steps of the Dionisio theatre.

The assembly was sovereign, each athenian could be called to intervene to discuss a particular proposal. A direct democracy was effectively verified, with the athenian to vote by rising hands in the air, instead of what occurred in the past, in which the decisions were handed down by the elders and by the most powerful. It was also possible to be sorted to perform a certain role in a political body, reflecting the idea that every citizen had a duty to participate in public life, to worry and to take care of the business of the state.

Nevertheless, what underlies and causes each athenian to gather at the crowd? The answer is reached when we perceive that each citizen could see himself in the other, in the sense that, there is in each of them the conviction and the conscience that will or idea is shared at that moment with the others. What actually happens is that they mutually suggest themselves. As an integral part of the crowd, the citizen acquires, albeit unconsciously, the sense of social integration. This sense of belonging, ends up generating another feeling, that of equality, even though, restricted to the moment in which one is in crowds.

Another historical example, can be found in what is commonly called the «Tulip Crisis». In the mid-17th century, in the Netherlands, namely in the city of Amsterdam, occurred a cross-sectional phenomenon to all social classes, which had at its origin, a flower.

The passion triggered by the tulip exceeded unimaginable boundaries, they became popularized in such a way that it became an object of desire, for the rich and for the poor. This exacerbated demand has triggered up a price rise of this flower and impelled their consumption. This behaviour made possible the existence of the transaction of the tulip bulbs, which was no more than a simply sale of their "seed". This market aroused so much interest and mobilized so many transactions that tulip bulbs gave rise to property bonds, which have been traded on a market similar to the stock exchange. Bubble bursted at 1637, the tulip market was closed, the

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economic effects of the reversal of the speculative cycle were limited only to those directly involved.\textsuperscript{13}

However, one question remains, how was a tulip capable of mobilizing a crowd? The answer can be reached by a simple fact, the human being feels better in the middle of the crowd instead of being alone.\textsuperscript{14} The crowd is attractive and it is able to generate feelings that otherwise the individual would not be able to experience. Intrinsically the human being is a being full of fears, the fear of failing to achieve a certain objective, the fear of rejection (this self-limit accompanies man since the beginning). The crowd gives the inverse: in a mass, man feels safe, confident and allows certain behaviors that alone he would never have. This means, that, alone, the man would value this flower in a completely different way, as a perishable good, in which it is difficult to ensure the quality and rarity of the tulip bulb, whether the value they solicit for the purchase is proportional to the qualities they aim to ensure. In other words, a person alone is more sensible, thoughtful, judicious or zealous; in a group, these barriers descend and give way to more impulsive, imponderated and unreflected acts. Every citizen feels protected in the middle of the crowd; the fear does no longer exist.

In the crowd, the tulip bulb is something overvalued, it is idealized as something scarce, that should be bought in the immediate, since the opportunity of a big business might fade, «money and the luxury are not for all but are desired by all».\textsuperscript{15} This group of people is mutually suggestive without being aware of that. Sharing the same will concerning something, in this specific case, the tulip, has caused the demand for it to increase disproportionately and consequently its price to rise too. If the other has, I also want to have! If the other can buy, I can also buy! This social mirroring is a reflection, even if illusionary, of what the crowd provide: equality. Here we add an important note: the crowd is no longer linked to the concept of physical proximity. It is no longer a \textit{sine qua non} condition, that the multitude share the same physical space. The person-to-person communication capacity is no longer limited to a specific area, but it is capable of materializing, flowing beyond a confined space. It is this break in the concept of physical proximity that allows to call the crowd of camaleonic. Camaleonic in the sense of constantly adapting to society, without losing its essence, mobilizing a heterogeneous set of

\begin{thebibliography}{99}
\bibitem{14} Elias Canetti, “Crowds and Power”, cit., pp. 16-18.
\end{thebibliography}
people, that in certain moments share the same ideal or will. The cohesion factor is simple conviction or consciousness, that this will or this ideal is shared with others.

### 1.2. Crowds at present

It might be assumed that when we think in crowd, we can define it as a large group of people. Although crowds are more than that, it can aggregate many different persons, belonging to different social classes, of different religions, different genders, different cultures or different nationalities, basically is a multitude of bodies. Precisely by having this characteristic (aggregation of an independent individuals), we can verify their dynamics, consciousness and freedom.

By following this line of reasoning, we are able to observe their nature: crowd is a society reproduction, nutshell, is productive and is not static.\(^{16}\) That happens because crowds are made up a multiplicity of singularities, which are not completely free because they depend of external factors, such as, social environment. Consequently, we can say without a shadow of doubt, that each society has the crowd that they deserve, because it will be exactly the product of their circumstances.

It should however be clarified before forging ahead, the difference between *people* and crowd. People can be defined as a set of human beings who constitute a community by their characteristics, customs, and traditions and are integrated in a region or country, being represented as a unit. By the opposite side, crowds aggregate internal differences that cannot be mitigated. Their essence consists in joining a multiplicity of persons and by that capable to develop autonomously.

Another point also should however be clarified: power and force are distinct things.\(^{17}\) In other words, the sovereign power can try to limit the effects of the crowd, but this power is always bated by rules that will not allow it to overcome certain limits. This sovereign power won’t be able to root out a crowd. In its turn, crowd as in its essence is «constitutive of being»\(^{18}\) has the force and power to eliminate the sovereign power.

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Nowadays, reality presents itself to the citizen as extremely challenging, once we are at a time, when the pace of technological evolution is so fast and everything seems to be in a distance of a click.

Internet allows the access to everything: information, entertainment, culture, fun, as a consequence, the citizen disconnects in relation to the other. We live in such a technological era in which artificial intelligence gains more and more space in society. Money, in the way that we know it, might disappear in a close future and become just an algorithmic.

Does it still make sense to speak in crowds?

The idea of crowds made up for a multiplicity of individuals itself, as a force and power structure, leads us to the conclusion in a positive response.

The reasons to back up my arguments are the fact that the human being is a being of habit, carries in itself the historicity of his ancestors. The social environment in which we grow, the values and ideals that are transmitted to us from birth are a very strong brand that will follow us for a lifetime. Just remember the expression of the look of the other: the father, the mother, the teacher, that look of reproach, that look we still feel from society when we have behaviors that in their optics are less proper… As much as society changes, we always end up influencing each other.

This society will never cease to be made up of people and it is this element that gives it authenticity: the aggregating and influencing capacity that the other has in us. Crowd can be understood in several ways, however, we will focus on these two vectors: (i) that crowd gathering in a certain physical space in favour of a particular objective (example: demonstrations against a particular policy of a country) which is the most frequent; (ii) that crowd that is composed of a group of people, which though physically separated are mentally united.

But how is that possible? Once this group of people does not see each other, is not in touch, does not engage, does not hear each other, how can it be incorporated in a crowd?

The answer is mental cohesion.

It is enough to perceive, that there is someone besides them, who at that moment, shares the same opinion, will or ideal\(^9\). This power of influence, of suggestion, is grounded on the idea of protection, of security, that is transmitted to us by others. The physical presence of the other is no longer a necessary condition for an existence of a certain group.

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With technological evolution, everyone is in contact with everyone, and the concept of physical proximity is no longer required to form a crowd, since the internet enables its virtual side. This virtual crowd is no longer constrained by, for example, weather conditions (sun to increase it and rain to dissipate it\textsuperscript{20}). A mere computer, smartphone or tablet is all it takes. Explaining very simply, something that allows them to contact with the outside, without leaving the comfort of their home. The mobilization of the masses through technology is a consequence of digital transformation. Nowadays, there are very few barriers to signing an online contract, and the same template can be signed many times by a set of people. This arises an important question, why does this happen? Because they have the same will and conviction as the others that also signed the contract. That conviction is sufficient to give them the confidence and the necessary protection to do so. The technology has opened doors to make this social interaction easier, with greater reliability and efficiency.

Furthermore, this access to society through digital means allows anonymity. This anonymity gives them certain protection, a sense of invisibility, which is capable of to increase their force to do certain acts.

It is this sense of mobility in the digital platforms, that allows new economic forces to be developed on a global scale, such as, the collaborative economy.

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\textsuperscript{20} Gabriel Tarde, “A Opinião e a Multidão”, cit., pp. 19 – 34.
2. Crowdfunding in the United Kingdom

2.1. Historical background [Economic Part]

On August 9th, 2007 the BNP Paribas froze three of their funds, indicating to the markets that they have no way of valuing the complex assets inside them known as collateralised debt obligations (CDOs) or packages of subprime-loans. It was the first major bank to acknowledge the risk of exposure to subprime mortgage markets. This situation foresaw what was going to happen a year later in 2008, when economic crisis in the United States provoked by the collapse of the real estate market, started by the bankruptcy of Lehman Brothers and was able to provoke an economic crisis across the world.

In 2009 the world economy slowed down due to the effects of the financial and credit crisis with a strong decrease in business confidence and with the development of policies to extend its credit restrictions.

Banks’ financial problems and the European monetary policies, as Santos has posited «in a sequence of mass injections of liquidity (Quantitative Easing) and very low interest rates [...] several banks did not (re)distributed the credit to the companies, specially SME or families or even other banks [...] with foreclosure of interbank market, especially in credit institutions in countries with a serious risk on sovereign debt such as Greece, Ireland, Portugal, Italy, and Spain». The consequence of this behaviour was obvious: the effects of economic crisis increased.

At the time, across the world people were dealing with liquidity problems, the level of indebtedness of people was too high and the access to funds was extremely difficult to get.

Crisis means evolution, learning from mistakes made and being able to create a new mechanism, which allows us to reach a new result sufficiently capable of removing us of that situation.

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The development of Web 2.0 allowed the users to participate in the creation of the content in all aspects of operation and management of their own websites, transforming the capacity of sharing information, and interaction with other users through social media. This evolution in digital media allowed the creation of crowdfunding.

Crowdfunding introduced a new digital age in the financial market and has become an important online alternative finance channel, in which promoters have the possibility to raise money for their projects, through the use of appropriate technologies (online platforms), which enable the promotion of their project in order to induce investors’ interest (tripartite business).

Crowdfunding provides to consumers and investors a new model of business which can adapt according to their interest and it can be done with no complex process, noteworthy, that in the past years the reality has been changing and new models of crowdfunding have become more appealing.

2.2. Introductory remarks

Crowdfunding introduced a new digital age in the financial market (digital economy), whereby the United Kingdom ("UK" hereinafter) is a leader in the European market in this kind of funding.

The supervision and monitorization of crowdfunding is the responsibility of the Financial Conduct Authority ("FCA" hereinafter) and will be examined in accordance with this regulatory regime.

