



# Crowdfunding report summary

Warsaw, November 2014

# Introduction

Crowdfunding has many faces. Charitable organisations have received support through this route, as have travellers, athletes, scientists and inventors, and the creators of such humble concepts as making potato salad—a project to which the public contributed over USD 55,000. But often crowdfunding is the main source of financing for innovative ideas which in the long run can drive economic development and positive social changes.

From this perspective, the role of crowdfunding can hardly be overestimated. It functions as the missing link in the chain of financing of the economy, providing an influx of capital to places traditional forms of financing do not reach because of the high risk. Thanks to crowdfunding, there is a growing likelihood that the creators of many innovative concepts will succeed in commercialising their inventions and knowledge.

Crowdfunding has vast potential in contemporary economies. According to figures from the European Commission, in 2012 some half a million projects were carried out thanks to crowdfunding. Estimates indicate that the value of financing obtained in this way in 2013 approached a billion euro. In Poland as well, crowdfunding platforms are appearing and enjoying growing interest from internet users. The first spectacular successes of crowdfunding

campaigns are appearing here. An example is Aneta Kopacz's documentary *Joanna*, which won awards at numerous film festivals and through the cultural platform [wspieramkulture.pl](http://wspieramkulture.pl) and a mailing of promotional materials managed to raise almost PLN 40,000 from 442 people in less than three weeks. And it was largely thanks to a successful crowdfunding campaign that Zbigniew Bródka could attend the Olympic Games in Sochi—where he won a gold medal in speed skating.

But is the basic idea of crowdfunding new at all? Largely no, as demonstrated for example by the fact that Poland adopted a Public Fundraising Act back in 1933. But in the internet era crowdfunding is much more than traditional public fundraising. Without a global network it was impossible to achieve the effect of scale to which crowdfunding now owes its growing success. The technology of the internet has raised this concept to an entirely new level, as it has also done to many other existing phenomena. Just as Netflix is more than a video rental counter, YouTube is more than an updated version of television, and Uber is more than a local taxi service, crowdfunding opens up entirely new possibilities for raising funds notwithstanding its similarities to earlier forms of public fundraising.

Numerous different models of crowdfunding have already developed. Some of the simpler

models are reminiscent of traditional public fundraising, but thanks to the internet occurring on an incomparably larger and more global scale. But there are also much more advanced crowdfunding structures based on a model of equity or credit financing, leading to formation of complex legal relationships between the beneficiary and the funders.

Online social financing is not yet subject to special regulations under Polish law. The regulations governing public fundraising were updated not long ago, but these regulations have little practical application to new forms of crowdfunding. It should be assumed that as in the case of most new social phenomena, crowdfunding will also sooner or later face its own set of regulations. The purpose of our report is to identify the most important legal issues which the legislature should address in this case.

We attempt in our report to submit the phenomenon of crowdfunding to a legal and tax analysis from the point of view of all stakeholders: funders, beneficiaries (project

designers), and crowdfunding platforms. We suggest changes in the law which could help to fully exploit the positive potential of crowdfunding.

We limit ourselves to a presentation of the legal aspects of crowdfunding in the context of Polish law. But we realise that this perspective may not be enough. Many crowdfunding platforms extend their reach to numerous jurisdictions. In the case of such platforms, it will be necessary to analyse other legal systems as well to obtain a complete picture of the legal conditions for crowdfunding. There is a debate underway on introduction of crowdfunding regulations at the European Union level, but it is still at an early stage.

This report was prepared on the basis of Polish regulations in force as of 8 September 2014.

We should stress that the views and theories presented here are the personal views of the authors and must not be treated as a legal opinion or a formal statement by Wardynski & Partners.



