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GLOBALIZATION

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The “Law and Economics Yearly Review” is an academic journal to promote a legal and economic debate. It is published twice annually (Part I and Part II), by the Fondazione Gerardo Capriglione Onlus (an organization aimed to promote and develop the research activity on financial regulation) in association with Queen Mary University of London. The journal faces questions about development issues and other several matters related to the international context, originated by globalization. Delays in political actions, limits of certain Government’s policies, business development constraints and the “sovereign debt crisis” are some aims of our studies. The global financial and economic crisis is analysed in its controversial perspectives; the same approach qualifies the research of possible remedies to override this period of progressive capitalism’s turbulences and to promote a sustainable retrieval.

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ZOOMING IN ON THE “INDIVIDUAL PORTFOLIO MANAGEMENT OF LOANS” IN THE AMBIT OF THE REGULATION ON EUROPEAN CROWDFUNDING SERVICE PROVIDERS

Nina Dietz Legind* - Andrea Minto**

ABSTRACT: *During recent years, crowdfunding platforms have settled into the marketplace, becoming a real alternative mean to raise funds. In approaching the recent Regulation (EU) no. 2020/1503 on “European Crowdfunding Service Providers” (ECSPR), the article aims to examine the individual portfolio management of loans due to its peculiar characteristics which single this service out from those generally offered by lending-based crowdfunding platforms.*

The individual portfolio management of loans entails the allocation of a predetermined amount of funds of an investor to one or multiple crowdfunding projects, in accordance with a specific mandate. Unlike what generally happens with the credit provided through the traditional banking intermediation, therefore, the client is not directly selecting the project they want to invest in. Rather, the client indicates the parameters against which the crowdfunding service provider will sort out how to allocate the funds. The mandate thus becomes an extremely relevant factor as it allows, ex ante, the choice of investment and, ex post, the evaluation of the results produced by the management activity, provided that the crowdfunding

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Although this article is the result of a joint reflection, par. 1 and 5 can be primarily attributed to Nina Dietz Legind, with the remaining sections primarily attributable to Andrea Minto.

service provider does not take any risk of its own, and, thus, the risk remains entirely on the investor.

Such interesting relationship between the crowdfunding service provider offering individual portfolio management of loans and the investor eventually calls for an enhanced level of investor protection which translates into a wide set of transparency obligations and disclosure requirements.

SUMMARY: 1. Introduction. The Regulation on European Crowdfunding Service Providers (ECSPR) – 2. The crowdfunding intermediation and the lending-based crowdfunding – 3. The features of the individual portfolio management of loans – 4. The disclosure obligations and requirements for the crowdfunding service provider offering individual portfolio management of loans – 5. Concluding remarks.

1. During recent years, financial innovation has brought about significant changes in how markets function as well as in the breadth of products targeting financial users¹.

Recent studies and surveys show that the scale of crowdfunding platforms is still relatively small as activity and, most importantly, remains confined to the national market with very little cross-border activity². This creates differences in

¹ See W. S. FRAME, L. D. WALL and L. J. WHITE, *Technological change and financial innovation in banking: Some implications for fintech*, 2018; see also M. QAMRUZZAMAN, J. WEI, *Financial innovation, stock market development, and economic growth: an application of ARDL model*, in *International Journal of Financial Studies*, 2018, 6.3: 69; with regard to financial innovation in the ambit of crowdfunding see G. FERRARINI, *Regulating fintech: Crowdfunding and beyond in European Economy*, 2017, 2: 121-142; W. L. HARRIS, J. WONGLIMPIYARAT, *Dynamics of crowdfunding and FinTech challenges in International Journal of Business Innovation and Research*, 2020, 23.4: 501-514; A. MUNEEZA, N. A. ARSHAD and A. T. ARIFIN, *The application of blockchain technology in crowdfunding: towards financial inclusion via technology in International Journal of Management and Applied Research*, 2018, 5.2: 82-98; F. AKINBAMI, *Retail financial products and the global financial crisis*, available at SSRN 2087548, 2012; V. CAIVANO, M. GENTILE, N. LINCiano, and P. SOCCORSO, *Report on Financial Investments of Italian Households. Behavioural Attitudes and Approaches, CONSOB Statistics and Analyses, Survey (October 22, 2018)*.

² T. ZIEGLER, R. SHNEOR, K. WENZLAFF, A. ODOROVIĆ, D. JOHANSON, R. HAO, L. RYLL, *Shifting paradigms. The 4th European alternative finance benchmark report*, University of Cambridge 2019; P. BELLEFLAMME, N. OMRANI and M. PEITZ, *The economics of crowdfunding platforms in Information Economics and Policy*, 2015, 33: 11-28; A. ROSSI; S. VISMARA. *What do crowdfunding platforms do? A comparison between investment-based platforms in Europe*, in

national regulations, which, in turn, increase transaction costs and exacerbate problems of regulatory fragmentation³. This shortcoming inevitably represented an obstacle for crowdfunding platforms wishing to operate in a cross-border fashion, as they were relentlessly faced with different regimes and requirements from Member State to Member State⁴.

Among the phenomena that have been closely scrutinised by policy and law makers, crowdfunding platforms are most certainly ranking on the top list along with crypto assets⁵. On 20 October 2020, the *Regulation on European Crowdfunding Service Providers* was enacted (Reg. (UE) no. 2020/1503, which will be referred to as

Eurasian Business Review, 2018, 8.1: 93-118; J. GERA and H. KAUR, *A novel framework to improve the performance of crowdfunding platforms*, in *Ict Express*, 2018, 4.2: 55-62.

³ G. FERRARINI and E. MACHIAVELLO, *FinTech and Alternative Finance in the CMU: The Regulation of Marketplace Investing* in D. BUSCH, E. AVGOULEAS and G. FERRARINI (eds.), Capital Markets Union in Europe,

Oxford University Press, 2018; S.N. HOOGHMSTRA and K. DE BUYSERE, *The Perfect Regulation of Crowdfunding: What Should the European Regulator Do?* in O. GAJDA and D. BRÜNTJE (eds.), *Crowdfunding in Europe – State of the Art in Theory and Practice*, Springer, 2015.

