Where are they now?

A report into the status of companies that have raised finance using Equity Crowdfunding in the UK

November 2015
Nabarro is delighted to be able to support AltFi Data in the delivery of this report.

Crowdfunding is a key growth area for the funding of small and medium sized enterprises in the UK. Access to capital has traditionally been an extremely difficult challenge for start-up companies to face. Even with a large number of angel investors in the UK market, achieving a fully funded investment round was time consuming, clunky and often the result of luck, as opposed to access to the right people.

Crowdfunding has revolutionised that process. It allows a broader range of people, from full-time professional angels to those with a small amount of capital to deploy, to engage in the investment process and share in the success of the UK’s growing entrepreneurial community.

Nabarro has acted on the creation and structuring of a number of crowdfunding platforms. We are extremely proud of the fact that we have been able to add to this market.

We have not yet been able to see the results of this work and how it will pan out over the long term. However, this report goes a great deal of the way towards understanding what that might look like in the future, and what success has been had to date. We look forward to discussing the report, and what it means for the future of Crowdfunding, with you all.
It is impossible to dispute the notion that equity crowdfunding is having a hugely positive effect on the ability of small companies to access finance. The press is filled with stories highlighting the amount of capital that young companies have raised, as well as flagging realisations and other positive developments. However, are investors aware of the risks that an equity investment in a young company entails? In fact, does anyone even have an accurate picture of what has become of the 450+ companies that have crowdfunded to date?

This report has been conducted with the aim of exploring the returns that investors are experiencing in this space. The results are impressive. Over 80% of the companies that crowdfunded between 2011 and 2013 are still trading. Of these, many have raised further capital at higher valuations and one has even realised a return for investors. This ranks alongside an October 2014 report by the insurer RSA that found that 55% of UK Small and Medium sized Enterprises (SMEs) did not survive five years. Similarly, a 2009 report into Angel Investments by Nesta “Siding with the angels” found that “fifty six percent if exits failed to return capital”

However, the results also suggest that transparency within the sector could be improved. This would ensure that investors are given every opportunity to understand the risks inherent in buying shares in young companies.

**Some Headline Statistics**

367 companies

431 Capital raises

29 ‘red’
41 ‘amber’
302 ‘green’
58 ‘Green Plus’
1 ‘realisation’
Research Rationale

This research project was conceived to address a lack of available information as to what happens to companies after they have completed a successful equity crowdfunding campaign.

Establishing a track record is central to the evolution of any emerging asset class. When considering the track record of an asset class, what is really meant is the return it offers to investors. Crowdfunding platforms are beginning to offer some means of tracking past campaigns. However, there is no centralised resource for such information and no consistency of reporting. Due to the long term nature of equity investment returns, it will be some years before firm conclusions can be drawn. Nonetheless, the four years of data at our disposal is sufficient to allow initial insight into successes and failures. This report aggregates this data to give an overview of the success rate to date.

On top of establishing a track record for the asset class, identifying the success rate of past campaigns should be a critical part of the appraisal that any investor should make before investing in crowd sourced equity. The Nesta report 2014 identified that 62% of crowd funding investors “described themselves as being retail investors with no previous investment experience”. It is therefore extremely important that investors are assisted in understanding the risks entailed in early stage equity investment by being made aware of the success/failure rate of companies that have previously raised finance through crowdfunding platforms.

Equally, the investor should be given the opportunity to perform a rudimentary test of a platform’s due diligence. Whilst any investor is expected to perform their own analysis of a campaign, any information made available can be supplemented by an understanding of how many campaigns funded to date have subsequently failed.
**Report Objectives**

This report has two objectives:

- To make an accurate and up to date appraisal of the current status of companies that have raised finance using equity crowdfunding in the UK.
- To make recommendations for best practice that, in our view, would serve the long term interests of the industry.

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**Report Scope**

This report surveys the companies that have raised equity finance on the most significant online platforms based on origination volume since the industry began in 2011:

- Crowdcube
- Seedrs
- SyndicateRoom
- Venture Founders
- CrowdBnk

- This report has tracked every campaign funded through the above platforms since the industry's inception in 2011 until June 30th 2015.
- The status of each campaign was reviewed as at 30th September 2015.

That amounts to 431 equity crowdfunding rounds by 367 companies.

