



LEGALINK
INTERNATIONAL BUT PERSONAL

EQUITY CROWDFUNDING & PEER-TO-PEER LENDING

2019 1ST EDITION



INTRODUCTION

Crowdfunding has already an established and proven recognition worldwide as a powerful alternative financing tool. Three main points should be signaled in this respect. On the one hand, the volume of the crowdfunding market keeps increasing sharply at global level. On the other hand, the crowdfunding market is very dynamic as new crowdfunding platforms have recently started to operate. Finally, the projects to be financed through crowdfunding platforms are more and more diverse.

In this context, at a time when crowdfunding regulation is subject to discussion around the globe (namely in the context of the Proposal for a EU Crowdfunding Regulation), it seems important to assess the legal responses from various relevant jurisdictions, in respect to Equity Crowdfunding and Peer to Peer Lending. Such is the purpose of this publication.

This book is dedicated to the memory of Georg Van Daal, Former Deputy Head of Legalink FinTech Forum. Georg was a brilliant lawyer and a partner at Ekelmans & Meijer from 2014 to 2018. He was key to the structuring and to the development of this project but unfortunately could not live to see its final form. He is dearly missed.

October 2019

Paulo Câmara
Managing Partner of Sérvulo & Associados
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INDEX

ARGENTINA.....	04
Nicholson Y Cano Abogados	
AUSTRALIA.....	09
Piper Alderman	
CHILE.....	14
Grasty Quintana Majlis	
COLOMBIA.....	18
MTA	
CZECH REPUBLIC.....	26
Felix A Spol.attorneys At Law	
GERMANY.....	33
Rittershaus	
HONG KONG.....	41
Charltons	
ITALY.....	48
Cocuzza E Associati Studio Legale	
LATVIA.....	53
Vilgerts	
LIECHTENSTEIN.....	57
Gasser Partner Rechtsanwälte	
MALAYSIA.....	61
Azman Davidson & Co.	
MALTA.....	66
DF Advocates	
MEXICO.....	71
Ramos, Ripoll & Schuster	
NEW ZEALAND.....	80
Lowndes Law	
POLAND.....	85
FKA Furtek Komosa Aleksandrowicz	
PORTUGAL.....	99
Sérvulo & Associados	
RUSSIA.....	104
Intellect	
SOUTH AFRICA.....	112
Fluxmans Inc.	
SOUTH KOREA.....	118
Barun Law	
SPAIN.....	124
Ventura Garcés & López-Ibor	
SWEDEN.....	128
Hellström	
TURKEY.....	141
Gun+Partners	
UK.....	146
Mishcon De Reya	
UNITED KINGDOM.....	151
Weightmans	

Equity Crowdfunding

For the purposes of the following, 'equity crowdfunding' means raising capital in an offering of shares (or instruments convertible into shares) through an online platform

South African Regulation of Equity Crowdfunding and Peer-to-Peer Lending – Provided for information purposes only and not intended to constitute legal advice.

1.Has your country introduced specific laws or regulations governing equity crowdfunding, or is it regulated under general securities or other laws?

South Africa is yet to introduce specific laws governing equity crowdfunding. Crowdfunding, inasmuch as it involves the offering of shares (or instruments convertible into shares), would fall to be regulated by the South African Companies Act of 2008 (the Companies Act). The Companies Act places certain restrictions on the offering of shares to the public. It also contains provisions regarding pre-incorporation contracts that may apply should the entity that is seeking crowdfunding not be incorporated. Moreover, the Companies Act would require entities to have Memorandums of Incorporation (MOI) authorising the public offering of shares in the entity.

Crowdfunding and the process involved in the transmission and storage of data related thereto may also be regarded as a cryptography product or service and thus fall within the ambit of the Electronic Communication and Transactions Act 25 of 2002 (ECTA). Additionally, the transfers of monies involved in crowdfunding may also attract regulation under the Financial Intelligence Centre Act 38 of 2001 (FICA).