See also, amongst the many reports, European Commission, *Legislative proposal for an EU framework on crowd and peer to peer finance – Impact Assessment*, 30 October 2017; European Commission, *Assessing the potential for crowdfunding and other forms of alternative finance to support research and innovation*, available at: <https://publications.europa.eu/en/publication-detail/-/publication/3190dbeb-316e-11e7-9412-01aa75ed71a1>; ESMA's Opinion and Advice are available at: https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1378_opinion_on_investment-based_crowdfunding.pdf and https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1560_advice_on_investment-based_crowdfunding.pdf, respectively; EBA's Opinion is available at [https://www.eba.europa.eu/sites/default/documents/files/documents/10180/983359/f6106173-dc94-4d22-ade8-d40fce724580/EBA-Op-2015-](https://www.eba.europa.eu/sites/default/documents/files/documents/10180/983359/f6106173-dc94-4d22-ade8-d40fce724580/EBA-Op-2015-03%20%28EBA%20Opinion%20on%20lending%20based%20Crowdfunding%29.pdf?retry=1)

03%20%28EBA%20Opinion%20on%20lending%20based%20Crowdfunding%29.pdf?retry=1 .

⁴ For instance, in Italy, the current crowdfunding regime is based on the provisions set out in art. 50 *quinquies*, 100 *ter* and 190 *quater* Italian Consolidated Financial Act, as well as – on a regulatory level – in Consob Reg. no. 18592/2013.

⁵ Among the various phenomena subject to regulation, considerable importance is undoubtedly attached to the recent proposal for a Regulation known as MiCA (Market In Crypto-Assets), published by the European Commission on September 24, 2020 to regulate crypto-activities not falling within the scope of EU legislation on financial services. See e.g. O. MCDONALD, “*New Cryptocurrencies and New Developments*”, in *Cryptocurrencies: Money, Trust and Regulation*, 25-48. Agenda Publishing, 2021, <https://doi.org/10.2307/j.ctv1wgvcz.6>; D. A. ZETZSCHE, F. ANNUNZIATA, D. W. ARNER and R. P. BUCKLEY, *The market in Crypto-Assets Regulation (MICA) and the EU Digital Finance Strategy*, 2020; S. T. OMAROVA, *New tech v. new deal: Fintech as a systemic phenomenon*, in *Yale J. on Reg.*, 2019, 36: 735; A. FERREIRA, P. G. SANDNER, T. DÜNSER, *Cryptocurrencies, DLT and Crypto Assets – the Road to Regulatory Recognition in Europe* (April 1, 2021). Forthcoming in: *Handbook on Blockchain*, Editors: My Thai (University of Florida), Duc A. Tran (University of Massachusetts), Bhaskar Krishnamachari (University of Southern California), Publisher: Springer Nature (Springer Series on Optimization and Its Applications: <https://www.springer.com/series/73>, Available at SSRN: <https://ssrn.com/abstract=3891401> or <http://dx.doi.org/10.2139/ssrn.3891401>; E. NOBLE, *Crypto-Assets: Overcoming Challenges to Scaling-An EU Approach*, available at *SSRN 3748343*, 2020.

ECSPR hereafter), which introduces important elements of novelty regarding the authorisation regime, the rules of conduct and other investor protection requirements. The ECSPR will apply from November 2021 (except for a one-year transitional regime for platforms that already provide crowdfunding services) and will introduce a common framework for all crowdfunding platform operators, assimilating – on a general level – investment-based and lending-based crowdfunding⁶.

Such piece of legislation will most certainly make history (as the *Market in Crypto-Assets Regulation* – MiCAR – will!) for a good set of reasons. Not only will it regulate an emerging segment of the financial markets with its own features⁷. It will also raise extremely delicate coordinating challenges with the existing articulated financial legislation⁸. As much commendable as the work of the EU legislators could be in (eventually) regulating, say financial innovation, it casts some doubts on whether and how legal certainty and legal clarity could be affected as the entire body of EU financial law grows bigger and bigger⁹. The very success of this gigantic corpus

⁶ See E. MACCHIAVELLO, 'What to Expect When You Are Expecting' a European Crowdfunding Regulation: The Current 'Bermuda Triangle' and Future Scenarios for Marketplace Lending and Investing in Europe, 2019; and see also *The European Crowdfunding Service Providers Regulation: The Future of Marketplace Lending and Investing in Europe and the 'Crowdfunding Nature' Dilemma*, in *European Business Law Review*, 2021, 32.3. For more details on lending platforms, see D. CHEN; A. S. KAVURI; A. MILNE, *Growing pains: The changing regulation of alternative lending platforms*, in *The Palgrave Handbook of Technological Finance*. Palgrave Macmillan, Cham, 2021. p. 441-475.

⁷ The introduction of a common regime, on a European level, for the different forms of crowdfunding, is therefore a factor of market development and investment incentive, as it allows crowdfunding service providers to apply for a European passport under a uniform regulation. For more details see S. N. HOOGHMSTRA, *Will the Proposed European Crowdfunding Regulation Lead to a "True" European Market for Crowdfunding?*, in *CROWDASSET: Crowdfunding for Policymakers*, 2020, pp. 413-436.

⁸ See A. SCIARRONE ALIBRANDI, G. BORELLO, R. G. FERRETTI, F. LENOCI, E. MACCHIAVELLO, F. MATTASSOGLIO, F. PANISI, and P. MUNAFÒ, *Marketplace Lending. Towards New Forms of Financial Intermediation?*, July 1, 2019. CONSOB Fintech Series No. 5, available at SSRN: <https://ssrn.com/abstract=3685318> or <http://dx.doi.org/10.2139/ssrn.3685318>; J. LERNER; P. TUFANO, *The consequences of financial innovation: a counterfactual research agenda*, in *Annu. Rev. Financ. Econ.*, 2011, 3.1: 41-85.