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**Crowdcube**

Crowdcube: “Crowdcube is the world’s leading investment crowdfunding platform. We enable anyone to invest alongside professional investors in start-up, early stage and growth businesses through equity, debt and investment fund options.”

Crowdcube was the first equity crowdfunding platform to launch in the UK, and now claims a 200,000 strong crowd as well as the largest amount of capital successfully raised.
Seedrs: “We let all types of investors invest in businesses they believe in and share in their success. We let all types of growth-focused businesses raise capital and business community in the process.

We do all of this through a simple, highly professional, online process that protects and empowers investors while helping businesses grow and generate returns.”

Seedrs offer a unified nominee structure for their investors aimed at increasing investor protection and streamlining the process for crowdfunding companies.

SyndicateRoom: “We allow you to invest in companies backed by professional investors.

While many online investment platforms have sprung up, at SyndicateRoom we have developed a unique model with benefits you can’t find anywhere else.

Here’s why: we only list companies that are already backed by professional ‘business angels’, who are investing their own money and thus have taken an active role in evaluating the strength of the deal. We then offer our members the ‘same share class and same price per share’ if they decide to invest alongside these professionals.

We believe this curated and transparent approach allows our members access to a more sophisticated set of investment opportunities.”

SyndicateRoom has recently announced that it will switch to a nominee structure, similar to Seedrs.

VentureFounders: “With a solid foundation in financial services expertise, the VentureFounders team is comprised of FCA approved, highly skilled investment professionals with extensive private equity, investment management and business growth experience.

What sets us apart is the thorough approach we take. We seek out ideas that excite us, leaders we believe in and numbers that stack up. We then apply expert due diligence to qualify and interrogate the true investment opportunity before we present it to our investors.”

VentureFounders is another platform to use a nominee structure.

Crowdbnk: “CrowdBnk is an investment crowdfunding platform that allows you to invest in UK businesses through equity and debt.

CrowdBnk provides every registered investor with full access to businesses that pass our selection criteria and make it through our rigorous due diligence process, we call it the CrowdBnk Bootcamp.”
Industry context

Equity crowdfunding has had a significant impact on the accessibility of growth capital to young UK companies. According to the Liberum AltFi Volume Index, the sector has advanced over £190m of equity capital to growing UK companies since 2011. Thanks to a compound annual growth rate of over 129%, the sector is on track to raise close to £140m in 2015 alone and is becoming an increasingly meaningful part of the SME funding landscape.

Figure 1 shows the growth of the industry by platform. Note that the grey bars reflect the volumes funded beyond the scope of this report, as well as an extrapolation of the current growth rate through to year end 2015.

Increased Sector Diversity

Alongside this growth there are also signs that the reach of equity crowdfunding is growing.

The size of crowdfunding campaigns is increasing

One of the benefits of a crowdfunding raise to a growing company is the brand champions that are created by recruiting a number of small investor supporters. Investors have a powerful “word of mouth” impact on the brand of the relevant company and the very act of posting the campaign on a crowdfunding platform may also attract useful publicity for the company. As such it stands to reason that the most compelling logic for an equity crowdfunding campaign is for consumer discretionary companies.
It is interesting to observe the other sectors which have also begun to participate.

Whilst consumer discretionary companies dominated the equity crowdfunding scene in 2011 and 2012, the last three years have seen a significant broadening as energy, healthcare, technology, financials, media and utilities have also begun to participate. Many of the financials companies are in fact platforms within the wider peer to peer (P2P) and equity crowdfunding universe. When we consider this it becomes clear that the same profile raising benefits may also be an attraction for at least some of these sectors. Certainly, technology, media and the type of financial companies being funded, would all seem likely to benefit from the marketing opportunity that crowdfunding can bring.

Increased Size

The second sign of growing reach is the increasing size of campaigns that are being funded through crowdfunding platforms.
Across all major current platforms there is a trend towards larger campaigns. Interestingly, the current status of companies that have been crowdfunded, as explored later in this report, suggests that companies that raised larger amounts have a better success rate. The rising average size is also symptomatic of platforms achieving larger raises, both through impressive valuations and funding larger companies.

There is a perception that all companies that use crowdfunding as a means of accessing capital are startups. Whilst this is true for some, the majority of companies have been established for several years prior to crowdfunding. Using Companies House dates of incorporation, the average age of companies that raised funds from the crowd in 2015 was 3.32 years. The oldest...
company ever to crowdfund had been incorporated 37 years at the time of the raise with the youngest being just a handful of days old.