In the UK crowdfunding is described as «a way in which people, organizations and businesses, including business start-ups, can raise money through online portals (crowdfunding platforms) to finance or re-finance their activities», Financial Conduct Authority, 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 [1.4] ("FCA PS14V4" hereinafter).

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25 It is important to clarify that the financial regulation of crowdfunding frequently involves several other government bodies or agencies, however, needs to be mentioned that this article will only review the regulatory regime put in place by the FCA, as the FCA serves as the key regulator and supervisor of crowdfunding activity in the UK.
This technical revolution on the «online platforms are drivers of growth, innovation and competition which enable business and consumers to make the most of the opportunities provided by the digital economy», according to the House of Lords.\textsuperscript{26}

Evolution of crowdfunding along these years allowed us to classify it into different models and these models can be distinguished in for-profit or non-profit ventures, which will be discussed in more detail in the next topic.

Finally, one last note to mention the existence of the two different strategies of fundraising in crowdfunding that is important to refer: the possibility of All-or-Nothing or Keep-It-All.\textsuperscript{27}

\textit{All or Nothing} means that a successful project reaches its objectives and raises all the funds that are necessary to the project, in consequence, the project receives the amount raised. On the other hand, if it is an unsuccessful, campaign the amount raised will be refunded to their investors’.

\textit{Keep-It-All}, even when the final expected result has not been reached, the fundraisers receive all funds raised, even if the initial target is not reached.

\section*{2.3. Crowdfunding Businesses Models\textsuperscript{28}}

\subsection*{2.3.1. Non-Profit Ventures}

In this non-profit ventures\textsuperscript{29} of crowdfunding, there are two different models to be analysed, (a) the donation – based crowdfunding and (b) the reward – based crowdfunding, both to be considered in turn below:


\textsuperscript{27}Carmen Estevan de Quesada, “European Contract Law in the Digital Age. Crowdfunding in Europe.” cit., pp.110-111.

\textsuperscript{28}Note that this topic [Crowdfunding in the United Kingdom] refers to the research taken over during the Program Erasmus+ which took place in London, at Centre of Commercial Law Studies, Queen Mary University of London, between February 1st and April 4th 2019. Thus, according to submitted schedule, available data reported until the year of 2017.

(a) Donation-Based Crowdfunding

In this model\(^{30}\), the contributors donate money on behalf of certain campaign or make charitable deeds without any compensation or return. The contributors know, since the beginning of the campaign, that it is an investment without a non-financial return. Its success can be explained by the spirit of mutual aid, for philanthropy actions or civic motivations to use in humanitarian projects. In this specific case, crowdfunding has on its genesis opening the doors to a more solidarity-conscious society, which explains its success.

On the Internet, the UK contributors can find online platforms for charity campaigns on websites, such as, JustGiving; Virgin Money Giving or Wonderful. These online fundraising platforms have been considering the best online platforms for charities in 2019.\(^{31}\)

In the UK in 2017, the total amount raised was £41 million and represents an increase of 4% when compared to 2016 where £40 million were raised.\(^{32}\)

Table I

![Total UK Donation-based Crowdfunding Volume 2013-2017 (£millions)](chart.png)

Source: CCAF 2018

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(b) Reward – Based Crowdfunding

In this model, the contributors donate funds to the consumer and in return they, after a certain period - which is previously clarified in the project- will receive goods or services for the support granted to the project - becoming a non-financial reward.

Contributors do not expect a certain amount of money in return for their investment. Instead, they expect to receive credits in a movie, a CD/DVD, a t-shirt, for example.

It is important to clarify that the return of the contributors can change according to the offer established in a campaign. If the consumer establishes the same return for all, all the contributors will receive the same reward at the end of the project. Otherwise, if the return is flexible, the contributors will receive the return according to the amount of money invested in the project.

In this specific model, the investors may have an active role in the product development process. Through their experience, their know-how, the investors can keep an on-going relationship with the consumer. Carmen Quesada, has posited another type of reward called «the pre-purchase model». This is a non-financial compensation, and consists in having access to the product before making the product available to the general public with a special benefit, for example, at a discount in relation to the expected retail price or at an earlier date than to the usual customers.

The contributors can search the offers on the online platforms, such as Crowdfunder; or Bloom VC.

For instance, in 2015 the amount raised was £42 million, in 2016 the amount raised was £48 million, however, in 2017 the amount raised only represents £44 million, an 8% decrease from 2016.

These two types of reward- base crowdfunding had become very popular in the UK. However, the latest statistics have demonstrated they have been lowered for the first time. One of the reasons might be the different investors interest, and started investing in another model of crowdfunding more appealing to their investments.

The other reason might be the fact that online platforms started applying high commissions to the investors, discouraging their investment.

Table II

![Graph showing total UK reward-based crowdfunding in 2011-2017 (£millions)]

Source: CCAF 2018

2.3.2. Profit Ventures

This model of crowdfunding is profit driven, the investors are likely to see a profit from their investment, making this a very attractive venture. Investors have access to a lot of business opportunities, where they can invest their money, and to get a great return in exchange. Because it is such an attractive investment, it generates a high demand of investors. However, these financial ventures are not free from risk, as investors cannot disassociate the inherent risks of this particular investment, the reason why they are subjected to high levels of regulation as the FCA’s Policy Statement.

Profit ventures can be found in two different models: (a) loan – based crowdfunding and (b) investment- based crowdfunding, both to be considered in turn below:
(a) Loan-based Crowdfunding

In this model\textsuperscript{38}, the investors (‘the lender’) invest some amount of money in the promoters’ (‘the borrower’) campaign, in a specific project or business and in return, the investors’ (‘the lender’) receive an interest rate fixed at the moment of fundraising.

One of the reasons for the success of this model is the fact that the lender can lend a certain amount of money to the borrower with attractive interest rates, which is more than the lender usually could obtain in the common market. It is estimated that it continues to grow in the next years, according to the studies done.

This model of crowdfunding can be divided into four types,\textsuperscript{39} \textsuperscript{40} each one with a specific demand, for example:

\textbf{1 - P2P Consumer Lending}

The purpose of the borrower campaign is raising money for personal loans: home improvement, purchase of a new car or family purposes. These funds can be obtained through online platforms, when a small amount of money is usually lent to the borrower without any guarantees (unsecured loans).\textsuperscript{41}

Consumer lending has been increasing in the UK, since it is easier for the borrower to raise funds using crowdfunding platforms than getting a financial credit at the common market with high long-term interest rates. Most of the times, banks do not approve a loan as the level of indebtedness is too high for its approval.

On the internet, lenders or borrowers can find some online platforms for their purpose, such as: RateSetter - an entity responsible for three asset classes: consumer lending, business lending, and property lending, or Zopa for investors seeking loans to purchase a car, consolidate debt, among others.\textsuperscript{42}

Concerning the graph below, this type of consumer lending has increased significantly.

\textsuperscript{38} Carmen Estevan de Quesada, “European Contract Law in the Digital Age. Crowdfunding in Europe.”, cit, p.114.
\textsuperscript{39} Ana Brochado, “Snapshot da Indústria do Crowdfunding na Europa”, Caderno de Encargos de Valores Mobiliários, No. 59, 2018, pp. 41 -44.
\textsuperscript{40}In this sense, CCAF - Bryan Zhang, Tania Ziegler, Leyla Mammadova, [et. al.], “The 5th UK alternative Finance Industry Report November 2018”, cit., pp.32-40.
\textsuperscript{42} ORCA, “Best peer-to-peer lending platforms in the UK”, available at \url{https://www.orcamoney.com/best-peer-to-peer-lenders-uk/} access on 27-03-2019.
In 2015 the raised amount was £909 million, in 2016 was £1.169 billion and in 2017 was raised £1.403 billion, an annual increase of 20% since 2016.⁴³

**2 - P2P Business Lending**

The purpose of this type of crowdfunding is the borrower, through online platforms, raise the necessary funds for a business, which are almost SMEs. The interested lenders, using the online platform, lend a certain amount of money to a business borrower with or without guarantees (i.e. secured and unsecured debt-based). This type of crowdfunding seems to be very eye-catching to the lenders. One of the reasons that can be identified is (i) the fact that lenders loan funds to the borrower and in return, they may receive a high interest rate in the short-term, regarding the conventional market and (ii) the fact that the quality of businesses and overall success of the fundraised amount might increment trust in the lenders.

This specific type of peer-to-peer business can be found online, for example, on the following websites: RateSetter; Crowdstacker; Crowd2Fund.

Analysing this graph below, the number of lenders which decided to use alternative finance has grown exponentially. In 2014 the amount raised was £749million and in 2015 the amount raised was £881million. However, between 2015 and 2016 increased by 31% when the amount raised was £1.232billion and increased 96% in 2017 in total amount raised of £2.039billion.

Table IV

![Graph showing total UK P2P business lending from 2011 to 2017 (in millions)]

Source: CCAF 2018

3 - P2P Property Lending

In this type of loan, the lenders, through their investment, allow the borrower to raise money for their purpose, most frequently for residential development, valuing the property or commercial loans. On the lenders perspective it is a secured loan, because there is a mortgage in their favour. All the loans are secured over a residential or commercial property, which is registered at the land registry.

The registered mortgage provides a sense of security to the lender, in other words, if the borrower fails to repay, the platform can repossess and sell the property in order to redeem the loan.

Online platforms P2P property lending can be found in: Proplend\textsuperscript{45}; Wellesley &Co, Assetz Capital.

Regarding the year of 2016 and the year of 2017, this type of model of crowdfunding slightly increased around £71 million, contributing for the third largest volume and still representing an important segment of the alternative finance in the UK.\textsuperscript{46}

Table V

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{chart.png}
\caption{Total UK P2P Property Lending 2015-2017 (£millions)}
\end{figure}

Source: CCAF 2018

4 - Invoice Trading

Invoice trading is a mechanism which allows the companies to sell their invoices at a discount to a pool of investors, with the purpose to free up cash «in order to receive funds immediately rather than waiting for the invoices to be paid». \textsuperscript{47}


Basically, the company applies to the online invoice trading platform to become an approved member. Once approved, the company upload the invoice into the invoice trading platform to sell the invoice and, in return, the company receives the funds at short-term.

The benefits such as liquidity are easily achieved by the company and, at the same time, the investors are able to earn good returns since the investors will receive a fee correspondent to the money previously invested.\(^{48}\)

The most widely known online platforms of crowdfunding in the UK are MarketInvoice and SME Invoice Finance.

This graphic shows that the invoice trading between the years of 2011 and 2013 where less widely used. This kind of financial alternative was not considered as economically viable; however, it started reversing considerably taking into account the last year’s numbers.