⁹ The complexity of the current body of EU law is the inevitable result of a huge number of sources: there are more than 80 acts in place at legislation level 1 (i.e. approx. 50 Regulations and 30 Directives), around 300 acts at legislation level 2 (approx. 290 RTS AND 9 ITS) and more than 170 documents at level 3 legislation. This increase in the amount of sources and pieces of law is also reflected at the international level. Indeed, it is worth noting that, over time, the Basel standards

of law rests – to our mind – on a very precise and tight coordination between the constellation of laws and regulations that form the EU financial law universe¹⁰. The overlapping regulatory frameworks established under the ECSPR and other pieces of EU financial and banking law, thus, might increase the risk of regulatory arbitrage and have a disruptive effect on access to finance and the development of capital markets in certain countries¹¹.

Lending-based crowdfunding platforms, as it is known, represent an alternative to traditional financial intermediation. They do that by putting in direct contact to those who offer credit (so-called lenders), on the one hand, and those who ask for it (so-called borrowers); although their use is still very limited¹², in some markets, they are acquiring an increasingly disruptive role, to the point of representing a real alternative to bank credit and on the other hand representing a new investment alternative to the lenders¹³.

passed from a document of 60 pages (Basel I, in 1988) to a document of 251 pages (Basel 2 to the 1626 pages of Basel III in 2013).

¹⁰ See e.g., M. HOBZA and A. VONDRÁČKOVÁ, *The New Financial Crowdfunding Regulation and Its Implications for Investment Services under MiFID II* (November 6, 2020). Charles University in Prague Faculty of Law Research Paper No. 2020/III/2, available at SSRN: <https://ssrn.com/abstract=3725997> or <http://dx.doi.org/10.2139/ssrn.3725997>.

¹¹ It is worth noticing that this problem is acknowledged by the same ECSPR (see for instance recital n. 17 and, quite significantly, recital n. 9 that specifies the following: “To avoid regulatory arbitrage and to ensure their effective supervision, crowdfunding service providers should be prohibited from taking deposits or other repayable funds from the public, unless they are also authorised as a credit institution in accordance with art. 8 of Directive no. 2013/36/EU of the European Parliament and of the Council. However, Member States should ensure that national law does not require an authorisation as a credit institution or any other individual authorisation, exemption or dispensation for project owners or investors where they accept funds or grant loans for the purposes of offering or investing in crowdfunding projects”). On regulatory arbitrage and the possible actions to be undertaken by policy-makers, see e.g. A. MINTO, S. PRINZ, M. WULFF, *A Risk Characterization of Regulatory Arbitrage in Financial Markets* in *European Business Organization Law Review*, 2021, vol. 3, pp. 1-34; V. FLEISCHER, *Regulatory arbitrage*, in *Texas Law Review*, 2010, pp. 227-289; F. PARTNOY, *Financial derivatives and the costs of regulatory arbitrage*, *Journal of Corporate Law*, 1997, pp. 211-227; F. PARTNOY, *The law of two prices: regulatory arbitrage, revisited*, in *Georgetown Law Journal*, 2019, pp. 1017-1043; E. MACHIAVELLO, *The European Crowdfunding Service Providers Regulation and the Future of Marketplace Lending and Investing in Europe: the ‘Crowdfunding Nature’ Dilemma*. Forthcoming in *European Business Law Review* 2021.

¹² For example, in the UK, business loans facilitated by crowdfunding platforms amounted to 15% of total small business loans in 2016, up from less than 1% in 2012. See e.g. ZHANG, BRYAN ZHENG, *et al. Entrenching Innovation-The 4th UK Alternative Finance Industry Report*, available at SSRN 3084570, 2017.

¹³ For a classification of virtual platforms also in consideration of the national legal context, from those falling within the perimeter of application of art. 100-ter of the Italian Consolidated Financial

2. The ECSPR applies to crowdfunding intermediation (namely, “*crowdfunding services*”) operated through a digital platform open to the public that matches – or facilitates the matching of – prospective investors or lenders with businesses that seek funding¹⁴. According to art. 2, par. 1, lett. a), crowdfunding service means “the matching of business funding interests of investors and project owners through the use of a crowdfunding platform and [...] consists of any of the following: (i) the facilitation of granting of loans; (ii) the placing without a firm commitment basis, as referred to in point (7) of Section A of Annex I to Directive 2014/65/EU, 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, as referred to in point (1) of that section, in relation to those transferable securities and admitted instruments for crowdfunding purposes”.

The notion of crowdfunding service has therefore been designed to capture both lending-based crowdfunding (“the facilitation of granting of loans”) and investment-based crowdfunding (the placing without firm commitment basis of transferable securities and admitted instruments for crowdfunding purposes issued

Act to those aimed at putting supply and demand for credit directly in relation to each other, see e.g. G. P. LA SALA, *Intermediazione, disintermediazione, nuova intermediazione: i problemi regolatori*, in M. CIAN – C. SANDEI (ed.), *Diritto del Fintech*, Wolters Kluwer-Cedam, 2020, 16 – 21; D. SICLARI – G. SCIASCIA, *Innovazione finanziaria e rafforzamento del mercato unico per i servizi finanziari retail: sfide, rischi, risposte della regolazione*, in *Riv. Trim. Dir. Ec.*, 2016, p. 200 ss.; ARGENTATI, *Le banche nel nuovo scenario competitivo. Fintech, il paradigma Open banking e la minaccia delle Big Tech companies*, in *Mercato concorrenza regole*, 20(3), pp. 441-466; L. B. JUNGE, I. C. LAURSEN, K. R. NIELSEN. *Choosing crowdfunding: Why do entrepreneurs choose to engage in crowdfunding?*, in *Technovation*, 2021, 102385.