The average age of companies at the time of their crowdfund raise has not changed significantly over the four years that the industry has been operating.

Generally companies that have been established for longer raise more money, however there are exceptions to this rule.

There is a difference in the average age of crowdfunded companies appearing on each of the crowdfunding platforms. Seedrs shows the greatest evolution in this respect. When the platform started out, funded companies had on average been going less than a year, very much seed funding as the name would suggest. In recent years the average age of companies raising money through Seedrs has increased and is now very similar to that of companies raising money on Crowdcube. Crowdcube, has maintained a steady average age of company at fundraise. The companies that fund successfully on SyndicateRoom have a higher age at fundraise than other platforms.

The average age of companies that raised funds from the crowd in 2015 was 3.32 years.
Headcount Increase at Crowdfunded companies

The benefits of the capital that has been raised through crowdfunding are clear to see. Good businesses with innovative ideas are getting access to capital that allows them the chance to flourish. Perhaps the clearest measure of this is increased headcount within these businesses. Around 25% of the companies we surveyed disclosed a change in headcount and of those the average increase after fund raises was 83%.

Delphi Score Analysis

The benefits can also be seen in the improved credit scores of companies post a fund raise.

Figure 8 plots in grey the monthly Experian Delphi score for each crowdfunded company. The average Delphi score for all campaigns is shown in the thicker blue data points. The data has been displayed such that the horizontal axis illustrates the months before and after the crowdfunding campaign with month zero being the month of the campaign. The average Delphi score improves significantly in the 24 months post fundraise.
Experian’s Delphi scorecard uses certain characteristics that are highly predictive in assessing rapid changes in a company’s trading position. These are:

- Average current days settlement beyond invoice terms
- Analysis of payments compared to the industry averages
- County court judgements in associated companies of the directors
- Worst consumer score of director (where use permitted)
- Insolvency events reported in London, Belfast and Edinburgh Gazettes
- Lateness of filing of financial statements
- Poor financial results
- Recent increase in credit applications tracked through previous searches.

### Industry Players

We have collected data to represent the current status of companies that have raised finance through these 5 following crowdfunding platforms:

<table>
<thead>
<tr>
<th>Platform</th>
<th>Founded</th>
<th>Equity Volume Funded to end September 2015 (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Crowdcube</td>
<td>2011</td>
<td>£93.3</td>
</tr>
<tr>
<td>Seedrs</td>
<td>2012</td>
<td>£36.0</td>
</tr>
<tr>
<td>SyndicateRoom</td>
<td>2013</td>
<td>£37.7</td>
</tr>
<tr>
<td>CrowdBnk*</td>
<td>2013</td>
<td>£8.2</td>
</tr>
<tr>
<td>VentureFounders</td>
<td>2014</td>
<td>£11.4</td>
</tr>
</tbody>
</table>

*Altfi Data estimate

However we have not included a breakdown of funds that have been raised through CrowdBnk and VentureFounders, due to the extremely limited sample size meaning that statistically significant trends within the platform’s fund raises are difficult to discern.
**Sector Specialisations**

Our research revealed an interesting sector breakdown between the platforms, which is suggestive of evolving specialties.

Crowdcube is dominant in the consumer discretionary segment. This is a reflection of the platform’s significant marketing spend and expertise which translate into a strong brand presence and the highest number of registered users – 200,000 at the last count.

A large position in financials demonstrates the impressive niche that Seedrs is building in the funding of P2P and equity crowd funding platforms.

Meanwhile, at SyndicateRoom there is a clear specialisation developing in healthcare technology. This may be a reflection of the platform’s geographical proximity to the research and innovation hubs around the University of Cambridge.

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**Figure 9 - Platform Sector Specialisations**
After collecting the data each company was assigned a status. The definitions used are listed below:

**Realisation**

Investors initial capital, plus a premium, has been returned after a successful exit.

**Green PLUS (Up Round)**

Evidence found that the company has raised further capital at a higher valuation. N.B. This only includes follow on rounds achieved on one of the 5 equity crowd funding platforms covered by this report. In 58 cases an uplift in value could be discerned. In a further 79 cases evidence of further equity issuance was found at Companies House but there is insufficient disclosure to allow calculation of the resulting valuation.

