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Crowdfunding: Requirements under Swiss law

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Introduction

Crowdfunding has become more popular in recent years, and Switzerland has not been left out with respect to its expansion. Put in simple words, crowdfunding is a term to define collecting money from many sources to finance projects.

Typically a large number of investors, each of whom provide an amount (often quite small) to the project developer who publishes the project on a designated online crowdfunding platform. Potential investors interested in a project have the opportunity to support it through the platform. Thus, the crowdfunding platforms have a linking function between the investors and the project developers.

Swiss financial markets legislation is designed as a technologically neutral regulation. As a consequence, there are no specific rules for crowdfunding activities.

Depending on how business models concerning crowdfunding platforms are set-up, some parts of the procedure may be covered by financial market regulations and by private law provisions. Thus, participants of crowdfunding business models may be subject to license requirements and to the prospectus requirement. Participants of a crowdfunding business model (such as investors, crowdfunding platform providers, project developers, and escrow agents (if any)) need to verify separately if they require a license and if they are subject to the prospectus requirement before launching their activities.

Four types of Crowdfunding

There are mainly four crowdfunding types. The main criterion to distinguish these types of crowdfunding is the return that the investors receive for their funding of a project. In a nutshell, the four types of crowdfunding are:

- Crowdlending: With the crowdlending model, loans are granted by the investors to the project developer (borrower) under the condition that the loans are paid back and, as a rule, that a compensation be paid (typically in the form of interest).

- Crowdinvesting: Crowdinvesting is a form of corporate financing, whereby the return shall be a participation in the company's success. In contrast to crowdlending, equity is granted. This financing form is often used by start-ups.
- Crowddonating: With the crowddonating model, the investors do not expect a repayment or a return.
- Crowdsupporting: With the crowdsupporting model, the investors reject a repayment and get a return in form of products or services.

License requirements

Bank

Taking of deposits from the public

The taking of more than 20 deposits from the public on a professional basis is, in general, subject to a banking license, issued by the Swiss Financial Market Supervisory Authority ("FINMA") and their subsequent supervision. Whenever received funds of the investors (project financers) are collected and booked on the accounts of the platform providers, the project developers, or any escrow agent (as the case may be), must verify whether such activity qualifies as taking deposits from the public. In this respect, it is worth mentioning that the advertising for funds may also qualify as such activity.

Reduced legal barriers in the Banking Ordinance

On 1 August 2017, the partially revised Banking Ordinance ("BO") entered into force, relating to financial technology (fintech) (regarding these amendments, please refer to our Newsletter of May 2017: 'New Fintech Regulations: Amendment of the Banking Act and the Banking Ordinance'). Since 1 August 2017, the execution period for settlement accounts is extended to 60 days; the earlier FINMA practice was seven work days. If the booking of the received funds on the accounts of the platform providers, the project developer, or any escrow agent qualifies as acceptance of deposits from the public (this is subject to discussion in the doctrine), the collected funds may be held for 60 days (no longer seven days) on their own accounts without qualifying as a bank. Therefore, this amendment is expected to be useful for crowdfunding platforms. Furthermore, since 1 August 2017, a banking license is no longer required if the funds accepted, coming from more than 20 investors for forwarding do not exceed CHF 1 million, and provided that the other requirements are met (i.e., the deposits are not re-invested, no interest is paid unless the main activity is commercial and/ or industrial, and the information duty is fulfilled). This amendment (so-called 'Sandbox') is expected to be less useful for crowdfunding activities than the extended period for settlement accounts because crowdfunding business models often intend to collect more than CHF 1 million.

Draft of the partially revised FINMA Circular 'Public deposits with non-banks'

FINMA is clarifying the two amendments of the BO, mentioned above, in its Circular 'Public deposits with non-banks'. On 1 September 2017, FINMA published the draft of the partially revised Circular. Regarding the extended period for settlement accounts, this draft determines,

inter alia, that registered securities dealers are not constrained by the 60-day settlement deadline and that this exemption for settlement accounts covers business models that involve forwarding, such as crowdfunding or money transmitting. The consultation procedure was closed on 16 October 2017, and the partially revised Circular will be published at the end of 2017 or at the beginning of 2018.

Collective Investment Schemes

Depending on how a crowdfunding business model is set-up, a license requirement by FINMA under the Collective Investment Schemes Act ("CISA") may be triggered.

In this respect, the key question is whether the collected funds are subject to an external administration of the account holder of the collected funds (i.e., the platform providers, the project developers, or any escrow agent). If that is the case, such activity generally requires a FINMA license under the CISA.