Notwithstanding, this type of crowdfunding begins to emerge in 2014 when £270million were raised. Between 2016 and 2017 there was a significant increase of 74% - from £452million to £787million of volume in just one year.\(^{49}\)

This behaviour can be explained, by the fact that one of the main advantages of invoice trading is to be subjected to the auction processes, which means investors are bidding against each other to advance funds against the invoices. The competition between investors tends to ensure that the company gets a more competitive rate and becomes more appealing.

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(b) **Investment – Based Crowdfunding**

This model of crowdfunding is a financial alternative which allows the investors through online platforms to show interest and invest in certain small businesses, mainly in start-up companies, which, by definition, are not appealing to the angel’s investors.

On the promoters’ side, when the companies’ cash flow is not sufficiently stable in order to obtain financial support from the capital market, they have to consider other alternative financial sources.

Considering both views – investors and promoters- investment - based crowdfunding answers to the demand of both parties, this is, the advantage of getting financial support (promoters) and the value of the investment made (investors).

Investment- based crowdfunding platforms were the last model to be created in the alternative finance and «took off to UK in 2011 with the launch of CrowdCube», however, «Seedrs become the first crowdfunding platform to be regulated by the Financial Conduct Authority (FCA)».

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According to the 5th UK Alternative Finance Industry Report, «in 2017, approximately 68% of all alternative finance market volume, which stands for £4.2 billion in total, were raised by UK start-ups and SMEs across a combination of the various debt, equity and non-investment funding options offered by the alternative finance industry».  

Briefly, it may be concluded that «as equity crowdfunding gains traction in the UK, crowdfunding platforms are trying out different styles and models of investment».  

This specific model of crowdfunding is the one which offers the highest risk to the investors which is subject to high levels of regulation. The risks involved have made it necessary to develop policies in order to protect the investor. It is essential that the investors can be aware of all these risks to protect their investments. 

The investment-based crowdfunding models are varied and may be portrayed in six different types as follow: 

1 - Equity-Based Crowdfunding

This specific kind of investment can be used when the investors wish to diversify their portfolio and purchase the securities issued directly from the promoters. Investors buy the equity mostly in early stage firms, and in return receive a share (common or preferred shares) from the promoters in exchange for the investment. That way, they grant a certain amount of control of the company. 

Purchase of securities is increasing since it reveals a very attractive businesses model, with a great capacity of return. 

Investors’ aim is to achieve earnings that far outweigh the amount of money invested because they are always looking for ways to get a great return. That return can also include the comparative tax benefits, in exchange for this kind of investment - the investment is treated as taxable capital gains and these rates are lower than income tax, which means more gains.

In 2017 the purchase of equity was of £333million, a 22% increase from the past year, where £272million were raised.  

Table VII

![Total UK Equity-based Crowdfunding Volume 2011 to 2017 (£millions)](chart)

Source: CCAF 2018

2. Debt-Based Securities

If the investors have opted to choose the debt directly from the promoters, the relationship between the promoters and the investor would be different from the previous hypothesis. In case the investors choose to buy debt, it is important that they carry out a thorough analysis, to determine which debt can bring them more advantages and fewer investment risks. «Mini-bonds (type of debt security) are illiquid and can be high risk, as the failure rate of small businesses is high.»

In this particular model, when an investor has decided to purchase a bond, they can do it in two different ways: bond with a fixed rate or bond with a variable rate.


57 Financial Conduct Authority, “A review of the regulatory regime for crowdfunding and the promotion of non-readily realisable securities by other media”, 2015 p. 9 [61].
When an investor purchases a bond with a fixed rate, at the time of the purchase of this bond, it has (i) a fixed maturity date and (ii) fixed coupon, and these conditions will not change regardless of what happens to wider economy or interest rate.

When an investor purchases a bond with a variable rate, there are two options: (i) floating or variable interest rate, or (ii) coupon rate. The rate adjusts according to a predetermined formula outlined in the bond's prospectus or official statement at the purchase.

When the maturity time comes, the investors can receive the adjusted face value of the indexed bond and also the final coupon grounded on the adjusted face value. «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»\(^{58}\).

This specific type of investment generated interest from the investors only in 2016 when it raised £79 million and had a considerable increase of 1177% from 2015 to 2016. \(^{59}\)

However, it is necessary to consider that there is a small decrease of 9% from 2016 to 2017.

Table VIII

<table>
<thead>
<tr>
<th>Year</th>
<th>Total UK Debt-based Securities Volume (£millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>£21m</td>
</tr>
<tr>
<td>2013</td>
<td>£29m</td>
</tr>
<tr>
<td>2014</td>
<td>£16m</td>
</tr>
<tr>
<td>2015</td>
<td>£34m</td>
</tr>
<tr>
<td>2016</td>
<td>£77m</td>
</tr>
<tr>
<td>2017</td>
<td>£77m</td>
</tr>
</tbody>
</table>

Source: CCAF 2018

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\(^{58}\) Financial Conduct Authority, “A review of the regulatory regime for crowdfunding and the promotion of non-readily realisable securities by other media”, 2015 p. 9 [62].

3 - Securities not issued by the promoter

This situation happens, when the investors purchase securities, even though they are not issued by the promoter, but, instead, by a third party who holds stock, for example, a Special Purpose Vehicle (SPV) or a Collective Investment Scheme (CIS). That may be established by the existing contract on the platform. In this scenario, the investor does not have direct contact with the partner or project, the investor has an intermediary between him and the promoter company.

4 - Profit sharing crowdfunding

Another type of investment is completely different from the previous ones. In this particular case what the investors want is the right to participate in the profits, consequently, the securities are not involved. The investors can invest some amount in a certain project and in return of that investment, they receive a percentage of the profits which will be distributed proportionally.

5 - Community Shares

This type of investment of crowdfunding is appealing to specifically targeted investors which are the local population of a certain place, who is given the opportunity to invest by the online platforms in a community project. The community shares (in specific, the share capital) can only be issued by co-operative societies, community benefit societies and charitable community benefit societies. The shareholders have the right to withdraw their share capital, subject to the terms and conditions stated in the society’s rules and share offer document. However, they cannot sell or transfer their shares, or liquidate the business in order to achieve a capital gain.

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61 See, Ana Brochado, “Snapshot da Indústria do Crowdfunding na Europa”, cit., p. 41
The Community Shares Booster Programme is one of the online platforms where it is possible to support this community business.

This type of crowdfunding has not grown up from 2015 to 2017, where the campaigns suffered a 55% decrease from £44 million in 2016 and they raised funds in 2017 of £20 million.  

Table IX

![Graph showing Total UK Community Shares Volume 2012-2017 (£millions)](image)

Source: CCAF 2018

6 - Real Estate Crowdfunding

This is a type of investment which allows the direct access to the real estate market through crowdfunding to solicit investments from high-net-worth investors who are eager to make an investment in this kind of market. The investors get access to the real estate market with small amounts of money, so the effort rate it is not high and they get to work directly with real estate developers, have an opinion, making decisions in the process, and have the chance to choose in which real estate projects they want to invest their money.

Meanwhile, it is necessary to be aware of the problems that can appear in this type of investment, such as the movement of the market, if the market goes south, an investor will likely lose money if the market is at north; another problem is a lack of liquidity, as the absence

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of a secondary market restricts easy access to selling opportunities for investors or even, the risk of investment default.

Analysing the graph, we can observe the increase from 2016 when £71 million were raised and in 2017, when £211 million were raised, this represents a rising of 197%.\(^6\) Basically, this is the type of crowdfunding becoming more and more popular among the investors.

Table X

![Graph showing total UK real estate crowdfunding 2011-2017 (£millions)](image)

Source: CCAF 2018

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3. Online Platforms

3.1. Tripartite business

Nowadays, crowdfunding has become a legitimate alternative channel of raising finance for a project, business or to support some charity, through an online web-based platform. Crowdfunding likely appears as the perfect market solution for raising funds, however, it is important to understand how this process works.

Crowdfunding is a tripartite business given to the fact that it encompasses (i) a project owner, (ii) the platform which acts as intermediary and (iii) a investor who funds the project. Project owners (promoters) are the persons or companies who need to raise funds, in order to get finance for their project or business, for that, promoters have to promote their project or business through an online web-based platform, in order to induce investors’ interest.

Investors are the individuals with a will to invest in a new project or business and for that, contribute with a certain amount of money funding the project. Therefore, they expect to have a good return on investment, and these investors can be individuals or can also be legal persons.

At last, to consider is legal entities of online platforms, which have real control of the website. These online platforms can be considered as an effective vehicle to promote the exchange of interest, between promoters and investors’ wills. Thus, online platforms are an essential element due to the fact that they arise as a connection element which intermediates the interest of both parties, coordinating the whole process in exchange for a fee.

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3.2. General Rules of the Contract Platform

An online platform of crowdfunding is a web-based finance, which involves two or more sided of the markets, intermediating between those raising money and those seeking to invest. «The essential service/activity undertaken by crowdfunding platforms is to provide a mechanism for projects to find investors and investors to find projects [...] crowdfunding platforms have really emerged since internet technology evolved in such a way as to allow two-way communication, which enables interaction between the members of the ‘crowd’ of investors, as well as between the ‘crowd’ and the project owners pitching.»

Online platforms of crowdfunding are beginning to be considered a key driver of growth, not only from the perspective of the parties (alternative finance) but also for those who work directly in the platforms with creating employment. Before we move forward, it is relevant to clarify that non-profit ventures, such as donation-based crowdfunding and reward-based crowdfunding are not supervised by Financial Conduct Authority (FCA), due to the fact, that these models of crowdfunding are for altruistic purposes or to receive a reward. These models of crowdfunding are on the scope of the Second Payment Services Directive 2015/2366/EC (PSD2), as given effect to in the Payment Services Regulations 2017 (the ‘PSRs 2017’).

On the opposite side, in order to keep ensuring the protection of investors, online platforms of profit-ventures, such as loan-based crowdfunding and investment-based crowdfunding are within an appropriate regulatory/supervisory framework in order to increase confidence of the user. The supervisory authority regulated the conditions that need to be fulfilled by the entities of platforms [operators of electronic systems] in order to obtain the necessary license for this activity. This supervisory authority also established the conduct of business rules, the warnings that should be done to investors considering the risk of investment, as explain below.

National rules were created and enacted on 1 April 2014: FCA’s Policy Statement14/4, Crowdfunding and the Promotion of Non-Readily Realisable Securities Instrument 2014 (“FCA PS14/4” hereinafter). For instance, in this regulation, the supervisory authority directed its

attention to protect the investor from the risk of the platform entity becoming insolvent, «a firm must all times be able to meet its liabilities as they fall due.»