**Green**

All indications suggest the company is trading. Whilst it is not possible to judge how well the company is trading versus expectations, the survey results indicate that the company does not fall into any other category.

**Amber**

Company exhibits one or more of the following criteria which could indicate that the business is experiencing difficulties:

- Not contactable by telephone over a 3 week period
- Not responding to email or website form enquiries
- Social media presence exhibits a significant interruption to usual pattern or has ceased to be active e.g. Twitter, Facebook, LinkedIn
- Company website off-line
- Late statutory filings at Companies House
- Company has raised further capital at a lower valuation
- Company has restructured to preserve the value of investor’s initial investment

**Red**

Company exhibits one or more of the following criteria, which are strongly indicative of a business failure:

- Listed as ‘dissolved’ at Companies House
- Listed as ‘in administration’ at Companies House
- Listed as ‘in liquidation’ at Companies House
- Company website indicates trading has ceased
- Funding platform confirms that company has stopped trading
- Directors of the Company have indicated that company has stopped trading
The information gathered in this report derives from two sources:

- Companies House filings
- Survey data

**Companies House Filings**

Companies incorporated and dissolved in the UK are required by law to make this information publicly available through Companies House, a government agency sponsored by the Department for Business, Innovation and Skills.

The report draws current company status information direct from Companies House.

Filing Annual Accounts and Returns with Companies House is a statutory requirement for all UK registered companies. Companies are penalised when they fail to file appropriate accounts and annual return documentation with Companies House. Late filings may simply be an administrative oversight but they can also be an indication that a company is facing difficulties. We have therefore used late filings as one of a number of clues that might suggest that a company might be categorised as amber, albeit this information was always supplemented by survey data.

We also used Companies House data to support valuation analysis, which we then used to estimate the uplift in value created by follow on funding rounds.

Companies House data is not always timely:

- Accounts and annual returns are only filed once a year. It may therefore take up to 18 months for a problem to show up in Companies House records.
- The process of a company going into administration or being dissolved can be lengthy, taking up to 18 months, and therefore there is the possibility that companies that are in difficulties will not yet be highlighted.
- Companies House data is occasionally incomplete.
- Companies with no creditors can continue to file accounts with Companies House indefinitely despite not actively trading.

As a result of these shortcomings information from Companies House was supplemented by survey evidence.
Survey Data

As a result of the possible delay between changes in a company's status and reporting to Companies House, the data was supplemented by a survey.

All companies that have received financing through crowdfunding campaigns were approached over a period of 4 weeks in September 2015. We have detailed data behind all of our survey findings.

Survey methods

To establish a company status, referred to in the Status Definitions above, a range of survey methods were used.

- Telephone calls
- Emails
- Observation of web activity
- Observation of social media activity

This approach does include some subjectivity. However, used as a supplement to the Companies House information, a high degree of confidence in the accuracy of the classifications can be achieved.

Report Limitations

A report into the status of recently funded companies in a new segment of finance needs to carry a number of caveats including:

- This report only takes into account companies funded on online crowdfunding platforms. It therefore ignores all offline angel funding.
- Sample Size – The number of companies surveyed, particularly in 2011 and 2012, is too small to serve as a representative sample.
- Short History – Establishing a measure of investor returns in the equity of young companies takes time. Most business plans include forecasts for two or three years. As such that is a reasonable indication of the minimum time required to discern if a company is developing in line with, ahead of, or below, expectations.
- Exposure to recently funded companies - The final issue is to some extent a combination of the above. For the bulk of the companies in this sample, less than two years have passed since funding. These companies have not yet had much of a chance of failing, or offering a realisation opportunity.

The depth and utility of this data set will therefore improve significantly over time, allowing greater conviction in the conclusions.
The data reveals the proportion of companies that are showing no sign of difficulties, or that have realised a return for investors, by cohort:

We would reiterate the limitations explored above at this point. The sample sizes in 2011 and 2012 are too small to be representative. Equally, not enough time has passed for either the 2014, or the H1 2015 sample to have deviated significantly from their business plans. 2013, arguably is the most representative sample.