¹⁴ See T. JOVANOVIĆ. *Crowdfunding: what do we know so far?*, in *International Journal of Innovation and Technology Management*, 2019, 16.01: 1950009; J. PASCHEN, *Choose wisely: Crowdfunding through the stages of the startup life cycle*, in *Business Horizons*, 2017, 60.2: 179-188; B. K. ADHIKARY, K. KUTSUNA, T. HODA, *Crowdfunding – Types and Models*, in *Crowdfunding*. Springer, Singapore, 2018, pp. 9-20; D. CUMMING; L. HORNUF (ed.). *The economics of crowdfunding: startups, portals and investor behavior*. Springer, 2018; K. TAEUSCHER, R. BOUNCKEN, and R. PESCH, *Gaining legitimacy by being different: Optimal distinctiveness in crowdfunding platforms*, in *Academy of Management Journal*, 64(1), 2021, 149-179; O. HAVRYLCHYK, *Regulatory framework for the loan-based crowdfunding platforms*, 2018. See also art. 1 ECSPR that reads as follow: “This Regulation lays down uniform requirements for the provision of crowdfunding services, for the organisation, authorisation 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 Union” (see also recital no. 1).

by project owners or a special purpose vehicle ('SPVs') and the reception and transmission of client orders with regard to those transferable securities and admitted instruments for crowdfunding purposes)¹⁵.

Unlike, for example, the banking business where both the activities of “taking of deposits or other repayable funds from the public” *and* “granting credit for its own account” have to be performed by the entity for it to qualify as a credit institution¹⁶, the crowdfunding platforms are not required to provide both activities jointly. Despite the circumstance that lending-based and investment-based are included in the notion of crowdfunding, the platform could most certainly limit its activity to either financing or offering financial instruments¹⁷. Consistently, art. 12 ECSPR on “the authorisation as a crowdfunding service provider” requires the applicant/prospective provider to draw up a “programme of operations” setting out “the types of crowdfunding services that the prospective crowdfunding service provider intends to provide and the crowdfunding platform that it intends to operate, including where and how crowdfunding offers are to be marketed” (see art. 12, par. 2, lett. d))¹⁸.

Both in the case of lending-based crowdfunding and investment-based

¹⁵ Recital 1 ECSPR points out that “Crowdfunding represents an increasingly important type of intermediation where a crowdfunding service provider, without taking on own risk, 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. *It is therefore appropriate to include within the scope of this Regulation both lending-based crowdfunding and investment-based crowdfunding, since those types of crowdfunding can be structured as comparable funding alternatives*” (emphasis added).

¹⁶ See art. 4(1), point 1, letter (a) of Regulation (EU) No 575/2013 (CRR) and European Banking Authority, *Opinion of the European Banking Authority on elements of the definition of credit institution under Article 4(1), point 1, letter (a) of Regulation (EU) No. 575/2013 and on aspects of the scope of the authorisation*, 18 October 2020.

¹⁷ See CHIOMENTI, ITALIAFINTECH, *Position Paper Il Regolamento UE 2020/1503 relativo ai fornitori europei di servizi di crowdfunding per le imprese*, 7 May 2021, available at <https://www.chiomenti.net/public/files/0/Position-Paper-Crowdfunding-IF.pdf>.

¹⁸ Another important element worth mentioning is that there is no requirement for an exclusive corporate purpose, and crowdfunding service providers may also offer activities other than those covered by the Regulation, provided that – obviously – relevant applicable EU and/or national law are complied with. For further information, see S. PANAGIOTIS, *The European Union Proposal for a Regulation on Cross-Border Crowdfunding Services: A Solemn or Pie-Crust Promise?*, 2020, 31, in *European Business Law Review*, Issue 6, pp. 1047-1122, available at <https://kluwerlawonline.com/JournalArticle/European+Business+Law+Review/31.6/EULR2020039>.

crowdfunding, three types of actors are involved: the project owner that proposes the project to be funded, investors who fund the proposed project and an intermediating organisation in the form of a crowdfunding service provider that brings together project owners and investors through an online platform¹⁹.

In line with the aim of this article, the analysis will be confined to lending-based crowdfunding only.

As said, the “lending-based crowdfunding” consists in facilitating the granting of loans. The ECSPR does not define what “facilitation of granting of loans” means. It does specify, though, that such notion includes services such as presenting crowdfunding offers to clients and pricing or assessing the credit risk of crowdfunding projects or project owners. Favouring a more elastic and flexible approach over an (unrealistic) narrow definition of “facilitation of granting loans” ensures – to our mind – that different business models enabling a loan agreement between one or more investors and one or more project owners (and concluded through a crowdfunding platform) come within the scope of application of the regulation. This could surely be framed a well-done attempt to strike a balance between technological neutrality and legal certainty²⁰. Loans included within the scope of the ECSPR should be loans with unconditional obligations to repay an agreed amount of money to the investor, whereby lending-based crowdfunding

¹⁹ See recital n. 2 ECSPR and HOOGHMSTRA S.N., *The European Crowdfunding Regulation – Towards a harmonised framework for crowdfunding in Europe?*, in *ACE Comptabilité, fiscalité, audit, droit des affaires au Luxembourg*, 2021/4, p. 12.

²⁰ The EU Commission is still requesting advice from the European supervisory authorities (ESAs) on how to address technological neutrality issues that can be sum up in the principle “*same activity, same risk, same rules*”. In this regard, see https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/210202-call-advice-esas-digital-finance_en.pdf. For more information about technological neutrality, see D. KWAK, *No More Strategical Neutrality on Technological Neutrality: Technological Neutrality as a Bridge Between the Analogue Trading Regime and Digital Trade*, in *World Trade Review*, 2021, 1-15; M. AMSTAD, *Regulating fintech: Objectives, principles, and practices*, in *Asian Development Bank Institute Working Paper Series*, 2019, 1016; D. W. ARNER, D. A. ZETZSCHE, R. P. BUCKLEY AND J. N. BARBERIS, *FinTech and RegTech: Enabling innovation while preserving financial stability*, in *Georgetown Journal of International Affairs*, 2017, 47-58; G. FALCONE, *Tre idee intorno al c.d. “Fintech”*, in *Rivista di diritto bancario*, https://rivista.dirittobancario.it/sites/default/files/pdf_c/giovanni_falcone; N. LINCIANO, P. SOCCORSO, *FinTech e RegTEch: approcci di regolamentazione e di supervisione*, in M.T. PARACAMPO (a cura di), *Introduzione ai profili giuridici di un mercato unico tecnologico dei servizi finanziari*, Torino, 2017.

platforms merely facilitate the conclusion by investors and project owner of loan agreements without the crowdfunding service provider at any moment acting as a creditor of the project owner (see recital n. 11).