Financial Intermediaries

Any of the participants of the crowdfunding business model who collect and book the funds on their own accounts (i.e., whether the platform providers, the project developers, or any escrow agent) qualify generally as financial intermediaries because they constitute a payment transaction service and are, therefore, subject to anti-money laundering provisions, as long as they render professional services. As a consequence, they must comply with the duties of due diligence and the duties to report to the Anti-Money Laundering Act ("AMLA"). Furthermore, they must either become a member of a self-regulatory organisation (SRO) recognised by FINMA or obtain a license from FINMA as a directly supervised financial intermediary (DSFI) if they are not required to obtain a banking license.

The obligation of compliance with the AMLA provisions is generally not a substantial barrier to entry into the crowdfunding market.

Consumer Credit

If private persons take out loans through crowdlending platforms, which cannot be attributed to their professional or commercial activity, the Consumer Credit Act ("CCA") may apply, unless the single loan amount exceeds CHF 80,000 (which is normally not the case). As a consequence, a license is required for the lender (investor), and that can be a private person or an entity. Thus, lenders which grant loans through crowdfunding platforms without a license, are exposed to a risk to be liable for prosecution. This risk also exists for the respective platform providers unless they have a license as credit intermediaries. Furthermore, a credit assessment needs to be carried out, and the loan agreement must comply with some formal requirements.

Further license requirements

As a general rule, crowdfunding business models do not qualify as securities dealer, financial market infrastructure or insurance, and are therefore not subject to further license requirements by FINMA. These license requirements, however, also must be verified on a case-by-case basis before launching the crowdfunding business activities.

FINMA's Investigations

FINMA determined, in its Fact Sheet 'Crowdfunding' from 1 August 2017, that it will launch investigations if it receives specific information indicating that an activity relating to crowdfunding is being conducted without FINMA authorization, membership of an SRO, or holding a DSFI license.

Prospectus requirement

The Swiss Code of Obligations provides for a prospectus requirement for companies (issuers) that offer publicly owned shares or bonds for subscription. Where this prospectus requirement is not met, any person involved is liable to the acquirers of such securities for the resultant losses.

The prospectus requirement is relevant in terms of the crowdinvesting, and, depending on how a business model is set-up, it may also be relevant for crowdlending activities. If the business model provides for an offer for a subscription that is not directed to a limited number of persons (e.g., through register barriers), generally the prospectus requirement is triggered and needs to be complied with to prevent liability risks (also, regarding the platform providers). Furthermore, crowdfunding activities also need to comply with the prospectus requirement of the respective foreign jurisdictions, which are targeted by the platform.

Draft Financial Services Act and Financial Institutions Act

The drafts of the Financial Services Act ("FinSA") and of the Financial Institutions Act ("FinIA") are part of the new regulatory laws and were issued by the Federal Council on 4 November 2015. The FinSA and the FinIA will most likely enter into force in the course of 2019 (at the earliest). In relation to the regulatory requirements, the current drafts of the FinSA and the FinIA do not remove the above mentioned main barriers for crowdfunding activities.

Concerning the prospectus requirement, the draft FinSA, however, contains some exceptions to the prospectus requirement (e.g., the offer goes to less than 150 investors that qualify as private customers; it has a minimum division of CHF 100,000; and it does not exceed CHF 100,000 during a twelve-month period) that could be useful for crowdfunding business models. Furthermore, the draft FinSA authorizes the Federal Council to specify relaxations of the prospectus requirement for issuers, which do not exceed two of the following thresholds in the last business year: (i) balance sheet total of CHF 20 million; (ii) turnover of CHF 40 million; and (iii) a yearly average of 250 full-time. If the Federal Council uses this legislative power, this will have a positive effect for certain crowdfunding business models that involve SMEs as issuers.

In addition to the prospectus requirement, the draft FinSA requires creating a basis information sheet under certain circumstances before a financial instrument is offered to private customers. It will need to be verified on a case-by-case basis whether this requirement applies for the respective crowdfunding business model.

Conclusion

Crowdfunding business models may trigger several regulatory requirements. The main barriers for crowdfunding may be the requirement of a banking license and the requirement of a license under the CISA. It may happen in practice, therefore, that some crowdfunding platform providers collaborate with licensed banks. In this context, the new regulatory changes in the BO are to be welcomed for crowdfunding business models. Also, it may be accepted that the FinSA's entering into force may have a positive impact on some crowdfunding business models. However, in this new fintech area legal uncertainty still exists. Therefore, it is to be hoped that FINMA will continue to clarify its practice and that the focus remains to reduce further still existing market barriers on a political level to strengthen the competitiveness of the Swiss crowdfunding market (and the 'fintech market' in general).

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