In the US there is an often quoted, but rarely substantiated, mantra that ‘9 out of 10’ start ups fail. Meanwhile in the UK the RSA 2014 study, referenced earlier, suggests that 55% of SMEs fail in their first year.
five years of existence. Furthermore, the Nesta 2009 report suggested that 56% of angel investments failed to return capital. Relative to any of those benchmarks, crowdfunded companies seem to be out-performing significantly. In the 2013 cohort, only 27% of companies are classified as either red or amber. One could argue that companies that have just received a large amount of equity investment should out-perform the average. Equally the sample of companies in this report is older than the RSA study given that the average age at the time of funding is already over 3 years. Notwithstanding these two caveats, we are impressed by these findings.

At the other end of the spectrum a significant number of companies that raised funds through crowdfunding have gone on to raise further funds at a higher valuation. Whilst this does not denote a return of any kind to the original crowdfunding investors, it is a good indication that there may be the prospect of a return at a future date.

Finally, to date there is one confirmed realisation in the UK. E-Car Club Limited, funded through Crowdcube in 2013, was acquired by Europcar in 2015. Unfortunately exact numbers are impossible to acquire, but the return to the original investors was said to be “around 2.5x”.

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Figure 11 - Aggregated Company Status by Origination Year %

![Graph showing aggregated company status by origination year percentage.](image)
Statistically Crowdcube has the most useful sample. It is both the largest sample size and has the longest trading history amongst the crowdfunding platforms in this survey. It is therefore unsurprising that Crowdcube offers the broadest range of outcomes in terms of company status. Amidst a majority of companies categorised as Green, investors have also seen Green Plus and Pink, as well as a smattering of Red and Amber.

Crowdcube offers all platform subscribers the ability to track past campaigns by linking directly to Companies House data. However, portfolio level statistics derived from this information are not made available to investors. i.e. overall statistics are not displayed meaning a prospective investor would have to trawl through all previous campaigns to get a sense of any failure rate.

That said, whilst Companies House data is not very timely, it is at least the right kind of approach in terms of being transparent about the current status of companies that have received funding through Crowdcube.
From Figures 12 to 14, it is immediately notable that Seedrs has the highest proportion of the Green Plus category. This platform uses a nominee structure, aimed at increasing investor protection by simplifying the administration of the investment and enabling Seedrs to monitor and enforce investor rights. A result of this structure is that follow on fundraising rounds always appear on the Seedrs platform (albeit sometimes these rounds are limited to existing investors). Seedrs does not, however, offer investors any means of tracking past campaigns either on a campaign-by-campaign or average basis. Whilst there is clear room for improvement here, we do at least see the follow on requirement as an excellent way of ensuring an ongoing opportunity for the crowd to participate in future fundraisings of crowdfunded companies in which they have invested.
Until September 2015, SyndicateRoom had no companies with a Red status. However, when the first Red did emerge the reaction was impressive. The platform immediately contacted all its investors (whether they had invested in the failed company or not) and offered coverage of the failure. This served both to highlight the risks to investors and to allow an opportunity for investors to learn from the past. We also note that at the beginning of November 2015, SyndicateRoom announced that it would also adopt a nominee structure for investors which should ensure that any follow on rounds will be shown to the crowd.

72% of companies in the 2013 cohort are showing no signs of difficulties.
AGGREGATED RETURN ANALYSIS

If we assume a monetary value for each of our categories we can make an estimate of the return that could have been achieved by an investor. Clearly any such analysis is purely an estimate and the values attributed to each category are subjective:

**Red**

Value at zero.

**Red**

Whilst we have assumed that all companies categorised as Red are worth nothing, there could in fact be scenarios where investors get some of their money back. Nonetheless we see zero as a realistic approximation.

**Amber**

Value at 25% of par except in the case of a ‘down-round’ where we can calculate the actual value reduction.

**Amber**

Even if a company categorised as amber does indeed fail it may not be worth zero. One could also argue that a company could recover from amber – albeit we have not seen any examples of this in our research. We see 25% as a conservative estimate of the effective value of an amber company.

**Green**

Value at par i.e. money invested.

**Green**

This research has not explored whether or not companies categorised as green are performing in line with below, or ahead of expectations. We have merely identified that they are active.

**Green PLUS (Up Round)**

Establish the average valuation uplift achieved in the latest follow on raise.