In that sense, FCA PS14/4 required that all entities of platforms have a minimum capital requirement of £50,000.00, and others requirements as protecting the agreements settled and which an operator of a platform must comply with.

Furthermore, the FCA Handbook Conduct of Business Sourcebook (COBS “hereinafter”) - Chapter 2 Conduct of Business Obligations COBS 2 - lay down the rules of professional conduct and idoneity in taking decisions, saying that «A firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule), [...] In relation to its eligible counterparty business, a firm must act honestly, fairly and professionally, taking into account the nature of the eligible counterparty and its business.»

An entity of platform should provide all the necessary information considering nature and risks of a certain business (expected and actual default rates; details of creditworthiness assessment; a fair explanation of the likely return considering fees, rates ad tax’s).

However, these are not the only obligations that entities of platforms need to follow; they are also obliged to conform to Client Money Rules [Client Assets Sourcebook (Amendment) Instrument 2016], as outlined in the FCA Handbook in the section relating to their Client Asset Sourcebook rules (or CASS “hereinafter”).

The Peer-to-Peer Lending Instrument 2016 came into force on 6 April 2016 and this instrument has the purpose to «reflect the introduction of the IFISA, and the fact that providing advice on investing in P2P agreements will be a regulated activity» with the aim of both loan and investment-based crowdfunding (under Article 36H agreements in the Regulated Activities Order (RAO) to be included in Individual Savings Accounts (ISA’s).

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75 Financial Conduct Authority (FCA) (2016b), FCA Handbook, cit., COBS. 2.1.1A.
An important note is the fact that FCA warned investors that these kinds of investments on crowdfunding (loan or investment) do not constitute a deposit, therefore, they are not covered by the guarantee funds deposit, consequently, investors won’t have access to the Financial Services Compensation Scheme.

Another relevant regulatory matter is the amount that can be invested. While in some jurisdictions there are no limits, some others, such as Portugal or the UK, established certain criteria.

FCA PS14/4 and COBS regulated, in the sense, to limit the amount that can be invested to differentiate investors.

Platforms entities, can only accept investments from (i) certified high net worth investor or (ii) a certified sophisticated investor or (iii) self-certified sophisticated investor, which «is an individual who has signed, within the period of 12 months ending with the day on which the communication is made, a statement in the terms set out in the applicable rule listed below, substituting “non-readily realisable securities” for “non-mainstream pooled investments.”»

In this situation, these investors have no limit for their investments because they are understood as professional investors, having a lot of experience in the trade market, with an awareness of the risks that these types of investments entail.

However, a (iv) restricted investor «is an individual who has signed, within the period of 12 months ending with the day on which the communication is made» received investment recommendations, (b) declared in the 12 months preceding the date of the statement, he had not invested more than 10 per cent of their net assets in non-readily realisable securities, (c) declared that in the 12 months following the date of the statement he must not invest more than 10 per cent of their net assets in non-readily realisable securities, among others. This limit can be explained given to the fact, that a restricted investor has no experience in the trade market, that is not so well prepared, that cannot be aware of the risks of the investments and its consequences, being exposed to a significant risk of losing all money.

It is noteworthy to mention that while professional investors are not limited, a restricted investor is. If the genesis of the crowdfunding is the crowd, will this limitation not overthrow the original concept?

It is a difficult question to answer because it is not so simple as it might seem.

80 Financial Conduct Authority (FCA) (2014), cit., p.17 [4.7.9].
81 Financial Conduct Authority (FCA) (2014), cit., p.17 [4.7.9].
On the one hand, given to the fact that crowdfunding is a mechanism available for the crowd, to solve some liquidity problems that otherwise have no solution, this limit for investment will probably make no sense. This alternative finance channel had its origin in an attempt to support promoters which had no means to raise funds, due to the fact the banks denied the credit - it allows the growth of start-ups by means of alternative investment, it gives the opportunity for development of project or business, that by its nature is unable to finance itself in the common markets.

On the other hand, if we look to history, we note that people invested their money without consciousness of the inherent risks, sometimes people do not have the necessary economic concepts capable of helping them in their decision taking. Economic crisis in the United States provoked by the collapse of the real estate market in 2008 is proof of that (people have taken out two or three different loans, at the same time, with variable rates and with a level of indebtedness considered too high).

This limit can be acceptable: it is to protect investors with no practice in the trade market in order to safeguard their money, to reduce a significant risk of losing their funds, even when this may eventually collide with the principle of economic freedom.

In the European Union, European and Securities Market Authority (“ESMA” hereinafter), has a relevant role in harmonizing and supervising practices, assuring consistent approaches and common procedures in all countries of European Union (Regulation EU 1095/2010, art.29).


On 4 June 2019 in the UK came into force the FCA Mortgages and Home Finance (Peer to Peer) Instrument 2019.

An important final note to be mentioned, FCA Loan- based (‘peer-to-peer’) and investment-based crowdfunding platforms, feedback CP18/20 and final rules, PS19/14 will come into force on 9 December 2019.

These new rules will affect ‘peer-to-peer’ (P2P “hereinafter”) platforms; IB platforms; trade bodies for these sectors; consumers and business investing or those considering investing in
this type of crowdfunding; intermediaries who might refer home finance customers to P2P platforms and consumer organisations.

The main changes are: (i) clarifying the requirements for controlling platforms especially on credit risk assessment, risk management, and fair valuation practices; (ii) strengthening rules on plans for the wind-down of P2P; (iii) applying marketing restrictions to P2P, in particular to new or less-experienced investors; (iv) minimum of information that P2P need to give to investors; (v) a new requirement for a more assertive assessment to be undertaken.

«In a world of perfect competition, life is good».
Einer Elhange, Damien Geradin

4. Economics and Competition Law
4.1 Economic goals

Looking at economics from the perspective of price formation study and discussing market functionality with the aim of ensuring the organization and efficient distribution of resources in the market are more important than ever. These factors have become especially necessary, at a time when there is a lot of information and limited time to process it. Economic efficiency of resources (allocative efficiency) determines that any production is achieved with the minimum cost, i.e. there is no waste and appropriate prices of inputs are used. Connected to that, Pareto defined the increase in total welfare as what occurs in the conditions in which consumers improve as a result of the exchange without anyone getting worse. In this sense, for Pareto the trade would take place in a competitive market between economical agents, where the ratio of marginal utilities of the marketed goods equalized the ratio of their prices.

For the economy, competition is good. Competition allows innovation, the increase of the quality of the product or service, permits the pursuit of excellence, in a way that the result is verified through better products, lower prices, with a wider choice to the consumer, thus achieving a dynamic efficiency.

To achieve this ideal of competition the neo-classical economic theory has developed a model of perfect competition, which gave a real meaning to the social welfare concept. Through the sophisticated model\(^{85}\) of perfect competition, a more efficient allocation of resources would be achieved. The idea of perfect competition itself, as a market structure, is very difficult to implement, as there are certain criteria that need to be fulfilled, such as homogeneous products, the number of sellers and buyers must be large, full information concerning the market conditions must be available to all parties involved, and free entry or exit of the market\(^{86}\). The difficulty in aggregating all these criteria makes this theory of perfect competition difficult to apply to markets. In fact, the existence of a market with all these characteristics and with no price oscillations by the producer seems to be only an ideal.\(^{87}\)

On the other hand, the free market can lead to monopoly situations, which despite being rare, have an extraordinary power to control the market. Monopoly situations do not benefit the welfare of the consumer, in reality they create a significative impact to competition since their goal is their own strengthening. To achieve that result certain acts can be done in the market resulting from practising of high prices, whether it is reducing production or creating barriers that prevent other competitors from entering the market.

Unlike monopoly situations that are unusual, economic behaviour has been showing us a new reality - the existence of firms with a dominant position in the market. The abuse of a dominant position by a firm or set of firms is a restrictive practice of competition, which arises from the unlawful use by a firm of the power it has in a certain market. The abuse of dominant position happens when a firm carries out behaviours that are likely to influence the structure of a market. As a result, the degree of competition is low, as explained in more detail later.

The above-mentioned situations are the proof that these commercial behaviours generate an inferior position of consumer welfare. The consequence is obvious - inefficient allocation of resources.


In this sense, in order to safeguard competition and avoid abusive practices that disrupt the market, competition law intervenes.

As a conclusion, the aim of competition law is to protect the welfare of consumers, ensuring free and fair competition by increasing economic efficiency. Competition law has the essential tools to be able to act when necessary, sanctioning harmful practices that are occurring on the market, eliminating inequalities and restoring the equilibrium in order to assure good commercial practices.

### 4.2. Competition Law: main concerns

Competition law aim is to safeguard the welfare of the consumer and increase economic efficiency.

In the light of the above, in order to pursue these objectives, two major changes were made in the competition law of the UK: the Competition Act 1998 and the Enterprise Act 2002. Later, with the legislative amendment of the Enterprise and Regulatory Reform Act 2013 ("ERRA"), entered into force on April 1st 2014, the Competition and Markets Authority ("CMA") replaced the previous authorities: Office of Fair Trading ("OFT") and the Competition Commission ("CC"). Further, the Consumer Rights Act 2015 has extended the scope of jurisdiction of the Competition Appeal Tribunal ("CAT"), granted more powers to this court, allowing it to have an effective control over the processes related to the competition law.

Thus, the objectives of the CMA are intertwined with the objectives of the competition law, that is to say, guarantee the regular functioning of the market, in order to protect the commercial and economic interests of all economic agents, as well as the welfare of the consumer, both within and outside the UK.88

Observing market behaviour, some facts can be identified as restrictive acts of competition89 such as the anti-competitive agreements between companies.

In this sense, Chapter I of Competition Act 1998 (“CA”) applies to «agreements between undertakings, decisions by associations of undertakings and concerted practices which, may affect trade within the United Kingdom, and have as their object or effect the prevention,

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restriction or distortion of competition within the United Kingdom, are prohibited unless they are exempt in accordance with of this Part.»

A similar rule is also found under Article 101 of Treaty on the Functioning of the European Union ("TFEU"), which establishes as prohibited, the «agreements between undertakings, decisions by associations of undertakings and concerted practices, which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market.»

These agreements between companies, can significantly change the structure of the market. Nevertheless, this does not mean that all agreements are prohibited. Sometimes, a certain agreement does not distort competition, therefore posing no danger itself to the market - in this specific situation it makes no sense to prohibit it - or, for instance, the agreement satisfies the exemptions provided for in the Chapter 1 (9) CA or in 101 (3) of the TFEU.

On the opposite side, there are agreements between undertakings whose objective is to adopt collusive behaviour in order to control effective competition in the market. These collusive behaviours are achieved by these anti-competitive agreements, which have as their object or effect, the control of competition by an increase in prices, reducing sales volume and decrease in quality of products or services. In these cases, competition is significantly affected and by consequence proves to be detrimental to the consumer's well-being.