In addition, the Collective Investment Schemes Control Act 45 of 2002 (CISCA) may apply, given that crowdfunding in exchange for equity could be regarded as a collective investment scheme. To the extent that equity crowdfunding involves instruments that may be converted into shares, the use of cryptocurrencies must be considered. Cryptocurrencies may be offered in exchange for fiat/material currency or assets, with the cryptocurrency convertible into shares in the entity seeking funding (alternatively, representative of those shares itself).

In this regard, a number of proposed regulatory frameworks exist in the form of the Cybercrimes and Cybersecurity Bill of 2017 and the Intergovernmental FinTech Working Group (IFWG) consultation paper on policy proposals for crypto assets by the Crypto Assets Working Group (CARWG), published in January 2019.

The consultation paper by CARWG proposes a number of applicable recommendations for the future regulation of crypto assets. Currently, in terms of the ECTA, the Director-General of the Department of Communications would have the applicable regulatory authority to oversee and implement regulation pertaining to crypto assets.

2.If your country regulates equity crowdfunding, what are the names of the government agencies responsible for regulating it?

South Africa does not directly regulate crowdfunding. It may, however, be indirectly regulated through the potential application of the legislation and proposed legislation mentioned above.

In terms of the Companies Act, the Companies and Intellectual Property Commission (CIPC) would

have regulatory powers over crowdfunding-seeking entities. In terms of FICA, the Financial Services Commission (FSC) would have the requisite regulatory powers. In terms of Cisca, the registrar would have the requisite regulatory powers.

In this regard, the consultation paper by CARWG proposes that existing bodies should either be given new powers to deal with cryptocurrencies (thus crowdfunding as applicable) or, alternatively, new bodies should be established if adaptation is not possible.

3. Are there limits on the amounts that can be raised by crowdfunding companies?

There are currently no limits in place.

4. Are there restrictions on the types of purchasers to whom shares can be offered?

There are currently no restrictions inasmuch as the shares are understood to be normal shares being offered for subscription to the public in terms of the Companies Act. The only restrictions that may be created are restrictions in terms of the MOI of the entity offering them.

5. What information needs to be disclosed to potential purchasers, and are offer documents or marketing materials required to be registered or approved by your country's regulators?

Offers of shares in companies to the public are restricted in that they must be accompanied by registered prospectuses made available to prospective buyers. If these documents are not made available, the sale and issue of shares can be invalidated.

6. Is there any requirement for an equity crowdfunding platform and/or its operator, or a crowdfunding company, to be licensed or registered or to comply with any particular rules?

It may be argued that an equity crowdfunding platform or operator is offering a cryptography service or product which is designed to facilitate the use of cryptographic techniques for the purposes of ensuring that: the authenticity or integrity of such data or data message is capable of being ascertained; the integrity of the data or data message is maintained; the data or data message can be accessed or can be put into an intelligible form only by certain persons; and the source of the data or data message can be correctly ascertained. In any of these circumstances, the equity crowdfunding platform falls to be registered with the Minister of Communications in terms of the ECTA.

7. Please provide any additional information you feel is important to understanding the regulation of equity crowdfunding in your country.

Currently, South Africa has only taken steps toward adopting legislation aimed at the regulation of cybercrimes and cryptocurrencies. In a country such as South Africa where a large portion of the populace do not have bank accounts, it is clear that regulatory priorities are aimed at encouraging the use of informal banking and business sectors such as crowdfunding to provide greater financial inclusivity. It may be unwise for South Africa to overregulate this space and potentially hamper the exponential growth that could occur.

8. Please identify a point of contact at your firm for equity crowdfunding-related enquiries.

For further information regarding equity crowdfunding in South Africa, please contact **Ryszard Lisinski** (email: rlisinski@fluxmans.com; tel: +2711 328 9333) or **Jonathon Beard** (email: jbeard@fluxmans.com; tel: +2711 328 9384).

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Peer-to-Peer Lending

For the purposes of the following, 'peer-to-peer lending' means lending by individuals to businesses or other individuals where an online platform is used to match lenders with borrowers.

South African Regulation of Equity Crowdfunding and Peer-to-Peer Lending – Provided for information purposes only and not intended to constitute legal advice.