**Green PLUS (Up Round)**

To establish the value of the companies that have done follow on capital raises at higher valuations, we established the increase in valuation achieved by the subsequent round and adjusted the return to the original investors to reflect any dilution from the issuance of new shares. Only subsequent rounds that were successful on equity crowdfunding platforms have been captured, as only in these instances can we consistently discern both the increase in valuation and corresponding dilution.

**Realisation**

Value the % return assumed to have been achieved, by the original crowdfund investors, on successful exit.

**Realisation**

If, for confidentiality reasons, the exit multiple is not available, an estimate based on market intelligence is used.
• There has been no account taken of any differences in value for differing share classes. The analysis is also only on the further issue of ordinary shares.
• The uplift of each Green PLUS was used to give the actual valuation increase across the category.
• To calculate the investor return we have factored in both any change in valuation as well as the dilution caused by the new issue of shares. Where a platform displays an amount of equity offered we have assumed this to be the pre-money % of equity owned by the new investors.

An Internal Rate of Return (IRR) calculation was then used to establish the portfolio return of the sample of companies.

This return amounts to **2.17%** expressed as an IRR. This can be equated to an annualised effective compounded return rate. Given that our sample includes capital raises across a period of time, an IRR is the best way to reflect the return that might have been achieved to September 30th 2015.

Figure 15 shows how the IRR varies with the year that the fundraise occurred. It can be seen that, broadly speaking, the longer ago the fundraise occurred, the higher the IRR. This might be expected as it takes time to create equity value. However, when interpreting the chart, the small sample size of the 2011 and 2012 cohorts must be considered, putting a question mark over the statistical significance of any analysis for those years.

The UK Government’s SEIS and EIS tax incentive schemes alter the economics of investing in qualifying unquoted companies such as those commonly found in crowdfunding campaigns. Over 90% of the crowdfunding campaigns in this report were SEIS/EIS eligible. The EIS and SEIS schemes give tax relief (30% and 50% respectively) on the amount invested and offer the ability to offset capital losses against gains for tax purposes. EIS and SEIS are subject to a three year minimum holding period with the relief clawed back if shares are disposed within the minimum holding period. This could be a further reason why so few crowdfunded campaigns have given investors an exit so far.
Based on our analysis, the IRR of the crowd portfolio is 2.17%.

Existing Regulatory Position

Equity Crowdfunding platforms are regulated by the FCA as investment-based crowdfunding platforms. As such they are able to market non-readily realisable securities to retail clients only if the client is:

- Certified as a “high net worth investor”
- Certified or self certified as a “sophisticated investor”
- Certified as a “restricted investor”

At the behest of the FCA, the platforms all use similar risk warnings which reference that most start-up businesses fail, or do not scale as planned. The risk warnings also highlight that failures may result in the investor losing all of their investment.

Given these acknowledgments it would seem logical that platforms should allow investors the ability to easily track just how many have failed, and what is the overall proportion of success to failure. As a retail investor dominated market, platforms should do their utmost to ensure that investors are fully appraised of the likelihood of them backing a successful campaign.

Modeling the impact of SEIS and EIS reliefs on investor IRR provides a significant uplift. Assuming that full advantage of these reliefs is taken by the investor the portfolio aggregate IRR rises to 33.79%. On top of the assumption that full advantage of the relief is taken, an assumption around the holding period is also required to calculate this return. The calculation therefore pro-rates the tax relief over the holding period for companies that funded less than 3 years ago on the assumption that all investments are held for the minimum holding period.

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CONCLUSIONS

- High proportion of crowdfunded companies remain active.
- Contrary to popular perception the sector is not just funding start-ups. The all-time average age of companies across the sample at fund raise at 2.91 years.
- The sector is increasingly funding larger campaigns and companies from a wider range of sectors.
- The annualized IRR across the portfolio, based on our valuation assumptions, is **2.17%**. In effect, the average annual return across companies since inception has been 2.17pence for every pound invested. This is before any adjustment is made for government tax incentives such as EIS/SEIS.
- After taking SEIS/EIS into account the IRR increases to **33.79%**
- All stakeholders in this new asset class should recognise that retail investors dominate the market and that access to retail investors brings responsibilities. Democratising small business funding comes at a price and that price is the obligation to maximize transparency. Companies that fund should also recognize these obligations.
- Platforms should therefore do everything they can to assist the crowd in finding a valuation level that offers a sufficient prospect of a return to compensate for the risk.