In this field, we can find two types of anti-competitive agreements, which can be horizontal or vertical.

Horizontal agreements arise in competition law as those that are most restrictive of competition that produce the greatest anti-competitive effects and by that, are the most harmful.

We will not cover all possible horizontal agreements (cartel or cooperation agreement), taking into consideration the fact, that they are not relevant for the analysis of the theme we intend to develop. However, we cannot proceed without briefly analysing one of the types of horizontal agreements that most concerns arise for competition authorities - cartels.

For Whish and Bailey market cartelisation can be explained as an agreement and/or concerted practice between actual or potential competing undertakings with the aim of restricting competition and achieving more effective control in the respective market, developed to limit

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or eliminate competition between them, with the purpose of increasing prices and profits of the participating companies. This agreement may be done in various ways and found on the market as price standardization, production quotas, market sharing, exchanges of information, etc. These agreements contain very significant restrictions in terms of their impact on competition, in reality, this collusive behaviour ends up subverting the law of supply and demand. With this manipulation in the process of competition, consumers are likely to be harmed. This is one of the reasons why a cartel is considered, in several jurisdictions, as an anti-competitive practice extremely detrimental to the market and to the consumers. This collusive behaviour between firms is very difficult to prove, since the parties are aware of their harmful behaviour and therefore try to adopt strategies in order to hide it as much as possible. In this sense, the effort to root out the cartel is not only an internal battle of the UK competition authorities (CMA), but also a battle of the European Commission. Cartel agreements are not likely to be legitimate when its practice aims to improve the structure of the market, i.e., exempted under article 9 CA and under article 101 (3) of TFEU.

The other type of anti-competitive agreement is a vertical agreement, which is, by its nature, very different from horizontal agreements. In this sense, «vertical agreement means an agreement or concerted practice entered into between two or more undertakings each of which operates, for the purposes of the agreement or the concerted practice, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services.» This type of agreements creates fewer competition concerns than horizontal agreements. Nevertheless, they can also produce a negative impact to competition, when they have contractual restraints with the purpose to adopt anti-competitive behaviour (foreclosing market access to actual or potential competitors, for instance, by increasing their costs or prejudicing their capacity to compete normally).

These anti-competitive agreements, for these authors referred above, whether horizontal or vertical, have strong potential to restrict competition, generating harm to consumers. These harmful commercial practices are not exhausted by the anti-competitive agreements in the market; it is possible to discover other unlawful practices, for example, the abuse of a dominant position by a certain firm or a set of firms.

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The abuse of a dominant position\(^95\) by a firm is a restrictive practice of competition, when the firm makes unlawful use of the power it holds in the market, carrying out behaviours that influence its structure\(^96\).

The abuse of a dominant position can manifest in two distinct ways. It can manifest\(^97\) itself through exploitative abuses, such as excessive prices, unequal contractual conditions to the parties, or through exclusionary abuses, for example when they have the purpose of removing other competitors from the market, with the refusal of supply and with the use of predatory prices. The Chapter II of CA determines when any conduct on the part of one or more firms configures an abuse of dominant position and similar rule is also found under Article 102 of TFEU.

It is important to mention, that concentrations arise when two or more unrelated undertakings merge; when occurs the acquisition by one undertaking of all, or a majority of the shares of another undertaking, or when a joint venture is created and enjoys operational autonomy.

For Whish and Bailey, concentrations (“mergers” hereinafter) are based on a perspective of economic growth and it is necessary to evaluate the impact of a merger on competition, to assess whether, as a result of the merger, it can significantly affect competition.\(^98\)

In this sense, it becomes necessary to analyse and assess the possible anti-competitive effects that a merger can generate in the market considering, \textit{a priori}, that the merger can occur in three distinct types.

The first type, horizontal merger\(^99\), arises in situations where, in the same relevant market, direct competitors and with similar products merge. The objectives of this new merged firm, among others, is to increase revenue and achieve a more efficient economic scale. However, it is important to clarify that, in certain situations, a horizontal merger can significantly impede competition, causing an adverse effect, inducing a substantial competitive concern, as it will be explained below.


The second type, vertical merger\textsuperscript{100}, arises between firms that are along the same supply chain and with the same end product. In other words, it is the merger that occurs with firms that are not competing with each other in which, most of the time, there is already a previous business relationship (producer → distributor, for example). The reasons that justify this merger are increasing efficiency and reducing costs. These objectives can be achieved through the guarantee of access to raw material; the elimination of a separate distributor/supplier demand process, and consequently the elimination of the associated costs (such as: to select one to distribute among the various on the market, the inherent negotiations, the conclusion of the respective distribution contract); reduction of the product placement time on the market, among others. This type of vertical mergers, most of the time, do not raise competitive concerns and are likely procompetitive.

The third type, conglomerate merger\textsuperscript{101}, is the merger between firms that operate in different industries, this means the merging firms have no overlapping business areas. An advantage of a conglomerate merger can be, for example, to ensure dominance of the market with an expanded share and to reduce its business risk (diversifying its business operations; gaining cross-selling products, etc).

The latter two types of mergers are not likely to represent a concern for the competition authority as horizontal mergers, most of the time, these non-horizontal mergers induce efficiencies\textsuperscript{102} (increasing pricing efficiency; increasing productive efficiency; prevent profit expropriation and reduce transactions cost)\textsuperscript{103}. However, it is important to mention, sometimes, they may also affect competition when an adverse effect is verified.

Diagonal merger is a merger involving a combination of two companies or more, which are in a vertical or conglomerate relationship, and also direct competitors (current or potential).\textsuperscript{104} The diagonal merger may involve both horizontal and non-horizontal effects.

Generally speaking, we can conclude that mergers are important for the economy to increase efficiency and make the market more dynamic. It is a wrong premise to start from the idea that all mergers generate anticompetitive effects in the market; in fact, most of them are harmless.

\textsuperscript{100} Ioannis Kokkoris, Howard Shelanski, “EU Merger Control – An Legal and Economic Analysis”, cit., pp. 337-379.
\textsuperscript{102} “Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings.”, OJ, C265, 2008.
\textsuperscript{103} Ioannis Kokkoris, Howard Shelanski, “EU Merger Control – An Legal and Economic Analysis”, cit., [9.3 – 9.5].
\textsuperscript{104} Ioannis Kokkoris, Howard Shelanski, “EU Merger Control – An Legal and Economic Analysis”, cit, [7.5].
In small markets where economies are still under development, mergers can be helpful to the economy, in order for the companies to compete more efficiently.

However, some mergers can produce an adverse effect and when that happens, it can strongly restrict competition. To avoid that, competition authority needs to predict, assessing all market conditions, if a certain merger has the potential to impede competition.

Theories of harm can be used, as a tool to provide greater predictability, in a way to realize which impact a specific merger may have on the market. There are two main theories of harm in the assessment of mergers.

Unilateral effects or non-coordinated effects arise when, after a merger, the new merged firm increases their market power and by that, it is enabled to increase prices or reduce the innovation of products or services or decrease their quality. This unilateral conduct in the post-merger market causes a distortion in the process of competition, making it less competitive, consequently, harmful to the consumer.

Taking into account that this topic needed a more thorough and careful approach given the relevance and importance of the theme, the chapter will present briefly the factors that are taken into consideration in the assessment according to the EU Horizontal Merger Guidelines. The criteria that must be analysed are: (i) merging firms have large market shares; (ii) merging firms are close competitors; (iii) customers have limited possibilities of switching supplier; (iv) Competitors are unlikely to increase supply if prices increase; (v) merged entity able to hinder expansion by competitors; (vi) merger eliminates an important competitive force. These factors should not be considered as cumulative and these factors cannot be considered an exhaustive list.

Another theory of harm is Coordinated effects.

For Kokkoris and Shelanski\textsuperscript{105}, the coordinated effects arise when there is the possibility to change the nature of competition, allowing firms to coordinate their behaviour and increase prices, reduce the innovation of products or services or decrease their quality after a merger, and it happens in highly concentrated markets. In other words, the coordinated effects are verified when after a merger the other competitors are more likely to coordinate their behaviour than previously, being a strategy to exercise collective market power (depending on the market this coordination may involve raising prices or avoiding very low prices; controlling outputs; sharing the market, etc). To be able to claim that that a merger raises coordinated effects, three

requirements must be fulfilled: (1) the coordinating firms must be able to coordinate their behaviour; (2) if the parties deviate from this conduct, there are penalties; (3) there should be no impediments from other competitors, current or potential, as well as from customers who may undermine the objectives of coordination.

The vertical effects arise when a vertical merger can significantly affect competition in either or both of the input and the output market. The most common is foreclose access to the market to rivals, eliminating by that a potential entrant or encourage their exit from the market. This behaviour may entail, for example, the exclusive access by a firm in an upstream market, to an asset, whose substitute product does not yet exist or it is very difficult to reproduce, affecting the distribution process. Or, in a situation, which the merged entity is able to collude with other competitors, exercising the market power in order to control the inputs or outputs of the market. Finally, conglomerate effects are very difficult to verify in the market, considering the own nature of the merger. As Kokkoris has posited «Conglomerate mergers are mergers between firms in apparently unrelated markets which would rarely significantly impede effective competition». A merger leads to competition harm when the merged entity is able to diminish the willingness and ability of rivals to compete. One of the main concerns is the foreclosure of competitors. The merged firm may be able to leverage its market power from one market to another, «by means of tying and bundling»107, (bundling «usually refers to the way products are offered and priced by the merged entity» and tying «usually refers to situations where customers that purchase one good (the tying good) are required to also purchase another good from the producer (the tied good)»108, thus forcing rivals to exit. Another criterion is the incentive to foreclose competitors. To assess the incentive to foreclosure of competitors can be a real concern is to observe and verify if through bundling or tying this strategy is profitable for the merged firm. The last criteria into account are the overall likely impact on prices and choice. Forcing tying and bundling may lead to a reduction in competitors’ capacity to compete and through this behavior (exit of the rivals) the merged firm acquires market power leading to a restriction of competition, and generating harm to consumers.109

In this field, the concerted practice would consist of a coalition with another competitor with the aim of eliminating competition on the market.

108 Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings, cit., [95,96,97].
109 Guidelines on the assessment of non-horizontal mergers” cit., [99,100,101].
All in all, mergers cannot be assumed *ab initio* as harmful to the market, with anticompetitive effects on it - it is necessary to make an assessment to ascertain whether the merger improves the welfare of consumers or has an adverse impact on competition.\(^\text{110}\)

Some authors consider that the public restrictions of competition, such as legislative measures, regulations, do not allow the normal functioning of competition,\(^\text{111}\) in fact, for these authors, the direct oversight by the competition authority over economic agents influence their actions and decisions.

