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Cite this article as:

MS. BHAVYA CHOUDHARY, "*Equity Crowdfunding: A Review Article",* Vol.3 & Issue 4, Law Audience Journal (e-ISSN: 2581-6705), Pages 166 to 176 (26th March 2022), available at ***https://www.lawaudience.com/equity-crowdfunding-a-review-article/.***

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Name of the Author: *David Groshoff.*

Title of Article: *Equity Crowdfunding as Economic Development.*

Citation: *38 Campbell L. Rev. 317 (2016) (48).*

I. AUTHOR'S THESIS AND PURPOSE:

David Groshoff analyses the equity crowdfunding as a part of economic development. The author analyses in detail the JOBS Act and argues that until there is a complete implementation of the JOBS Act, the penalty will still accrue on startup enterprises, specific investors and probable employees. The Article first gives the background of the JOBS Act by concentrating on law and economic development and crowdfunding as a means of economic development. Then the article goes on to explain the meaning of equity crowd-funding and a brief overview of securities law along with the fraud and the oversight to overcome the fraud in crowd-funding. The article also compares different sites of crowdfunding and the regulatory measures to get the best result of crowd-funding with regard to economic development. The article argues that as the securities law is broad based nature any country was to pass a stringent law regulating equity crowd-funding, the nature of it being interstate would then stand to be questionable. Finally, the article concludes by stated that proper regulatory measures is the need of the hour to protect the Country's economy from facing economic uncertainty.

The main purpose of the article is to see whether equity crowdfunding can be seen as a means of economic growth in a country. The article gives an idea to the readers that equity crowdfunding is derived from the field of law and development economics. The first part provides the history of development economics while the second part gives the history and background of microfinance and analyses the regulation. The article further blends law and economic development with microfinance and equity crowdfunding. The second part of the article gives a brief background of the JOBS Act and the meaning of equity crowdfunding in the context of both law and economics. It goes to highlight the fears on the part of the

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investor in equity crowd-funding. The article goes on to compare all the websites designated solely to equity crowdfunding. The author explains in detail the advantage of regulation. The registered investors, broker dealers and crowdfunding portals are capable entities by whom crowdfunding websites are handled. The fourth part analysis in detail the proposed alternative for existing equity crowdfunding business. This part attempts to cogitate on some potential alternatives of crowdfunding. The article finally concludes by saying that equity crowdfunding remains one of the important sources of economic development which is needed for market growth. Though there is regulation A+, there is still a need for final rules under Title III of the JOBS Act.

II. THE MAIN IDEAS:

The foremost idea of the article is to fully implement JOBS Act and to connect equity crowdfunding to economic development. The author argues that even if a country passes a robust equity crowdfunding law, the interstate nature of the law makes the law questionable. The article has further highlights that the SEC's delay in finalizing rules under Title III of JOBS Act has hindered the bipartisan bill and it has caused confusion, frustration and lost business opportunities. The author suggests the potential alternative to Title III of the JOBS Act is to rely on other promulgated rules such as regulation A+.

III. DESCRIPTION OF THE ARTICLE AND INTERPRETATION:

The article first starts to explain why the author thinks that equity crowdfunding is derived from field of law and development economics. Therefore, firstly it describes the history of development economics and pronounces microfinance as a bridge between development economics and equity crowdfunding. The need for capital to develop the business and the need for fundamental arrangements to lead to economic development leads the author to believe that there is a relation of equity crowdfunding with the law and development economics. The article also proclaims that all sorts of crowdfunding is derived from microfinance which assists both entrepreneurs and micro-entrepreneurs and helps increase social mobility and living standard. It also helps to reduce agency costs. The author of the article gives a wider interpretation of microfinance to enlarge financial access to lower-

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earning people and that is why the article uses 'equity crowdfunding' to elaborate upon 'investment crowdfunding'. The article also gives enough proof to suggest that micro finance does not give a harmful outcome on economic development. It does not in any way exceeds the cost of the society or funds of the government. The author treats microfinance and crowdfunding as an economic development system regardless of the fact that it is a developed country or a developing country. The article proposes to provide a regulatory framework that would make it more fruitful. The article also gives evidence to show that the microfinance industry cannot reach its full potential until MFIs are regulated and supervised prudently.