In line with the objective of drawing clear lines between reserved activities – and consequently overcoming the mentioned problems of regulatory arbitrage – the facilitation of granting of loans that falls within the scope of ECSPR is to be kept separated from the activity of a credit institution, which grants credits for its own account *and takes deposits or other repayable funds from the public*.

This, in turn, brings us to the notion of “loan”, which, for the purposes of the ECSPR, refers to “an agreement whereby an investor makes available to a project owner an agreed amount of money for an agreed period of time and whereby the project owner assumes an unconditional obligation to repay that amount to the investor, together with the accrued interest, in accordance with the instalment payment schedule” (see art. 2, par. 1, lett. b)).

By avoiding a definition of “facilitating the granting of loans”, the “lending-based crowdfunding” thus ends up revolving around the notion of loan. The ECSPR opted for a regime governing the intermediation of direct financing only, that is, financing from the investor to the company promoting the project to be financed. Consequently, platforms that may be engaging in activities of facilitating the purchase and sale of receivables (so-called invoice trading platforms) therefore appear to be excluded from the scope of application of the ECSPR²¹.

3. The individual portfolio management of loans is defined in the ECSPR as “the allocation by the crowdfunding service provider of a predetermined amount of funds of an investor, which is an original lender, to one or multiple crowdfunding projects on its crowdfunding platform in accordance with an individual mandate given by the investor on a discretionary investor-by-investor basis” (see art. 2, par. 1,

²¹ For a description of the invoice trading platforms, see e.g. V. ANNONI, *Financing Italian Firms Through Invoice Trading Platforms*, in *International Journal of Economics and Finance*, 2020, Vol. 12, No. 3, pp. 78-85.

lett. c).

The individual portfolio management of loans should be singled out from the general lending-based crowdfunding. Indeed, this type of crowdfunding, unlike the one mentioned above, is characterised by the discretion of the service provider in the allocation of the client's resources for the financing of one or more crowdfunding projects, in accordance with the instructions contained in the investor's mandate. Therefore, the service amounts to something much more sophisticated than merely facilitating the granting of loans, and someone could question indeed whether this service should be referred to the general category of the lending-based crowdfunding.

The novelty of the individual portfolio management of loans, as well as the practical implications and relevance that such service might have on the marketplace, could be implicitly drawn from the specific provisions that are dedicated to such service. Indeed, on top of the general rules and principles applying to all crowdfunding service providers, a wide array of additional requirements characterise the provision of such service.

This is clearly the case, for instance, of one of the guiding provisions of the ECSPR, namely art. 3 regarding the provision of crowdfunding services and organisational and operational requirements of crowdfunding. This provision sets out a series of general principles applying to all crowdfunding services (individual portfolio management of loans, too). The principles span from imposing that crowdfunding services shall only be provided by legal persons which are established in the Union and that have been authorised as crowdfunding service providers to requiring the crowdfunding service providers to act honestly, fairly and professionally in accordance with the best interests of their clients (see paras. 1 and 2). Art. 3, par. 4, then, sets out that "crowdfunding service providers may propose to individual investors specific crowdfunding projects that correspond to one or more specific parameters or risk indicators chosen by the investor. Where the investor wishes to make an investment in the suggested crowdfunding projects, the investor shall

review and expressly take an investment decision in relation to each individual crowdfunding offer”. The second subparagraph of the same par. 4 elaborates further by specifically tackling individual portfolio management of loans and specifying that those crowdfunding platforms “shall do so in adherence to the parameters provided by the investors and shall take all necessary steps to obtain the best possible result for those investors. Crowdfunding service providers shall disclose to investors the decision-making process for executing the received discretionary mandate”.

Par. 5 closes up on this by specifying – rightly so – that “*by way of derogation from the first subparagraph of paragraph 4, crowdfunding service providers providing individual portfolio management of loans may exercise discretion on behalf of their investors within the agreed parameters without requiring investors to review and take an investment decision in relation to each individual crowdfunding offer*” (emphasis added).

Consequently, while a crowdfunding service provider, generally speaking, may propose to individual investors specific crowdfunding projects that correspond to one or more specific parameters or risk indicators *insofar* the investor reviews and expressly takes an investment decision in relation to each individual crowdfunding offer, the provision of the individual portfolio management of loans entails that the crowdfunding service provider may exercise discretion and basically act without the investors reviewing each individual crowdfunding offer²². In line with the very wording of this provision, the crowdfunding service provider of an individual portfolio of loans *may* exercise discretion and, consequently, bypass investors’ involvement. How this discretion could be actually exercised – and to what extent – will be relentlessly dependant on the very content of the mandate that establishes the contractual relationship between the investor and the crowdfunding service provider.

²² According to recital n. 20 ECSPR, the so called “auto-investing” should be considered individual portfolio management of loans. Auto-investing refers to business models using automated processes whereby funds are automatically allocated by the crowdfunding service provider to crowdfunding projects in accordance with parameters and risk indicators predetermined by the investor.

In making an offer and setting the relative price, the crowdfunding service provider should perform a (credit) risk assessment which resembles pretty closely the scrutiny undertaken by credit institutions when granting credit²³. In this case, the lending activity rests on the parameters that the client is providing to the crowdfunding service provider. Unlike what generally happens with the credit provided through the traditional banking intermediation, the client is thus not directly selecting the project they want to invest in. Rather, the client indicates the parameters against which the crowdfunding service provider will sort out how to allocate the funds²⁴. In other words, the parameters design the contours of the mandate that the client is giving to the crowdfunding service provider. Nature of the delegation and parameters will be strictly intertwined since the exercise of the delegated powers is subject to strict review in the light of objective criteria determined by the delegating party (the client).