However, the role of competition policy is extremely important to ensure effective competition on the market, not only fair competition and consumer welfare, but also to convey to the consumer the idea of protection.

As Audretsch has posited, «competition is favoured by economists and by the law because it forces firms to pursue efficiency, product improvement and vigorous innovation».\(^\text{112}\)

As explained above, there are too many factors that affect the market, which need to be avoided in order to achieve efficient production and consequent effective allocation of resources. In this line of reasoning, it is necessary to regulate the market, given that perfect competition is impossible to achieve.

### 4.3. Goals of Competition Law

One of the main objectives of the competition law is to protect the welfare of the consumer, who are usually the stakeholders in the most fragile position.

It is necessary to become clear that competition law seeks to protect consumers.

Competition policies were created to avoid inequalities. All are equal before the law (*isonomy*).\(^\text{113, 114}\)

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\(^\text{113}\) This principle dates back to ancient Greece, fifth century B.C., precisely to Athens, the birthplace of democracy by the hand of Cleisthenes as we’ve pointed out before. A democratic state is one where the law is the same for all and the order that comes by law and respect for the law is the only certainty of a sane political life for all citizens.

If we look at the market, we easily conclude which are the consumers’ interests (the product or service they wish to buy and the price they are willing to pay) and the interests of the other economic agents on the market.

Competition law arises as a mediator of these economic interests and, in this sense, a number of domestic laws in the UK have been developed aimed at punishing certain anticompetitive behaviors, such as Competition Act 1998; Enterprise Act 2002; Changes to domestic law as result of Regulation 1/2003 and Enterprise and Regulatory Reform Act 2013, and Consumer Rights Act 2015.

Another goal that the competition law seeks to safeguard is the fairer distribution of wealth and the dispersal of economic power.

Competition law should address conducts that lead to inefficient allocation of resources (e.g. monopoly markets, which reflect unfair competition with exclusive control of the market). However, the idea that competition law should regulate prices to promote efficient resource allocation has been losing force. For example, the case Attheraces Ltd v British Horseracing Board,\textsuperscript{115} in which the Court of Appeal rejected the idea that competition law should interfere to regulate prices since such intervention would result in a distortion of the competitive fabric of the market. Therefore, the redistribution needs to be moderate, in order not to influence the structure of the market.

We should not forget that competition law has another important objective, which is not only geared towards the interests of consumers but is also indirectly connected to the process of competition.

Competitors play a strong role in this economic chain, which is why it makes perfect sense to provide small competitors with powers, granting the necessary protection and allowing them to compete more directly with the strongest competitors, instead of being harmed by them. In a nutshell, given the necessary protection, small competitors will receive a fair opportunity to compete and succeed in the market.

Competition law has the purpose to ensure fair competition, where access to the market is done by an open economy, which allows a wider choice for consumers, better products and where it is possible to achieve greater efficiency, which otherwise would not be possible.

4.4. Competition Law and Crowdfunding

When we look to competition law and crowdfunding, we can wonder if they have something in common and in the case of a positive answer, what unites them. Crowdfunding introduced the financial market in a new digital age and has become an important online alternative finance channel, in which promoters have the possibility to raise money for their projects, through the use of appropriate technologies (online platforms), which enables the promotion of their project in order to induce investors’ interest.

It has become an essential tool for promoters or investors, because it creates a new opportunity of raising funds in an expeditious and effective way, which overcome the traditional market, as already explained in chapter 1.

When we approach crowdfunding, we need to recall what are the basis of its structure: share and collaboration.

These two concepts provide the efficient distribution of resources on a global scale, that means, when the conditions are fulfilled, we can have a pareto efficient allocation of resources.\textsuperscript{116}

It is noteworthy that we also found these two concepts in competition law.

Competition law has the aim of ensuring the organization and efficient distribution of resources in the market by increasing economic efficiency.

Following this reasoning, resources are allocated concerning to the consumers' wishes, avoiding concentration of economic power in the hands of certain undertakings, preventing that way certain behaviors that are considered harmful to competition.

If we keep comparing these similarities, we are able to suggest another one, competition law overlaps with crowdfunding in another interesting point – the focus on welfare of the consumers.

As it was said before, one of the first concerns of competition law is to protect the interest of the consumers and this protection is not only concentrated on observing the behaviour of the process of competition, it goes beyond that. Competition law has an important active role by punishing anticompetitive conducts of undertakings - it effectively ensures the benefits of consumers.

On the other hand, crowdfunding is a mechanism targeted to population (crowds), it is a new business model which gives crowd additional possibilities to funding an activity/service.

The main idea is to give people the opportunity to choose between the “traditional” sources of funding and this new alternative source of funding. In other words, it is beneficial to consumers and to investors, because these people can raise or invest their funds, in a simple, easy and fast way and usually get access to better bank fees (depending on the type of crowdfunding).

In a different perspective, getting a loan in a traditional market, may become a complex process, with likely higher bank fees and commissions, or even be refused (level of indebtedness is too high for loan approval).

A final note to stress the protection that competition law can enable smaller competitors to enter a market and be granted space and conditions to compete. Crowdfunding also offers protection to certain types of investors, restraining the level of their investment, as said in the previous chapter.

«Crowdfunding is more popular or rather successful in advanced economies, as it is quite dependent on mature internet markets and access to money […]»

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5. Can Crowdfunding be a concern to Competition Law?

5.1. Can crowdfunding platforms be considered as a two-sided market?

In a digital economy, it becomes essential to approach the concept of a two-sided market in economic theory, in a way to discover if crowdfunding can be framed on it.

For economists, as Rochet and Tirole\textsuperscript{118} «market is two-sided if the platform can affect the volume of transactions by charging more to one side of the market and reducing the price paid by the other side by an equal amount; in other words, the price structure matters, and platforms must design it so as to bring both sides on board. A necessary (but insufficient) condition for a


market to be two-sided […] is that the relationship between end-users must be fraught with residual externalities. 

Another perspective of a two-sided market concept is given by Luchetta: 119 for this author, a platform is capable of intermediating both sides when three conditions are verified: (i) there is a transaction between two different groups using the same platform; (ii) a large presence of these two different groups provokes reciprocal interside positive externalities; (iii) there is some interdependence between these two different groups, necessary to the operation.

As UK CAT in Case 1262/5/7/16 (T)120 posited «there is an interactive relationship between the two customer groups. The more customers there are on one side, the more attractive the platform is to the other side […]. This feature, generally referred to as “network effects”, means that a potential new market entrant must consider how best to create demand on one side of the market in order to create demand on the other, so that it may benefit from these network effects».

In the light of the above, a platform operates on a two-sided market whenever (i) it acts on the market as an intermediary in a transaction of two unrelated groups; (ii) these two unrelated groups perform some type of interdependence between them; (iii) and by that are able to produce an indirect network effect.

All in all, to achieve these requirements, it is necessary that a platform becomes an attractive one, it cannot adopt a neutral role, on the opposite, it needs to be dynamic.

Considering crowdfunding specifically henceforth, online platforms are appealing by the easy and fast way of doing businesses. Online platforms need to be well structured so that they can have the capacity and dynamics needed to reach both sides of the market. Thus, they are more attractive as more promoters and investors join them. An attractive online platform means that the number of projects on the platform needs to be high. This fact may proportionally increase the opportunity to close deals (more investors) and thereby increasing profit. Consequently, an online platform grows and gains market power by acquiring more users in these two unrelated groups.

These two unrelated groups co-exist on opposite sides of the market: (i) project owners or promoters (“promoters” hereinafter), on one side of the market; (ii) contributors or investors (“investors” hereinafter), on the other side of the market. When these two unrelated groups

120 United Kingdom Competition Appeal Tribunal, Case 1262/5/7/16 (T), 5 July 2017, CAT 15, between Agent’s Mutual Limited vs Gascoigne Halman Limited (T/A Gascoigne Halman), p. 88 [140].
participate on the same online platform directly, the interaction between them arises and is able to produce network effects.

A network effect «refers to the effect that one user of a good or service has on the value of that product to other users». The more attractive an online platform is, the more network effects it will be able to generate. This happens because the value of a good or service increases at the same time that increases the number of other users using it.

Regarding that, it is possible to assert that indirect network effects are verified on crowdfunding platforms. The indirect network effects «occur when a change in a number of users on one side of the platform changes the value of a product or service to a group of users on the other side of the platform». In other words, the more promoters on the crowdfunding platform, the more valuable that network platform is to investors, and vice versa.

For example, on promoters’ side, they can benefit from the use of platforms to advertise their projects or businesses and therefore attract a large number of potential investors (increases the range of opportunities of raising money). On the investors’ side, they can benefit from the use of the platform, as it allows the access to a vast number of projects or businesses that can be interesting to them (thus, they have more business opportunities).

These indirect ‘network effects’ are able to produce within-side or cross-side effects on these two unrelated groups.

Within-side effects are verified, when an additional value of the platform happens for users on one side of the market, as a result of the presence of other users on the same side of the market - increasing the number of users, the value to other users will also increase. These within-side effects are able to produce positive or negative effects on one of the parts of the market. Viotto for example, refers that within-side positive ‘network effects’ can be verified on crowdfunding, on the investors’ side, when a large number of projects or businesses achieve their objectives. That stand is acceptable as, when the investors receive their payments, the

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value of the platform will increase, becoming more attractive to other investors- creating a mirror effect.

Within-side negative ‘network effects’ can also be verified on crowdfunding, on the promoters’ side. That situation occurs when an increase in the number of promoters decreases the value of the platform to other promoters. The more projects on the platform, the greater is the competition between promoters to get the potential investors’ attention – spillover effects, as Viotto postulated.

Cross-side ‘network effects’ are verified when an additional value of the platform is achieved for the users of one side of the market as a result of the presence of another group on the other side of the market.127 Basically, as previously referred, the more promoters on the same network platform, the more valuable that same network platform is to investors, and vice versa. A large presence of promoters on the same online platform means a wider choice for investors (the possibility to find a project or business which may be of interest to investors increases in the same proportion as the offers). A large presence of investors on the same online platform increases the likelihood of a project or businesses being supported (more investors means more business opportunities).128

It is worth mentioning, that online platforms are not free from charge. When projects or businesses reach their goals, a platform charges a fee on the funds collected. However, a commission can also be charged prior to their goals’ achievement in certain models of crowdfunding, loan and investment namely, especially if it performs a due diligence to comply regulation.

