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## INTERESTING LEGAL FACTS ABOUT CROWDFUNDING in Romania

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Crowdfunding has become one of the main sources of funding for start-ups and, for a prolonged period of time, it has existed without being formally regulated. Consequently, along with the benefit of raising large amounts of money in a relatively short period of time came the growing risk of scams, raising justified concerns regarding the overall usefulness of crowdfunding.

On 7 October 2020, the European Parliament and the Council of the European Union adopted Regulation (EU) 2020/1503 on European crowdfunding service providers for business, and amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 (hereinafter referred to as the **“Regulation”**). In this context, a number of EU member states adopted national legislation regulating the activity of crowdfunding service providers, tailored to the characteristics and needs of local markets and investors. **In Romania, the Parliament issued a draft of the law implementing the Regulation, which has yet to be voted upon, but might well be adopted in the near future.**

This article will focus on the main aspects provided in the Regulation, as well as the provisions of the draft law proposed to be adopted in Romania. Please bear in mind that the provisions of the draft law might be subject to change and it is not mandatory for it to be adopted in its current form.

## **What is crowdfunding?**

The Regulation defines crowdfunding services as the matching of business funding interests of investors and project owners through the use of a crowdfunding platform and which consists of any of the following activities:

- (i) the facilitation of granting of loans;
- (ii) the placing, without a firm commitment basis, of transferable securities and admitted instruments for crowdfunding purposes issued by project owners or a special purpose vehicle, and the reception and transmission of client orders, in relation to those transferable securities and admitted instruments for crowdfunding purposes.

However, more commonly, crowdfunding is defined as the practice of funding a project or venture by raising money from a large number of people who each contribute a relatively small amount, typically via the internet.

Consequently, crowdfunding is an increasingly important type of intermediation where **a crowdfunding service provider, without taking on risk itself, operates a digital platform open to the public in order to match or facilitate the matching of prospective investors or lenders with businesses that seek funding.** Such funding could take the form of loans or the acquisition of transferable securities or of other admitted instruments for crowdfunding purposes.

Thus, the provision of crowdfunding services generally involves three parties: (i) the project owner, who proposes the project to be funded, (ii) investors who fund the proposed project and (iii) an intermediating organization in the form of a crowdfunding service provider that brings together project owners and investors through an online platform.

In addition to **providing an alternative source of financing, crowdfunding can offer other benefits to businesses**, such as (i) validating a business idea, (ii) offering entrepreneurs access to a large number of people providing insights and information and (iii) being a marketing tool.

Usually, crowdfunding service providers use online platforms for rendering their services, some of them **addressing all types of entrepreneurs** (e.g., Kickstarter, Indiegogo), while others **specialize in certain areas** (e.g., GoFundMe and Crowdfunder – personal fundraising, SyndicateRoom – start-ups and businesses, Crowdcube: early-stage companies, Seedrs –start-ups, Crowdrise – social causes and non-profits).

Numerous crowdfunding projects in various fields have proven to be successful, thus encouraging people to pursue this type of service in order to fund their projects. In this respect, we can list the following well-known successful projects:

- (i) Blockchain and cryptocurrency: Ethereum, EOS, Filecoin, Tezos, Polkadot, TRON
- (ii) Gaming (video and board games): Star Citizen, Frosthaven, Exploding Kittens, Kingdom Death Monster, The 7th Continent
- (iii) Hardware: Oculus Rift, Coolest Cooler, Pono Music, The Dash, Hyphen Wireless Earbuds, OUYA Video Game Console, Snapmaker 2.0
- (iv) Photography: Travel Tripod, The Everyday Backpack
- (v) Watch making: Pebble, Filippo Loreti
- (vi) Automotive: Sono Motors Sion
- (vii) Fashion: Baubax Travel Jacket
- (viii) Movies and television series: Bring Back Mystery Science Theater 3000, The Veronica Mars Movie Project, Reading Rainbow

## **What does the Regulation provide?**

### **Purpose**

The purpose of the Regulation is **to lay down uniform requirements** for the provision of crowdfunding services, for the organization, authorization and supervision of crowdfunding service providers, for the operation of crowdfunding platforms as well as for transparency and marketing communications in relation to the provision of crowdfunding services in the European Union (hereinafter referred to as the “EU”).