The fact that the mandate is at the epicentre of the provision of the individual portfolio management of loans is most certainly confirmed by art. 6 ECSPR, which is the provision precisely concerned with the “individual portfolio management of loans” and its legal characterisation. This provision in fact qualifies this service by the very mandate given by the investor. This mandate indeed postulates the parameters that the service provider must abide by in providing the service. Those parameters must include at least two of the following criteria that every loan in the portfolio will have to comply with: “(a) the minimum and maximum interest rate payable under any loan facilitated for the investor; (b) the minimum and maximum maturity date of any loan facilitated for the investor; (c) the range and distribution of any risk

²³ See art. 4, par. 4 ECSPR and, for the similarities with the approach used in the banking intermediation, EBA, *Guidelines on loan origination and monitoring*, 29 May 2020, EBA/GL/2020/06. The EBA, however, is entrusted by the same Reg. (EU) no. 2020/1503 with the mandate to develop a RTS project (which will be flanked by that concerning the adequate disclosure of information) on the need for crowdfunding service providers to have an appropriate framework for the assessment of credit risk, loan pricing and risk management techniques (art. 19, par. 7, ECSPR). This must be done in close cooperation with ESMA.

²⁴ See A. MANFROI, A. MIORELLI, *Il nuovo servizio di gestione individuale di portafoglio di prestiti*, in *Dirittobancario.it*, 17 June 2021, available at <http://www.dirittobancario.it/news/capital-markets/il-nuovo-servizio-di-gestione-individuale-di-portafoglio-di-prestiti>.

categories applicable to the loans and (d) if an annual target rate of return on investment is offered, the likelihood that the selected loans will enable the investor to achieve the target rate with reasonable certainty” (see art. 6, par. 1).

For the crowdfunding service provider to meet those requirements, an adequate internal governance system should be put in place. Indeed, operationalising the mandate stipulated with the investor rests on a sound set of internal processes and methodologies and on appropriate data which could be collected by the crowdfunding service provider itself or sourced from third parties²⁵.

In discharging the mandate, the crowdfunding service provider should establish internal arrangements in terms of policies and procedures for the detection of relevant factors that may have unfavourable effects on the performance of the loans. Indeed, the crowdfunding service provider bears a great deal of liability for the management of credit risk and the related financial modelling for that provision of services. Namely, the crowdfunding service provider must examine i) the credit risk of the individual crowdfunding projects that have been selected for the investor’s portfolio; ii) the credit risk of the investor’s portfolio, at an aggregate level and iii) the credit risk of the project owners selected for the investor’s portfolio by verifying the prospect of the project owners meeting their obligations under the loan. Further, the crowdfunding service provider is asked to provide a description of the method used for those three assessments to the investor.

The very characteristics of the individual portfolio management of loans, and its legal characterisation in relation to the underlying mandate, instinctively recall the service of “portfolio management” as provided for under MiFID II. Such investment service entails in fact “managing portfolios in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or

²⁵ See art. 6, par. 2, ECSPR. See also art. 4 ECSPR regarding specifically “effective and prudent management” of a crowdfunding service provider. Once again, on top of the general principles set out of the generality of crowdfunding service providers, par. 2 (second subparagraph) singles out those engaging in individual portfolio management of loans, which have to put in place “adequate systems and controls for the management of risk and financial modelling for that provision of services and that it complies with the requirements set out in Article 6(1) to (3)”.

more financial instruments” (see art. 4, par. 1, point 8 and Annex I, point 4 of Directive 2014/65/EU, and art. 25 for the suitability test).

The contract of portfolio management is centred around the mandate given to the intermediary. Indeed, it is substantiated in the service whereby the client delegates the intermediary to carry out i) the investment choices relating to a given portfolio (consisting of a set of fungible values whose investment can be diversified on the basis of the client’s financial needs) as well as ii) the set of activities necessary for such choices to be translated into operational terms²⁶.

In the case of portfolio management of loans, the law is much more detailed in indicating the parameters that inform the mandate underlying the service, which, to a certain extent, finds its reason on the circumstance that the crowdfunding service provider does not take any risk on its own, and, rather, the risks remains entirely on the investor²⁷.

Despite the clear, and meaningful, differences between those two services, in both cases, the information collected from clients is essential²⁸, and in the case of the individual portfolio management of loans, the disclosure obligations are particularly demanding as the next paragraph will show.

4. Where a crowdfunding service provider offers individual portfolio management of loans, it is subject to a very tight set of transparency and disclosure obligations. First off, in line with the relevance of the mandate, the provider must keep record of the mandate given and of every loan in an individual portfolio (see art. 6, par. 3)²⁹. In order to fill in the asymmetric gap between the weak and the

²⁶ See R. LENER, *Le società di gestione del risparmio nel regolamento Consob di attuazione del T.U.F.*, 1998, p. 1121 ss.

²⁷ See EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), p. 4.

²⁸ For portfolio management, see ESMA, Guidelines on certain aspects of the MiFID II suitability requirements, 06 November 2018 | ESMA35-43-1168.

²⁹ The crowdfunding service provider must keep records of the mandate and of every loan for at least three years after its maturity date on a durable medium.

strong party to the contract³⁰, and thus make sure that the investor is always aware of what risks they are exposed to and promptly informed, the crowdfunding service provider is required to provide a wide set of pre-contractual information as well as other relevant information during the execution of the contract. As for the pre-contractual phase, besides the marketing communications (which are regulated in art. 27 and 28 ECSFR for all crowdfunding service providers), the crowdfunding service provider offering individual portfolio management of loans must draw up, and make available to prospective investors, a key investment information sheet (KIIS) at platform level containing a very detailed set of information about the provider itself and its service (see art. 24 ECSFR³¹).

The key investment information sheet at platform level must be fair, clear and not misleading. It must be presented on a stand-alone, durable medium that is clearly distinguishable from marketing communications. Furthermore, the crowdfunding service provider is asked to keep the key investment information sheet

³⁰ See e.g. N.M. MOLONEY, *How to protect investors: lessons from the EC and the UK*. Cambridge: Cambridge University Press, 2010, pp. 194 –196; P. ŠEVČÍK, *Financial Contracts and the Political Economy of Investor Protection*, in *American Economic Journal: Macroeconomics* 4, no. 4, 2012, pages 163–97. <http://www.jstor.org/stable/23269723>; D. M. IBRAHIM, *Underwriting Crowdfunding* (February 18, 2020), in *Stanford Journal of Law, Business, and Finance*, Vol. 25, 2020, available at SSRN: <https://ssrn.com/abstract=3540296>; C. STEPHEN, *Regulating Investors Not Issuers: A Market-Based Proposal*, 88 *CAL. L. REV.* 279, 283 (2000) (“[A]n investor who lacks information on individual issuers might have good information on intermediaries, such as broker-dealers, mutual funds, or exchanges. Such investors will select intermediaries that offer desired investors protections.”).