A question that may arise is, which side the platform will support first. Crowdfunding platforms are intermediaries of both parties (promoters and investors), platforms need to attract and respond to the expectations of both. This interdependence of demand creates a “chicken-and-egg” problem.129 How to overcome this situation? Crowdfunding platforms solve the problem by supporting the promoters, doing efforts in a way of making campaigns to ‘catch the eye’ of investors and making them free of charge to promoters, in order to encourage others to join them, with new projects or ideas130.

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Bearing in mind all the explained above, crowdfunding platforms may be categorized as a two-sided market. The reasons to support this conclusion are the fact that crowdfunding platforms have the capacity to make themselves attractive to promoters and investors (two unrelated groups in the market). Since crowdfunding platforms are not neutral, they intermediate promoters and investors, when there is some type of interdependence between them, which enables platforms to create indirect network effects on these two groups.

5.2. Can Crowdfunding be described as an ecosystem that generates consumption synergies?

In the digital economy, a multilateral platform basically means innovation of services and applications - in the sense to have the capacity of attracting both sides of the market.

As said before, crowdfunding platforms have the capacity to intermediate and coordinate both sides of the market, however, to continue our study, it seems relevant to understand what is the concept of consumption synergies and whether crowdfunding can be framed on it.

As Bourreau and Streel\textsuperscript{131} defend, synergies can be generated on both sides of the market. On the supply side, through the economies of scope considering the development of products, and on the demand side, when the consumer chooses to buy products in the ecosystem.

For these authors, on the demand side, consumption synergies can be generated whenever a consumer decides to purchase different products or services from the same supplier, and these consumption synergies can be in two different types: (i) from bundling or (ii) from ties. Bundling, that can be defined as a package with two or more products at a lower price than when purchased in a separate way; or from ties, that can be defined when a linkage is formed between their different products, in a way to increase the complementarity between them, consequently, these ties grant an additional benefit to consumers.

For the same authors, «[…] when two products are not sold as a bundle […] we will refer to such a set of products sold separately by a firm, which generates consumption synergies for consumers when bought together, as a product ecosystem».\textsuperscript{132}


\textsuperscript{132} Marc Bourreau, Alexandre de Streel, “Digital Conglomerates and EU Competition Policy. cit., p. 10.
For Chen and Rey\textsuperscript{133}, consumption synergies arise when consumers decide to buy different products on the same supplier, benefiting from the one-stop-shop. For these authors «buying both products from the same firm thus generates one-stop shop benefits, by saving the cost of a second visit». In other words, the opportunity cost of time, for some consumers is a determining factor for generating consumption of synergies.

Overall, these consumption synergies, achieved by means of bundling or ties, encourage companies to develop strategies, in order to innovate and diversify their products and thereby generate product ecosystems.

When approaching crowdfunding in an overview, we realize that it encompasses several models and types. As we have pointed out, crowdfunding can be categorized in four main models, the Non-Profit Ventures, such as (i) Donation-based crowdfunding or (ii) Reward-based crowdfunding. And, also has Profit Ventures, such as (iii) Loan-based crowdfunding (for example, P2P Consumer Lending; P2P Business Lending; P2P Property Lending and Invoice Trading), or (iv) Investment-based crowdfunding (such as, Equity-based crowdfunding; Debt-based Securities; Securities not issued by the Promoter; Profit Sharing crowdfunding; Community Shares and Real Estate crowdfunding). As a result, different promoters and investors have the power to influence crowdfunding in several ways by creating a product ecosystem.

Crowdfunding as a tripartite business involves promoters, investors and platforms, representing the individual investments. On the scheme of crowdfunding, dependence on the performance of the promoter (creator) is the basis to the creation of synergies, conceiving a new product, project, business or start-up. In this sense, crowdfunding enables to join different types of co-creation values together with a platform, and by that makes possible the formation of new types of service and value-exchange ecosystems.

If we observe crowdfunding, we also find some hybrid platforms, which allow the investment/contributions in different crowdfunding types on the same platform. For example, the online platform Crowdfunder.co.uk is a platform that can provide several services, such as supporting a solidarity cause, or raising money for a certain project or even when someone wants to create a «big impact in community»\textsuperscript{134}. In other words, one company can be a contributor for a charitable cause [donation model] and a sponsor in a community project.


\textsuperscript{134} Crowdfunder, Available at \url{https://www.crowdfunder.co.uk/} accessed on 20-11-2019.
[reward model]. Both donations are done on the same platform, with distinct effects, becoming the company more efficient and spending less time in this process - one-stop-shop benefits- by that generating consumption synergies as a product ecosystem.

An important note is the fact that the existence of consumption of synergies enables that the supply of products or goods in the ecosystem can be subsidized.\textsuperscript{135} Regarding crowdfunding, whenever projects or businesses of promoters reach their target, a fee is charged by the platforms, so promoters often subsidize platforms\textsuperscript{136}. On the other hand, investors are subsidized [exception on donation model] by a return of their investment done in a certain campaign when the goal is achieved.

5.3. Single- homing, multihoming, asymmetric prices, network effects

As being said before, competition law has the aim of ensuring the organization and efficient distribution of resources in the market by increasing economic efficiency.

On the other hand, digital platforms such as crowdfunding, appear to improve competition, making the market more dynamic, and ensure a better match between supply and demand. crowdfunding is a mechanism targeted to population (crowds) and it is a new business model which gives crowd additional possibilities to funding an activity or service. Therefore, where can we possibly find restrictive practices to competition? As mentioned in the previous points, in their own model, crowdfunding platforms act as «matchmakers»\textsuperscript{137} and they deliver to promoters and investors significant network effects. Once a platform has taken an important position in the market – with huge numbers of promoters and investors – its expected strategy is to expand into a new market\textsuperscript{138, 139}.

\textsuperscript{136} Jordana Viotto da Cruz, “Competition and Regulation of Crowdfunding Platforms: A Two-Sided Market Approach”, cit., p.3.
\textsuperscript{139} For example, the company Crowdcube Limited, has two related undertakings: Crowdfunder Limited and Crowdcube Capital Limited on crowdfunding activities. Crowdcube Limited, registered number 07014587, Annual Report and Financial Statements for the year ended 30, September 2018, available at https://www.gov.uk/government/organisations/companies-house.
The platform Crowdfunder.co.uk., which belongs to Crowdfunder Limited is one of the most popular crowdfunding platforms in the UK. It can provide services regarding two different models of non-profit ventures, such as donation and reward-based crowdfunding.

The platform Crowdcube, which belongs to Crowdcube Capital Limited is another popular crowdfunding platform in the UK. This platform is for profit ventures - an equity-based crowdfunding, whose revenue has been growing, regarding their Shareholders’ update Q2 2019. According to that, this platform has been growing since the year of 2017 from an amount of £2million to the amount of £3,720,000,00 in the year 2019.

This expansion into a new market had the strategy to capture the attention of other promoters and other investors in a different area of business – profit ventures. As a result, the new platform benefits of their know-how in the primary market, the data of the users, the advantage of a good and established trade mark on the primary market and the trust of the users, as well as an advantage of shared components (software). Above all, significant indirect network effects.

These crowdfunding platforms have strong market power, so they may have the power to weaken competition in their respective markets and may become a dominant platform on their market.

In such a case, a dominant platform would benefit of significant indirect network externalities, so it would be able to attract more promoters and investors (“getting both sides on board”\textsuperscript{140}). The competitiveness between the dominant platform and the others would be weakened due to pricing strategy, single-homing and significant network effects.

For Caillaud and Jullien, the key to becoming a dominant platform is in the structure of price. For these authors, «transaction fees appear to be a powerful weapon for intermediation service providers to gain market shares»\textsuperscript{141}. However, when global multihoming is efficient, it means that the level of competition in the market is high and the possibility to arise a dominant platform is quite low.

If we observe the intermediation services of crowdfunding platforms, we realize that there are transaction fees.

Whenever projects or businesses of promoters reach their target, a fee is charged by the platforms - charging one side of the market.\textsuperscript{142} However, it is free of charge for investors [in

\textsuperscript{140} Jean-Charles Rochet, Jean Tirole, “Platform competition in two-sided markets”, cit., accessed on 29-11-2019, p. 1013.


\textsuperscript{142} It is important to mention, that a charge may be applied in the cancellation of a certain campaign (promoters).
certain models of crowdfunding, like loan and investment, if a platform performs a due diligence to comply regulation a fee can be charged].

The fee mentioned above, is only charged in transactions intermediated on the same platform between promoters and investors.

This policy, which charges one side of the market and is free of charge to the other side, reveals asymmetric prices structure.

These asymmetric prices are proportional to the transaction price and depend on the success of the campaign.

For Rysman «two-sided markets allow for a new form of price discrimination: discrimination based on heterogeneity in the attractiveness of an agent to the other side»\(^{143}\), and «discrimination increases the value extracted on one side, which leads to lower prices on the other side which has now become more valuable»\(^{144}\).

However, such new form of price discrimination cannot be carried out in a discretionary manner with the aim of becoming an attractive platform. Otherwise, it will be able to trigger anti-competition practices.

For example, in the markets where the level of competition is low, the dominant platform is able to charge transactions with high fees. By that, users will be affected, since on the promoter’s side the stipulated fee will be higher, and on the investor’s side the interest rate, in return for their investment, will be lower.

The dominant platform with these pricing practices triggers anti-competitive effects, which reveal themselves to be harmful to both sides of the market.

Furthermore, the dominant platform can eventually use their market power to foreclose a potential entrant on the market, through transaction fees and network externalities.

Notwithstanding, this issue can be mitigated, if the level of competition is high and multihoming is efficient.

For single-homing, we will use the definition of Rysman, for this author single-homing arises in the online market «when agents on one side use a single platform in a multi-platform context».\(^{145}\) In other words, when the user has available multiple platforms in the online market, but decides to always use the same platform. In such a case, single-homing will be strengthening competitive advantage of the dominant platform, since users want to continue using this

\(^{143}\) Marc Rysman, “The Economics of Two-Sided Markets”, cit., p. 131.

\(^{144}\) Apud: Marc Rysman, “The Economics of Two-Sided Markets”, cit., p. 131.

platform, despite higher fees, rather than switching to another more advantageous platform (cheapest ones).

One of the strategies that may be adopted by a dominant platform will be the development of ecosystem’s products, in order to tie the users to single-homing.\textsuperscript{146}

For Armstrong, multihoming can be defined as «the participation of users to multiple platforms».\textsuperscript{147} Putting in another way, multihoming happens when a user on one side of the market has the ability to be present on more than one platform.