The Regulation also aims to foster cross-border crowdfunding services and to facilitate the exercise of the freedom to provide and receive such services in the internal market, by eliminating obstacles to the proper functioning of the internal market in crowdfunding services and ensuring a high level of investor protection.

## Obligations set out for crowdfunding service providers

Given the risks associated with crowdfunding investments, in the interest of the effective protection of investors and of the provision of a mechanism of market discipline, the Regulation imposes certain obligations for service providers, such as:

- (i) Implementing a **threshold of EUR 5,000,000** for a total consideration for crowdfunding offers made by a particular project owner;
- (ii) Proposing crowdfunding projects to individual investors based on one or **more specific parameters or risk indicators**, such as the type or sector of business activity or a credit rating, which have been communicated in advance to the crowdfunding service provider by the investor;
- (iii) **Obtaining an authorization** from the competent authorities and providing services only under the supervision of such authorities. Only legal entities that have an effective and stable establishment in the EU, including the necessary resources, should be able to apply for authorization as crowdfunding service providers.

In this sense, the European Supervisory Authority (European Securities and Markets Authority or ESMA) shall establish a **public and up-to-date register** of all authorized crowdfunding service providers, which includes information on all operating crowdfunding platforms in the EU. Competent authorities from different member states shall cooperate with each other by exchanging and cooperating on investigation, supervision and enforcement activities.

However, an **authorization to provide crowdfunding services does not equate to an authorization also to provide payment services**. Therefore, where a crowdfunding service provider provides such payment services in connection with its crowdfunding services, it also needs to be a payment service provider;

- (iv) **The use of legal structures**, including special purpose vehicles, that interpose between the crowdfunding project and investors shall be **strictly regulated and permitted only where it is justified** by enabling an investor to acquire an interest in, for example, an illiquid or indivisible asset through issuance of transferable securities by a special purpose vehicle;
- (v) Being **subject to prudential requirements** and being prohibited from taking deposits or other repayable funds from the public, unless they are also authorized as a credit institution;
- (vi) Operating as **neutral intermediaries** between clients for their crowdfunding;
- (vii) Crowdfunding service providers shall **not pay or accept any remuneration, discount or non-monetary benefit for routing investors' orders** to a particular crowdfunding offer made on their crowdfunding platform or to a particular crowdfunding offer made on a third-party crowdfunding platform;

- (viii) Developing business continuity plans **addressing the risks associated with the failure** of a crowdfunding service provider platform;
- (ix) Facilitating transparency and ensuring proper documentation of communications with clients, and keeping all appropriate records related to their services and transactions;
- (x) Undertaking at least a minimum level of due diligence in respect of project owners that offer their projects to be funded through the service provider's crowdfunding platform;
- (xi) Implementing effective and transparent procedures for the prompt, fair and consistent handling of complaints received from clients;
- (xii) Maintaining and operating effective internal rules to prevent conflicts of interest. In this sense, crowdfunding service providers shall not have any participation in any crowdfunding offer on their crowdfunding platforms.

## **What does the Romanian draft law provide?**

The draft law sets out measures for applying the provisions of the Regulation in Romania.

Firstly, the draft law provides **that the competent regulatory authority shall be the Financial Supervisory Authority** (in Romanian Autoritatea de Supraveghere Financiara) (hereinafter referred to as the **"FSA"**). In this respect, it shall be responsible for complying with the provisions of the Regulation, being the point of contact for cross-border administrative cooperation between other competent authorities and the ESMA.

Furthermore, the draft law implements all the provisions of the Regulation, setting out the specific conditions to be followed in order for interested entities to be registered with the FSA as crowdfunding service providers. Also, the FSA will hold a registry of all such authorized providers. The draft law also regulates the sanctions applicable for failure to comply with its provisions, as well as with the provisions of the Regulation.

## **Conclusion**

The new regulations applicable to crowdfunding services will result in a more controlled environment, offering a higher level of security to potential investors, who may otherwise be discouraged from using such platforms. Consequently, such regulations will also help project owners by creating a larger pool of investors, thus being able to finance their projects faster than on an unregulated market.

Our law firm is prepared to assist you in navigating these new regulations, as well as offer any additional information that you may require regarding the matter analysed in the present article.

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