³¹ See also Annex I on the “key investment information sheet”. Part i) is dedicated to the information on individual portfolio management of loans to be provided by crowdfunding service providers: “(a) Identity, legal form, ownership, management and contact details of the crowdfunding service provider; (b) The minimum and maximum interest rate of loans that may be available to investors’ individual portfolios; (c) The minimum and maximum maturity date of loans that may be available to investors’ individual portfolios; (d) Where used, the range and distribution of risk categories that loans fall into, as well as the default rates and a weighted average interest rate per risk category with a further break down by the year in which the loans were granted through the crowdfunding service provider; (e) The key elements of the internal methodology for credit risk assessment of the individual crowdfunding projects and for defining the risk categories; (f) If a target rate of return on investment is offered, an annualised target rate and the confidence interval of this annualised target rate over the investment period, taking into account fees and default rates; (g) Procedures, internal methodologies and criteria for selection of the crowdfunding projects to the individual portfolio of loans for the investor; (h) Coverage and conditions of any applicable capital guarantees; (i) The servicing of portfolio loans, including in situations where a project owner does not meet its obligations; (j) Risk diversification strategies; (k) Fees to be paid by the project owner or the investor, including any deduction from the interest to be paid by the project owner”.

at platform level updated at all times and for the duration of the crowdfunding offer. Consistently, it must immediately inform the investors who have made an offer to invest or expressed an interest in the crowdfunding offer about any material change to the information in the key investment information sheet (see art. 24, par. 3. ECSPR). The relevance of the KIIS and its practical implications are also confirmed by the liability regime. In this case, the regulation is relying on national jurisdictions – as foreseeable, due to the national differences that exist in this ambit – in order to ensure the responsibility of the crowdfunding service provider for the information given in a key investment information sheet at platform level³². Indeed, along those lines, art. 24, par. 5 requires Member States to ensure that “their laws, regulations and administrative provisions on civil liability apply to natural and legal persons responsible for the information given in a key investment information sheet at platform level, including any translation thereof, in at least the following situations: (a) the information is misleading or inaccurate; or (b) the key investment information sheet at platform level omits key information needed to aid investors when considering whether to invest through individual portfolio management of loans”.

As for the contractual phase, the crowdfunding service provider is required to provide – on a continuous basis and upon the request of an investor – via electronic means at least the following information on each individual portfolio: i) the list of individual loans of which a portfolio is composed; ii) the weighted average annual interest rate on loans in a portfolio; iii) the distribution of loans according to risk category, in percentage and absolute numbers; iv) for every loan of which a portfolio is composed, key information, including at least an interest rate or other compensation to the investor, maturity date, risk category, schedule for the repayment of the principal and payment of interest, compliance of the project owner

³² See art.24, par. 4, ECSPR. In particular, it states that “those responsible for the key investment information sheet shall be clearly identified in the key investment information sheet at platform level by, in the case of natural persons, their names and functions or, in the case of legal persons, their names and registered offices, as well as declarations by them that, to the best of their knowledge, the information contained in the key investment information sheet is in accordance with the facts and that the key investment information sheet makes no omission likely to affect its import”.

with that instalment payment schedule; v) for every loan of which a portfolio is composed, risk mitigation measures including collateral providers or guarantors or other types of guarantees; vi) any default on credit agreements by the project owner within the past five years; vii) any fees paid in respect of the loan by the investor, the crowdfunding service provider or the project owner³³.

This demanding set of information that the crowdfunding service providers are required to provide to investors in the different phases of their relationship is crucial as it allows, *ex ante*, the choice of investment and, *ex post*, the evaluation of the results produced by the management activity (by means of the individual mandate that is given by the investor).

In order to ensure adequate and comprehensive investor protection, art. 6, par. 7, ECSPR entrusts the EBA, in close cooperation with ESMA, with the task of developing draft regulatory technical standards to specify the information that must be provided to investors so that they are adequately informed about the risks related to investments made through individual loan portfolio management³⁴.

In this regard, the EBA's Consultation Paper on "Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding

³³ See art. 6, par. 4. Furthermore, in case the crowdfunding service provider has carried out a valuation of the loan, it should also provide the investor with the following pieces of information: (i) the most recent valuation; (ii) the valuation date; (iii) an explanation as to why the crowdfunding service provider conducted the valuation; and (iv) a fair description of the likely actual return, taking into account fees and default rates.

It is worth noticing that the crowdfunding service provider may establish and operate a contingency fund for its activity related to the individual portfolio management of loans. In such a case, it must provide additional information to the investors, and namely: i) a risk warning specifying the nature of the contingency fund and the rights stemming from it; ii) a description of the policy of the contingency fund. Additionally, a crowdfunding service provider that has established and operates a contingency fund must also provide information about the performance of the fund to the public on a quarterly basis (in particular in relation to the size of the contingency fund compared to the total amounts outstanding on loans relevant to the contingency fund and the ratio between payments made out of the contingency fund to the total amounts outstanding on loans relevant to the contingency fund). For all the details about the additional information requirements associated with the contingency fund, see art. 6 par. 5 and 6 ECSPR.