The author gives evidence as to how regulation has helped over years to generate economic growth. Therefore, the author synthesizes law and economic development with microfinance and equity crowdfunding. Until the investor is made to come under the securities rules and regulations, equity crowdfunding remains exclusive and therefore, ineffective. The JOBS Act itself stated that SEC was required by law to promulgate rules regarding the crowdfunding by the year end of 2012. But SEC has already missed the deadline long before. The next part gives a brief background of the JOBS Act and defines the meaning of equity crowdfunding in the context of both law and economic development. The author does not limit equity crowdfunding to equity. The author takes it as a new and evolving method to raise money. Fraud is considered to be the biggest threat to crowdfunding and therefore it is suggested that transparency and centralized nature of crowdfunding portals will make the commission of fraud tougher. The author mocks and states that SEC has done nothing to protect the investors.

The next part takes into consideration the probable alternatives to move towards equity crowdfunding which promotes economic development and growth. The crowdfunding websites should be operated by registered investment advisers, broker dealers and crowdfunding portals. The article deals in detail about the procedures of being registered investment advisers, broker-dealers and crowdfunding portals. These portals, advisers and dealers have to get registered with SEC and consequently, the proposed funding portal has to face various regulatory and flexibility issues. The last part attempts to consider some capable

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alternatives for placing equity crowdfunding rules in final form. The article concludes by saying that equity crowdfunding remains one of the important sources of economic development which is needed for market growth. Though there is regulation A+, there is still a need for final rules under Title III of the JOBS Act. The article argues that as the securities law is of broad-based nature and if any country passes a stringent law regulate equity crowdfunding, the nature of it being inter-state is questionable. Finally, the author concludes by stating that proper regulatory measures are the need of the hour to protect the Country's economy from facing economic uncertainty.

IV. CONCLUSION:

The author has mainly considered equity crowdfunding as a method of economic development. I agree with the view of the author that equity crow funding is a method of economic development. Finally, the article concludes by stating that proper regulatory measures is the need of the hour to protect the Country's economy from facing economic uncertainty.

V. INTRODUCTION TO CROWDFUNDING:

Crowdfunding has spread like wildfire over the last few years. Much of the crowdfunding phenomenon remains concentrated in the U.S. and Europe where the large majority of crowdfunding platforms are found. However, crowdfunding emerged into a world with existing regulations and confusion still reigns over how the rules should be applied. This confusion may impede the development of crowdfunding and may have threatened to temper the benefits of this new financial tool. The Security Exchange Commission defines crowdfunding as "a new and evolving method to raise money using the Internet." Crowdfunding involves three participants: the crowd (or contributors); a crowdfunding platform; and the crowdfunding campaign creator. Crowdfunding[1] is the process of collecting or raising money by any startup through investors on an online platform. Here, the investors are unknown. Money is raised in the form of debt, equity and donations. It is a process where

[1] Ms. V. Akalya, A Study on Crowdfunding in India, International Journal for Research in Engineering Application & Management (IJREAM), available at file:///D:/College/Research%20papers%208th%20Semester/Corporate/IJREAMV04I1046129.pdf, last visited 12/02/2022.

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the investors invest a small amount of capital and expect high returns. This has made crowd-funding a secure option for raising capital. Among the various methods of fund raising, this tops the list of priorities for startup companies.

Crowdfunding platforms are categorized into four types. They are as follows:

Donation-based crowdfunding:

In this kind of crowdfunding, funds are raised for charitable organizations, non-profit organizations and disaster reliefs. From a large number of people, small amount of donation is collected. The investors invest the amount without expecting anything in return towards a social cause. It is no profit no loss deal.

Reward-based crowdfunding:

In this kind of crowdfunding, the investors are given an award for their investment. This is a kind of token offered from the company to the investor in the form of a service or product. It is also a way to attract investors to invest their money and get a reward as an incentive. The investors do not receive any financial return for the investment made.

Debt-based crowdfunding:

It is a method of collecting amount via online means. Companies can apply for debt on these platforms. There is an online application for raising funds which includes the company's interest rate along with the risk involved in the securities and the bond. In this kind of crowdfunding, investors get interested on unsecured loan. The investor can get back the interest after a fixed period by the company.

Equity-based crowdfunding:

In this kind of crowdfunding, the investors receive equity shares of the company for the money invested. They receive the equity shares as reward and they also receive a share of profit as a dividend. The investors are more exposed to risk in these kinds of investments in unlisted companies.

Each nation has its own set guidelines with respect to the ventures through these crowdfunding stages. Prize and Donation based crowdfunding are not identified with monetary profits so there is no possibility of a loss of speculation. These are known as network swarm financing. Value and Debt based group subsidizing face danger from the

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deficiency of capital, guarantee monetary degrees of profitability. They are known as equity-based crowdfunding. Financial specialists from this stage focus on returns once the organization builds up themselves and appreciates benefits.