# Summary

1. **Absence of specific regulations.** Under the current state of the law, there is no comprehensive and systematic regulation of crowdfunding. While this creates an opening for development of extremely varied forms of social funding, it is also makes it difficult to determine the substance of the legal relationships between the participants in crowdfunding platforms and thus to fully and precisely establish the rights and obligations of specific users of such platforms.
2. **Problems determining the substance of legal ties.** In the case of many crowdfunding platforms, the nature of the legal relationship between the funder and the beneficiary is inadequately defined. This could generate controversy if a dispute arises between funders and beneficiaries. In this context it would be worthwhile to consider imposing an obligation on crowdfunding platforms to publish a statement defining the legal relationship created between beneficiaries and funders. Undoubtedly this would increase the transparency of crowdfunding platforms. The substance of the legal relationship would obviously differ depending on the specific crowdfunding model.
3. **Patterns for legal relationships.** Lawmakers should also consider laying down patterns for the legal relationships that arise between funders and beneficiaries under various crowdfunding models. Such patterns could be applied in situations where a party (in practice, the platform operator) has not expressly modified the pattern. The patterns could also specify rules which the parties are not permitted to modify. However, this solution should be approached with great caution. Imposition of form contracts should not excessively limit the freedom of creators of crowdfunding platforms.
4. **Status of funds transmitted to platforms.** The lack of comprehensive crowdfunding regulations makes it unclear what the status is of funds entrusted to the operator of a crowdfunding platform. Most crowdfunding models provide that the funds should be held for some time by the operator (e.g. until the target amount of funding has been raised). From the perspective of users, it would clearly be desirable to have a solution that excludes funds on temporary deposit from attachment in the case of execution and automatically excludes such funds from the bankruptcy estate. For example, requiring operators to use escrow accounts as provided in the Banking Law could be considered, or other solutions of a similar nature. Regulations prohibiting operators from using deposited funds for their own purposes would also be

desirable. At the time, operators might be permitted to invest the funds entrusted to them in appropriately safe and liquid assets.

The provisions of the Payment Services Act concerning funds held by payment institutions could serve as a pattern in this respect. In this context, it would also be worthwhile to consider requiring platform operators to maintain records of payments made by funders enabling payments to be easily traced to specific users, for example in the event of the operator's insolvency.

5. **Protection of funders.** Because the legal status of crowdfunding platforms is unclear, the level of protection of platform users is in many instances lower than in the case of other legal relationships of a comparable nature (e.g. investment funds). In particular, there are no uniform rules governing the scope of information that should be provided to funders and beneficiaries.
6. **Consumer regulations.** Consumer regulations raise doubts in the context of crowdfunding. For the most part the regulations are fairly clear, but in some cases they are not suited to the specifics of crowdfunding, e.g. on issues concerning delivery of items by a business in a contract concluded at a distance.
7. **Intellectual property.** For project designers, using crowdfunding platforms carries a risk of exposure of their ideas. One of the necessary elements of both market and financial success of a crowdfunding project is for the project designer to adequately prepare and secure its own rights and protect against

infringing the rights of others. In the case of online crowdfunding, haste is certainly to be avoided, and a creator seeking financing must be well prepared to sell the project to funders. And as early as possible given the nature of the concept, the creator should secure its rights using the available legal means.

8. **Protection against dishonest beneficiaries.** From the funders' point of view, protection against dishonest recipients is vital. Current regulations do not clearly resolve whether or when a funder can demand refund of a payment or withdraw financial support provided to a beneficiary. In our view, it would be worthwhile to consider introduction of a statutory catalogue of situations which would entitle a funder to demand a refund (for example if the recipient used the funds for a purpose entirely different from that presented on the crowdfunding platform).
9. **Equity-based and credit-based crowdfunding.** Under current law, equity-based and credit-based crowdfunding undoubtedly generate the most regulatory difficulties. It appears that in both instances, an appropriate strategy for regulating these crowdfunding models is essential. Without legislative intervention, operators of crowdfunding platforms under either the equity model or credit model will be exposed to a risk of operating illegally. Hence they may refrain from creating appealing new crowdfunding models out of a concern over potential legal consequences resulting from the lack of clear regulations. In light of the positive potential of both of these crowdfunding models, creation of a regulatory

environment encouraging activity of this type should be considered.

**10. Trading in shares of private companies.**

Crowdfunding is yet another phenomenon revealing that some institutions of commercial law have not been adapted to the realities of economic life, particularly innovative activity. The statutory requirements for trading in shares of limited-liability companies are holding back the growth of equity crowdfunding in Poland.

**11. Capital markets law.**

The capital markets regulations currently in force in Poland do not provide a legal framework specifically governing equity crowdfunding or facilitating further growth of this form of raising capital. It is possible to structure crowdfunding projects so that the extensive formal requirements imposed on raising equity through public offerings and on the activity of investment funds do not limit the possibility of raising funds through equity crowdfunding. But this raises the concern that in such cases, protection of fundamental interests of funders is being overlooked, and whether they have the means at their disposal to protect their interests both individually and collectively.

**12. Payment services.**

Although intermediation in payments made by operators of crowdfunding platforms will be a payment transaction for purposes of the Payment Services Act, it should be assumed that in most instances operators will not be required to obtain a licence to perform payment services. This is because most platforms meet the conditions to qualify for the exclusion set forth in Art. 6(2) of the act.