³⁴ Art. 6, par. 7, ECSPR mandates the European Banking Authority (EBA), in close cooperation with ESMA, to develop draft regulatory technical standards (RTS) designed to specify the type of information to be provided to investors in order for them to gain an adequate understanding of (i) the potential risks of investments and (ii) the ability of service providers to analyse the credit risk of crowdfunding projects and the owners of such projects, as well as (iii) the methodologies used to assess risk.

service providers” confirms overtly the connection between the nature of this service, the relevance of the underlying mandate and the importance of the adequate disclosure of information to investor. Indeed, the mandate provides the crowdfunding platform with a number of requirements that the projects to be financed must fulfil, and the service provider will allocate the investor’s funds accordingly. Therefore, “when dealing with the allocation of their funds to a portfolio of loans by a crowdfunding service provider, it is important that investors are appropriately informed about the risks they are exposed to”³⁵. These risks may originate from the following circumstances: i) investors may underestimate the risks of their investment, assuming that every loan and project within a portfolio is subject to an adequate risk assessment process; ii) as crowdfunding is particularly relevant for small businesses and start-ups, often with little or no credit history, investors relying on these platforms may not be fully aware of

the real quality of borrowers and may find it difficult to appreciate the risks involved for each of the loans in the portfolio³⁶.

To overcome those risks, the EBA consultation paper puts forward an articulated set of rules projected at protecting the investor through disclosure information. The accuracy and reliability of information provided to investors rest on ensuring that “a. the data used to conduct the assessments of creditworthiness [...] are consistent, complete and appropriate; b. The measurement techniques are appropriate to the complexity and level of the risks underlying the single crowdfunding projects and/or the portfolios, are based on reliable data, and subject to periodic validation; and c. The procedures related to data management are robust

³⁵ EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), p. 7.

³⁶ EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), p. 4.

well documented, reliable and regularly updated”³⁷.

An essential part of those draft RTS is represented by the obligations enshrined in Chapter 2 on the “elements to be included in the description of the method to assess credit risk”. Indeed, investors are to be provided with a clear and precise description of the method to assess both credit risk of individual crowdfunding projects within a portfolio and credit risk at investor’s portfolio level³⁸. The RTS list a comprehensive set of elements to be necessarily included in those descriptions. The crowdfunding service provider must also provide adequate information on the models used for the credit risk assessment of crowdfunding projects, the creditworthiness assessment of project owners, the credit approval and monitoring processes and the composition of portfolios³⁹.

This compelling amount of information to be provided to the investor is most certainly the result of the major difference that exists between crowdfunding and traditional banking intermediation. The crowdfunding service provider merely facilitates the match between project owners/borrowers and investors but does not take any borrowers’ risk of its own. The risk stemming from the creditworthiness of borrowers remains entirely on the investor. Furthermore, the asymmetric information between lenders and project owners may increase the chance that the investor does not adequately consider the riskiness of an investment, possibly since they rely on the risk assessment process undertaken by the platform. This asymmetry of information is exacerbated in the case of the individual management of portfolio of loans, since the crowdfunding service provider allocates a pre-determined amount of funds of an investor to one or multiple crowdfunding projects, in accordance with

³⁷ EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), art. 1, p. 15.

³⁸ See art. 3 and 4 respectively, EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), art. 1, p. 16.

³⁹ See art. 6, EBA Consultation Paper on the Draft Regulatory Technical Standards on Individual Portfolio Management of loans offered by crowdfunding service providers under art. 6(7) Regulation (UE) 2020/1503, (EBA/CP/2021/22), art. 1, p. 18.

an individual investor's mandate. Against this backdrop, the ECSPR and the prospective RTS developed by the EBA devote much effort in enabling the investor to take a well-informed decision about the projects and the project owners they are financing through the crowdfunding platform. This decision rests on information disclosure and on a very heavy set of transparency obligations bearing on the shoulders of the crowdfunding service providers.

5. The advent of crowdfunding services is raising fundamental questions on the "what" and the "how" of modern financial intermediation. What is "investment", and what is "lending/borrowing" when bringing together project owners and investors? How are those three types of actors – the project owners, the investors and the crowdfunding service providers – interacting with each other? The ECSPR might seem to be blurring the traditional "silo thinking" in favour of a consolidated approach focusing on a well-functioning relationship between the three parties involved in the provision of a crowdfunding service. An insightful example of this comes from the individual portfolio management of loans.

The service of *individual portfolio management of loans* is one of its kind and must be regarded separately from the other services provided by crowdfunding platforms. This is straightforwardly demonstrated by the set of provisions building up the general principles applicable to all crowdfunding service providers and the provisions specifically regulating individual portfolio management of loans. As practice will likely show, the characterisation of this service (thus, its legal implications and consequences) derives from the mandate (and the parameters therein) the service provider has to stick to in offering the portfolio management. This will be crucial due to the risks the investor is exposed to. Indeed, it is worth remembering that the investor will be suffering any loss resulting from a borrower's failure to repay a loan.

A traditional and a very well-known problem regarding investor protection is asymmetric information between the investor and the provider of investments

products. Financial products marketed on crowdfunding platforms are – as the analysis above also shows – not like traditional investments or savings products, and the informational gaps between the crowdfunding service provider and the investor might be even more exacerbated. For this reason, the ECSPR is striving to overcome them by means of a particular stringent regime of disclosure requirements (and also by introducing requirements regarding entry knowledge test and simulation of the ability to bear losses). The ECSPR and the upcoming regulatory technical standards drafted by ESMA and EBA⁴⁰ seem designed to favour the integration of crowdfunding service providers into financial markets, demonstrating how important the policy-making strategy and the “regulatory touch” are in deciding the success, or the decline, of a new market trend. The way this emerging segment of the financial markets is regulated might bring in further perspectives to the important policy debates surrounding the completion of the Capital Market Union, in particular with regard to the thorny issues of regulatory coordination and consistency in the multifaceted financial regulatory landscape.

⁴⁰ See recital 71 ECSPR: “The Commission should be empowered to adopt regulatory technical standards developed by ESMA and EBA with regard to individual portfolio management of loans, complaints handling, conflicts of interest, authorisation as crowdfunding service provider, information to clients, default rate disclosure, the entry knowledge test and simulation of the ability to bear loss, the key investment information sheet and cooperation between competent authorities. The Commission should adopt those regulatory technical standards by means of delegated acts pursuant to Article 290 TFEU and in accordance with Articles 10 to 14 of Regulations (EU) No 1093/2010 and (EU) No 1095/2010.”