From a competitive point of view, multihoming is very important to competition, as it allows the coexistence of several platforms and avoids the concentration of market power. In this sense, Caillaud and Jullien postulated «competition is more intense when platforms cannot deter multihoming».\textsuperscript{148}

Regarding crowdfunding, Viotto\textsuperscript{149} refers in this specific matter, that promoters tend to single-homing and investors tend to multihoming. If a promoter has a project or a business, the first step is to choose a platform that better fits in their purposes, considering the model and the type of crowdfunding intended to do.

Consequently, promoters would be able to change to another platform in the case of new businesses or projects in different crowdfunding models or types than the previous ones - the chosen platform is not authorized to work on these activities.

Usually, when promoters have a new project, they start on the same platform again, but there is no obligation to do so.

On the investors’ side, the rule is to choose a platform that better matches its objectives. Investors can have the most varied interests and therefore participate in various platforms in different projects. Moreover, joining a platform is free of charge.

Briefly, single-homing improves market power and by that increases the possibility to arise a dominant platform. Multi-homing improves competition and allows the coexistence of several platforms on the market.

In short, crowdfunding platforms can pose some danger to competition and produce anti-competitive effects, when a crowdfunding platform acquires strong market power and becomes a dominant platform. In such a case, it benefits of significant indirect network externalities, and

\textsuperscript{146} Other strategies can be: the subsidization of users, bundling and tying.

\textsuperscript{147} Apud: Giacomo Luchetta, “Is the Google platform a two-sided market?”, cit., p.5.

\textsuperscript{148} Apud: Jean-Charles Rochet, Jean Tirole, “Platform competition in two-sided markets”, cit., p.994.

it is able to get both sides on board, as an attractive platform in the market. Consequently, it will charge transactions with high fees (promoter side) and on the investor side the interest rate, in return for their investment, will be lower. It may happen that it charges some fee to investors who choose to join it. Another strategy of the dominant platform will be to try to foreclose the market to a new entrant through the high transaction fees (asymmetric prices structure) and by that, avoid multihoming. Furthermore, its network effects are much more significant than those enjoyed by the entrant.

The dominant platform will do efforts in the development of projects or businesses in the ecosystem’s products, in a way of ensuring single-homing - tries to keep the competition weakened.

Another strategy would be bundling or tying considering the ecosystem products; however, so that a platform can be able to do that, it needs to have enough projects or businesses already, with the capacity to increase the complementarity between them. As crowdfunding creators are the promoters and they are unrelated, it seems difficult to find some linkage between the products, projects or businesses. Thus and for now, bundling and tying do not appear to be feasible.

5.4. Can a cartel be verified between crowdfunding platforms?

Another uprising phenomenon is the fact that a number of companies, by their scope, are certified to license online crowdfunding platforms to operate in the market.

This license process needs to meet with various requirements, and undergo a scrutineer, in order to verify if the entity complies with FCA regulations. After the certification is issued, they will be kept on an ongoing supervision, being dependent of that company, through frequent auditing. Furthermore, it is the company that granted the certificate, that will be held accountable to the FCA, to ensure they comply with the regulations.\textsuperscript{150}

These crowdfunding platforms still depend on this company as a representative, so the information exchange with the representative may constitute or not a concerted practice.

Before realising that, it is necessary to assess if those exchanges of information have as their object or effect the restriction of competition.\textsuperscript{151}

\textsuperscript{150} See ShareIn Limited available at \url{https://www.sharein.com/}

\textsuperscript{151} Richard Whish, David Bailey, “Competition Law”, cit., p. 551. See Article 101 of TFEU.
Most of times, the exchanges of information are about the functioning of the market, their conditions, quantity demanded by buyers and the quantity provided by sellers and the price, in order to follow the best strategy,\(^{152}\) therefore, poses no danger to competition. Sometimes, in the opposite way, the information exchanges can form highly sensitive commercial information, with the aim of restricting competition and achieving more effective control in the respective market. This sensitive commercial information can be shared in order to eliminate competition between them, thus, each of them adopts the stipulated strategies (conduct) and coordinate their behaviour.\(^{153}\)

Any concerted practice contains very significant restrictions in terms of their impact on competition. In reality, this collusive behaviour ends up subverting the regular functioning of the market, as said Whish and Bailey.

It is difficult to have access to documents to establish if these platforms are part of a concerted practice and potential price fixing practices.

In fact, as monitoring part, the representative receives all the information related to the crowdfunding platforms, where it is represented.

The main question is what does it do with sensitive commercial information?

If these platforms have their scope on different models of crowdfunding, such as one in non-profit ventures [donation and reward-based crowdfunding] and another one in profit ventures [loan and investment-based crowdfunding], do not seem to raise concerns to competition. Business areas are distinct, the commercial target is unrelated, there is no interest in coordinate their behaviours.

A different situation arises when these platforms act, not only in profit ventures, but at the same time, in the same model and sometimes in the same type of crowdfunding. For instance, if these platforms act in investment-based crowdfunding, in particular equity crowdfunding the likelihood for the existence of strategy or pricing intentions would be feasible.

On the example provided, these crowdfunding platforms share exactly the same sides of the market, with the same interests.

In a hypothetical situation, instead of improving competition through more competitive prices, in fact, they may end up receiving indications from the representative of how to act in the market, in order to improve their profit. Such as, indicating the fees to apply to each transaction, the interest rate to offer to investors, elements which would otherwise not be accessible to

\(^{152}\) Richard Whish, David Bailey, “Competition Law”, cit., p. 552.

competitors- strategic prices. Thus, each platform knows, with accuracy and detail, the characteristics of the other offers, eliminating competitive pressure, adapting its conduct on the market.

As Whish and Bailey cited «the exchange between competitors of strategic data is more likely to infringe Article 101 (1) ».\(^{154}\)

According to Article 101 (1) TFEU which establishes as prohibited concerted practices, those which have as their object or effect the prevention, restriction or distortion of competition within the internal market.

Basically, if competitors platforms act in the market, with collusive behaviour in order to control effective competition in the market, through intended prices, share data or conducts pre-stipulated, they form a cartel.

A cartel is an anti-competitive practice extremely detrimental to the market and to the consumers. With this manipulation in the process of competition, consumers are likely to be harmed.

Therefore, a question remains: if that dependence [regarding the representative] does not directly or indirectly influence the way the platform operates, no danger is posed to competition. On the contrary, if the company joins the platforms to negotiate pricing or strategy, then it is considered to be a cartel. These information exchanges can be an open door so that these platforms can coordinate and stabilise prices. In such a case, it is important for competition authorities to be conscious of this situation and be vigilant to those anticompetitive actions.

6. Conclusion

As said before, for the economy, competition is good. Competition allows innovation, the increase of the quality of the product or service, permits the pursuit of excellence, in a way that the result is verified through better products, lower prices, with a wider choice to the consumer, thus achieving a dynamic efficiency.

Competition reveals itself as a valuable economic mechanism in order to assure the best market practices, allowing consumers to reach benefits (better prices; better products; larger choice of products or services among others).

Crowdfunding platforms are seen as effective means to achieve allocative efficiency of resources.

Throughout this thesis it was observed that crowdfunding may act in the market in different models and types. It has become an essential tool for promotors or investors, because it creates a new opportunity of raising funds in an expeditious and effective way, which overcome the traditional market.

In general, crowdfunding will not pose any concerns to competition when in the market several platforms are available for different models, increasing the competition between them - multihoming. As it was demonstrated, crowdfunding platforms act in two-sided market, creating, therefore, indirect network effects allowing promotors and investors to get on board. This intermediation may be beneficial to both promotors and investors as it promotes a better economic efficiency.

In some rare occasions, crowdfunding platforms may display restrictive practices to competition when a strong market power is acquired. The abuse of a dominant position by a crowdfunding platform is a restrictive practice of competition, which arises from the unlawful use by a platform of the power it has in a certain market. The abuse of dominant position happens when a firm carries out behaviours that are likely to influence the structure of a market. The dominant platform benefits from a large number of indirect network effects and strong market power. Consequently, high fees transactions will be applied in the market, due to a lower level of competition, enabling to foreclose the market for new entrant or encourage their exit. That behaviour revels itself harmful to both sides of the market, promotors – high fee transactions; investors – lower interest-free credit, in fact, produces asymmetric prices, which constitutes a detrimental practice affecting the welfare of promotors and investors. These
asymmetric prices are proportional to the transaction price and depend on the success of the campaign.

Furthermore, in order to maintain a dominant position, ecosystem products will be developed to guarantee single-homing and, as a result, it may create a tie or bundling. Services provided by crowdfunding may be considered an ecosystem product. The difficulty is to create a tie in that ecosystem product. In my opinion, crowdfunding platforms depend on promoters, who are the creators of products and businesses, so these platforms do not enjoy of that capacity to tie because they are still attached to the promoters’ creations. However, bundling may be one of the strategies to be used by the platform. For example, platforms can make interest rates more attractive to investors, if they decide to invest, simultaneously, in two projects or businesses, previously selected by it as a bundling.

Along this thesis another relevant issue arose. It seems that competition authority needs to remain vigilant to the possibility of a carter between crowdfunding platforms, which have in common the same representative.

A cartel, as said before, is a practice between actual or potential competing company with the aim of restricting competition and achieving more effective control in the respective market, developed to limit or eliminate competition between them, with the purpose of increasing prices and profits of the participating companies.

Therefore, companies, which by their scope, are certified to license online crowdfunding platforms to operate in the market have access to sensitive commercial information. Most of times, the exchanges of information are about the functioning of the market, their conditions, quantity demanded by buyers and the quantity provided by sellers and do not represent any danger to competition.

According to Article 101 (1) TFEU which establishes as prohibited concerted practices, those which have as their object or effect the prevention, restriction or distortion of competition within the internal market. The main difficulty is to gather evidence of that coordinated behaviour.

If this sensitive commercial information can be shared in order to eliminate competition between them, thus, each of them adopts the stipulated strategies (conduct) and coordinate their behaviour, instead of improving competition through more competitive prices. In fact, they may end up receiving indications from the representative of how to act in the market, in order to improve their profit. Such as, indicating the fees to apply to each transaction, the interest rate to offer to investors, elements which would otherwise not be accessible to competitors- strategic
prices. Thus, each platform knows, with accuracy and detail, the characteristics of the other offers, eliminating competitive pressure, adapting its conduct on the market.

Basically, if competitors platforms act in the market, with collusive behaviour in order to control effective competition in the market, through intended prices, share data or conducts pre-stipulated, they form a cartel.

On the opposite side, if the representative does not directly or indirectly influence the way the platform operates, no danger is posed to competition.

All in all, competition authority, in the face of the rapid evolution of crowdfunding, needs to be attentive to possible restrictive practices of competition.

The digital economy is rapidly developing and competition law needs to be able to keep up with this development. It cannot be obsolete or behind the times, otherwise, it will not ensure effective competition on the market.
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