1. Has your country introduced specific legislation or regulations governing peer-to-peer lending, or is it regulated under generally applicable laws?

Peer-to-peer lending is not specifically regulated in South Africa. However, there are pending amendments to certain acts that could expressly regulate peer-to-peer lending. The Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS) may be applicable and has pending amendments that would bring peer-to-peer lending more squarely into its ambit. The Electronic Communications and Transactions Act 25 of 2002 (ECTA) may also apply where peer-to-peer lending is facilitated through the use of cryptography services. In addition, the National Credit Act 34 of 2005 (NCA) is likely to apply should a platform match lenders with borrowers in order to facilitate unsecured loans.

2. If your country regulates peer-to-peer lending, what are the names of the government agencies responsible for regulating it?

To the extent that the NCA applies, the National Credit Regulator and National Consumer Tribunal will regulate peer-to-peer lending. Should FAIS apply, the Office of the Ombud for Financial Service Providers will regulate peer-to-peer lending, while the registrar so named in FAIS will also have certain assigned regulatory powers.

3. Are there any limits on the amounts that can be lent?

To the extent that the NCA applies, the amount lent may be limited in that it cannot be more than the borrower can afford to pay back. In this regard, an affordability assessment must be conducted and credit extended in line with the result of this assessment. In the event that this assessment is not conducted, the extension of credit by the lender may amount to reckless lending as defined in the NCA.

4. Are there any restrictions on the types of persons who can lend and/or borrow, or restrictions on the rate of interest that can be charged?

If the amount lent exceeds ZAR 1 million and/or the lender regularly lends money to others, the lender may have to be registered as a credit provider in terms of the NCA and would not be entitled to lend in this scenario if this formality has not been complied with. In addition, the borrower would only be entitled to borrow money in terms of the NCA if an affordability assessment has been conducted and the borrower can legitimately afford to pay back the amount lent.

Moreover, a credit agreement may often require consumers to pay service fees, initiation fees, collection costs, cost of credit insurance and administration charges, in addition to interest. Section 103(5) of the NCA provides that the aggregate or sum total of such amounts (as contemplated in sections 101(1)(b) to (g) of the NCA) may not exceed the unpaid balance of the principal debt under that credit agreement as at the time that the default occurs.

The maximum amount that may be charged in fees or interest on a credit agreement is limited to the

amount as decided and proclaimed by the Minister in the government gazette from time to time. In any event, in terms of South African common law, the amount of interest may not amount to double the capital amount lent.

5. Is there any requirement for the online platform and/or the lenders to be licensed or registered or to comply with any particular rules?

If the online platform is merely facilitating deals between lenders and borrowers, then the platform must comply with the registration requirements of FAIS. To the extent that FAIS applies, the lender must be registered as a financial services provider.

In the event that the lending is facilitated by providing cryptography services, the lender would have to be registered as a cryptography provider with the Minister of Communications in South Africa.

Insofar as the NCA applies as detailed above, the lender may have to be registered as a credit provider.

6. Are there any requirements applicable to marketing and promotional documents and activities?

The NCA places restrictions on the types of marketing practices that may be conducted in marketing credit agreements. In this regard, a platform seeking to facilitate agreements may not use negative option marketing and must offer an opt-out function in all unsolicited communications.

This opt-out requirement is similarly set out in section 45 of the ECTA and section 11 of the Consumer Protection Act 68 of 2008 (CPA).

7. Are there any particular consumer protection provisions that apply?

There are certain provisions that may apply as outlined roughly above under FAIS, the NCA and the CPA. These provisions impose limits on intermediaries, the types of credit agreements that may be concluded and the marketing thereof.

9. Please provide any additional information you feel is important to understanding the regulation of peer-to-peer lending in your country.

The scope for conducting true peer-to-peer lending in South Africa is limited. In practice, an entity considering moving into this space will need to explore all of the potential legislative restrictions as highlighted above.

10. Please identify a point of contact at your firm for enquiries related to peer-to-peer lending.

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