VI. CASE STUDY: CROWDCUBE IN 2014[2]:

CrowdCube is among the best value funding sites in the U.K. CrowdCube exploits the plan exception that include raising support exertion under 5 million that elaborate less than 150 non-qualified financial specialists and quite a few qualified speculators. Information was gathered from the CrowdCube site about group subsidizing efforts that effectively shut in the plan year 2014. Subsequently, the contextual analysis centers around fruitful missions. CrowdCube doesn't keep data pretty much all effective missions on their site either, which makes a determination predisposition. In their yearly report, CrowdCube affirms that they subsidized 105 organizations out of 320 ventures in 2014 and gathered about £35 million. The data gathered was of around 72 organizations that raised 74 percent of these assets.

One organization was dispensed with in light of the fact that it offered no obvious value (just rewards) and three organizations since they fund-raised through securities rather than value. 68 organizations, or 66% of the organizations that effectively brought reserve through CrowdCube up in 2014, stay in the information examination. The dataset contains the name of the organization, the contribution particulars (sort of offers, value, sum focused on, capitalization offered, sum gathered, capitalization in truth, number of financial specialists, most noteworthy speculations), and other data about each organization. The information is gathered with publicly accessible information about each organization from the United Kingdom government's information base. To contrast with the dynamic organizations' dissemination, business segment information from the U.K. Office for National Statistics is utilized. Zeroing in on missions, 68 organizations offered on normal £191,000 for 12.24% of value however raised on normal £278,000 for 16.75% of value. The vast dominant part of organizations took into account overfunding prompting a normal overfunding: these

[2] Garry A. Gabison, Equity Crowdfunding: All Regulated but Not Equal, 13 DEPAUL Bus. & COMM. L.J. 359 (2015).

organizations found the middle value of raised 146% of the underlying capital advertised. From a game hypothesis outlook, this overfunding perception appears to be in accordance with the motivating forces made by the win or bust model that CrowdCube utilizes: a business visionary gets the assets just in the event that he arrives at a pre-determined limit; thus, business people are boosted to bring down the edge from what they need or need to what they can reach. Overall, 142 speculators put resources into each venture (with a huge standard deviation). By and large, 22.1% of the capital was raised. Past crowdfunding, the writing talks about how the main ventures regularly come from loved ones. Business visionaries may get these huge assets from their loved ones to kick off the cycle. Organizations that utilize crowd-funding are moderately youths. The most youthful organization was a month old (Quiz the Nation) and the most seasoned was twelve years of age (Bookbarn International).

By and large, each organization has less than one credit. Moreover, the majority of these organizations are little: five representatives overall. In this way, it appears to be that value crowdfunding draws in new businesses. A more intensive glance at the organization dispersion across areas shows that 12 assembling organizations, 12 discount organizations, 39 administrations organizations, and 5 organizations that fall outside these areas (development and cultivating) effectively raised assets. The 2013 FCA guideline zeroed in on financial specialists. The speculation per organization likewise expanded from about £175,000 to about £214,000; however, the degree of overfunding remains basically the equivalent. This perception shows that organizations didn't adjust their technique to under-request to arrive at the edge. The U.K. guideline opened speculation to another arrangement of financial specialists who didn't beforehand contribute. While it can't be seen where the assets come from, the guideline appears to have a freeing impact on the sum contributed per individual.

Thus, the sum raised per organization likewise expanded; this expansion might be because of raising more assets from every person just as more financial specialist per crusade. At the end of the day, explaining guidelines may have legitimized the group subsidizing practice and appears to have dis-hindered venture conduct: per speculation, more individual contributed

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(40% expansion) and every speculator contributed more (around 30% increment). Speculators appear to turn out to be surer. Further examination might have the option to distinguish whether speculators in group financing are people that didn't contribute beforehand. Strangely, swarm subsidizing has likewise pulled in the consideration of conventional speculators like funding organizations. This might be proof that guidelines have legitimized crowdfunding and urged conventional financial specialists to likewise make the most of these chances. It stays muddled what the effect will be on the assets accessible for speculation.