Accessing the retail investor for funding brings a responsibility to allow the enlightened appraisal of likely return. To achieve this, platforms need to offer maximum transparency both to allow the investor to appraise a specific campaign, but also to identify the success rate of past campaigns. By ensuring that the investors recognise that there is a risk that their principal may not be returned at all, it ensures that the investors only proceed with an investment at a valuation which offers the prospect of a return sufficient to compensate for that risk. This is even more important given that the process of price discovery in crowdfunding faces obvious challenges:

- Investors may have a relative lack of experience.
- There is an absence of proxies and no live secondary market pricing.

Quoted markets offer live secondary market pricing and significant regulatory scrutiny which brings some protections to investors that are not available in the crowdfunding sector. Without these structural informational advantages crowdfunding should do everything it can to ensure the crowd has as much information as possible to arrive at a reasonable valuation. Ultimately the long term success of this industry requires that companies are funded at a fair price. Too high and the investors will stop coming back, too low and the companies will go elsewhere. A transparent history of past campaigns would assist the industry in funding companies at an enlightened valuation.
RECOMMENDED BEST PRACTICE

Whilst there are existing regulatory protections in place platforms could pre-empt future regulatory scrutiny by ensuring that their customers are offered the maximum opportunity to appraise the likelihood of suffering loss. This is particularly important given that the platforms themselves acknowledge that failure is likely not just to result in the investor losing some money, but all of their money.

These concerns are exacerbated by the risk of accusations that platforms are acting purely as intermediaries and do not have ‘skin in the game’. Platforms do not risk material amounts of their own capital – if at all. It is useful to draw the comparison between equity crowdfunding platforms and P2P lending platforms, also operating within the same space of internet enabled financial disintermediation. In the case of P2P the platforms see their transparent track record as their ‘skin in the game’. Indeed, in October 2015 the UK P2PFA – the P2P industry body – made disclosure of platform loan books a requirement for membership.

The long-term success of the UK crowdfunding market would be enhanced if the platforms were to facilitate some tracking of previous campaigns.

At present there is no central repository for such information and the platforms themselves offer varying levels of disclosure.

One would expect the investors in a campaign to be informed of company developments and one might reasonably ask why a company should make disclosures to anyone else. However, crowdfunding platforms should encourage companies that the ongoing success of the sector depends on them being able to offer transparency to investors. Effectively, in order to enjoy the benefits of accessing this new market, platforms should explain to companies that doing so comes with certain obligations. This does not need to compromise the companies in question. For example, basic requirements could include an obligation to update investors and the crowdfunding platform on further fund raising rounds. On top of this, there should be prompt disclosure when a company fails, and, if possible, an exploration of what went wrong.

Based on the findings of this report we have outlined some proposed Best Practice.

• Platforms should take some responsibility for company updates. Some information, e.g. company status, should be shared with the wider subscriber base, as well as with investors, in as timely a manner as possible. Platforms should build this into their Terms & Conditions and ensure that companies understand that raising money from the crowd brings an obligation to make transparent disclosures.
• Platforms should allow all subscribers to see the latest Companies House information for all funded campaigns as a minimum and should work towards updating company status in as timely a fashion as reasonably possible.
• Platforms should communicate failures to subscribers in a timely fashion. Where possible, sufficient disclosure should be made to allow lessons to be learnt.
• Platforms should advertise their track record i.e. demonstrate what is the current status of previously listed campaigns. This should include follow on valuations and realisations as well as failures.
• Company status information should be displayed on aggregated basis as well as campaign by campaign.
• Platforms should introduce uniform standards for reporting statistics. There is currently no reporting standard for basic metrics such as volume funded, making comparative analysis tricky.
• Platforms should avoid issuing the crowd with a different class of shares from management and should ensure clear explanation of any differences.
• Platforms should attempt to ensure that funded companies ensure that follow on raises are shown to the crowd.
AltFi Data is the leading provider of data and analysis for the rapidly growing alternative finance sector. We also provide research and consultancy services. Amongst other data sets, AltFi Data publishes the Liberum AltFi Volume Index and Liberum AltFi Returns Index which track the volume and returns of loans originated by the UK and Continental European alternative finance industry platforms. AltFi Data is a sister company to AltFi, a company that provides news, commentary and events for the alternative finance industry.

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