**13. Money laundering.** At this time, most crowdfunding platforms based on the simplest crowdfunding models (grants, advance sales or prize-based) need not be subject to the regulations set forth in the Act on Combating Money Laundering and Financing of Terrorism. However, platforms based on an equity or credit model may fall under these regulations in certain situations (mainly because such models may imply that the operator of the platform is conducting a form of regulated activity covered by the act). A more systemic solution should be considered in this context. First it should be determined to what degree crowdfunding platforms are susceptible to abuse for money laundering purposes. Then it should be considered whether each type of crowdfunding activity should be subject to the Act on Combating Money Laundering and Financing of Terrorism, and if not, what exclusion criteria should be adopted (e.g. by amount, by analogy to the treatment of electronic money).

**14. Currency exchange.** Because of the limitations implied in the definitions set forth in the Foreign Exchange Law, operators of crowdfunding platforms need not enter their activity in the register of bureaux-de-change maintained by the President of the National Bank of Poland so long as they do not exchange currency in material form (banknotes or coins). Nonetheless, conducting currency exchange may require the operator of a crowdfunding platform to comply with money laundering regulations.

**15. Taxes.** The varied nature of crowdfunding, combined with a lack of regulations directly governing taxation

of social financing or interpretations of tax law addressing crowdfunding, requires familiarity with numerous tax regulations and the details of the specific venture and model of crowdfunding in order to determine the entity that bears the tax obligation and the amount of tax that should be paid. But these aspects are unclear for participants in social financing. This may discourage them from becoming involved in projects. This also makes it difficult to assess the true profit on a venture and may open up a risk that payments may be questioned, possibly even leading to criminal tax liability. Unleashing the potential of crowdfunding may therefore require intervention in the area of tax legislation. This should be undertaken cautiously, with due regard to the specifics of the market as well as the solutions adopted in other countries or in guidelines from the European Court of Justice (if and when they appear). On the other hand, the multiplicity of forms of social financing subject to different taxation

rules means that the stakeholders—the creator, funders, and the operator of the crowdfunding platform—now have the freedom to frame the relationships between them and therefore have at least some influence over the tax burdens. But this now requires an in-depth analysis on a case-by-case basis.

16. **Legislative initiatives.** Adoption of crowdfunding regulations in Poland or at the EU level should not be expected in the immediate future. The plan is to monitor the market and test the adequacy of the existing regulations. Decisions on what steps to take next may come in 2015.

17. **Innovative potential and legal challenges.** In its current form, crowdfunding appears to be just the beginning of new forms of financing. Its evolution may follow in the direction of the use of alternative forms of property (such as Bitcoin) in financing of projects. This carries with it numerous legal challenges which will have to be dealt with in the future.



# New Technologies Practice

For us, new technologies are all about new legal challenges. In many instances, we must tackle doubts surrounding the legal treatment of innovative products and services or an absence of relevant regulations. To assure clients legal security in such circumstances, lawyers must bring to the table experience, creativity, and an understanding of the business environment.

Therefore we have created an interdisciplinary New Technologies Practice within the law firm, bringing together highly skilled practitioners from selected fields of law. We are supported by technology experts cooperating with the firm and offering a wide range of technical knowledge.

We strive to meet our clients' needs as they arise by creating highly specialised legal services addressed to specific segments of the new technologies market. We provide comprehensive regulatory, tax and transactional advice.

Based on our existing experience, we have identified the following areas of our practice: biomedical and modern foods, creative industries, crowdfunding, cybersecurity, e-commerce, financing of new technologies, gaming, information technology, new payment solutions, new technologies in searching for energy, public-private partnership projects (PPP), protection of privacy, research and development (R&D), telecommunications.



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# About Wardyński & Partners

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The firm's practice is focused on such areas as arbitration, banking, bankruptcy, capital markets, competition law, corporate law, dispute resolution, employment law, energy law, environmental law, EU law, infrastructure projects and public-private partnership, intellectual property, maritime law, mergers and acquisitions, pharmaceutical law, project finance, public procurement, real estate, tax and tax disputes, and technology, media and telecommunications.

The firm is the owner of In Principle, a web portal for managers and lawyers, where we write simply about complicated legal issues that may have an impact on business. In Principle was created through a merger of the firm's Litigation Portal and Transactions Portal.

The firm is also the publisher of Wardyński+, the first Polish-language app on legal topics for iPad and Android. The app is available free of charge at the App Store and Google Play.

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