VII. CURRENT SCENARIO IN INDIA:

Crowdfunding is something that is known to India since years. We have always been donating '*beekh*'or '*chanda'* for socio cultural cause and to receive blessings of God. However, the procedure of crowdfunding being on an online platform is quite unknown to Indians[3]. Crowdfunding is at present at the puberty stage and is still facing a lot of problems in India. There are no appropriate rules and regulation for the same. Therefore, the commission of fraud is very probable. Also, there is no transparency which might lead to risk for the investors, and crowd-funding will result in a big failure. As said by author David, equity crowdfunding is a source of economic development, and India being a developing country must abide by it and bring proper regulations for crowd-funding.

The legislators noticed the need for regulation and therefore, the Securities and Exchange Board of India came up with a consultation paper on crowdfunding in 2014 admitting the need for the same.[4] SEBI stated that "*solicitation of funds (small amount) from multiple investors through a web-based platform or social networking site is crowdfunding*". The consultation paper proposed to put restrictions on who can be crowdfunding investors. The paper referred to the UK, US laws and came out with the same. SEBI has proposed the qualification to be a crowdfunding investor. SEBI will permit private position offers through web-based crowdfunding stages to quite a few Qualified Institutional Buyer (QIBs) and a

[3] Ibid.
[4] Jitendra Soni and Kanad Bagchi, Crowdfunding in India A Tale of Misplaced Regulation, available at file:///D:/College/Research%20papers%208th%20Semester/Corporate/24481069.pdf, last visited 12/02/2022.

limit of 200 High Total assets Individuals (HNIs). By and large, QIBs should hold at least 5% of the protections given and an organization will be needed to buy at least multiple times the min offers worth per individual. A high-net-worth individual is needed to buy in any event 3 times the base offer worth per individual. Additionally, for a retail speculator, the all-out of all interests in crowdfunding in a year ought not to surpass 10% of their net worth. Aside from these, there are sure conditions that an certify speculator should meet. As the speculation will be done through Demat, the speculators should hold a Demat account and the installment must be made through a DD or cheque. Installments with Cash or Credit Cards are not approved. Additionally, an individual may be qualified as a speculator, they are an Indian resident or an NRI.

A beginning phase startup or SME which is an unlisted public organization consolidated in India is qualified to raise crowdfunding on the off chance that they meet after measures.

- The organization meaning to raise capital must not surpass Rs. 10 Crore in a time of a year.
- An organization that is not advanced supported or identified with a mechanical gathering has a turnover in an abundance of Rs. 25 Crores.
- An organization that has no record on any trade.
- An organization that is not over 4 years of age.
- An organization that does not own land and also, does not perform anything which is not allowed under the mechanical arrangement of the Government of India.
- The organizations ought not haves chiefs, advertisers or partners referenced as a 'defaulter' or a 'willful defaulter' by RBI or CIBIL.

Aside from these, SEBI likewise expresses that an organization needs to raise crowdfunding ought not rundown on various crowdfunding stages. The organizations ought to obligatorily course all crowdfunding issues through a SEBI perceived Crowdfunding Platform. The organization keen on crowdfunding ought to likewise give arrangements to oversubscription. Among other conditions, the backers won't have any single financial specialist holding over 25% stake in the organization and the promoters will be needed to keep up at least 5% value stake in the organization for in any event 3 years[5]. The crowdfunding stages in India are as yet attractive and have far to go till they arrive at the status asserted by unfamiliar crowdfunding goliaths like Kickstarter, Indiegogo, and so forth Because of the prohibitive confirmation strategy of the majority of these unfamiliar stages, they are generally disconnected to maturing Indian new companies.

In the later piece of 2016, more than 20 crowdfunding stages were considered 'illegal' by SEBI. Prize based and Donor based stages actually work, while equity-based crowdfunding has seen a ton of investigation from SEBI. SEBI reported that it is examining crowdfunding guidelines and might soon even frame a legitimate system permitting equity crowdfunding.

VIII. SUGGESTIONS:

Internet based crowdfunding should be encouraged. The platforms should follow all the regulatory guidelines necessary. Transparency should be there and there should be full disclosure on the website itself. The platform should collect the money from the investors and give it to trusted startups and businesses. The startups and businesses must be registered in order to gain the amount. All the documents required must be submitted to the platform. Also, A chat window should also be provided within the platform to clear all the doubts of the investors before investing and for knowing the company well before investing. Adding to this, Section 42 of the Companies Act must be amended for the smooth functioning of crowdfunding in India. It is considered to be a good method of economic growth and therefore, India should come up with a legal regime for it.

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[5] Ethan Mollick, The dynamics of crowdfunding: An exploratory study, Journal of Business Venturing, 29 (2014) 1–16.

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