EQUITY CROWDFUNDING:

LEGAL FRAMEWORK IN ESTONIA

11 March 2015

Memorandum

BORENIUS

ATTORNEYS AT LAW

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LIST OF DEFINITIONS

ECRS	Estonian Central Register of Securities
FIN-FSA	Finnish Financial Supervisory Agency
FSA	Estonian Financial Supervision Authority
MTF	Multilateral trading facility
OTF	Organised trading facility

INTRODUCTION

Crowdfunding is a relatively new way of financing projects by obtaining funds from the public. The expression "crowdfunding" refers merely to a channel of financing, which can be used in many different ways. Broadly, crowdfunding can be divided into three types:

- donation, rewards or pre-sale based funding, called crowd sponsoring;
- loan based funding promising to pay back the capital on specified terms, called crowd lending;
- profit sharing and securities based funding, called crowd investing or equity crowdfunding.

While crowdfunding is not an entirely new concept, the use of respective online platforms and practices for attracting local and international investors needs to comply with the existing regulations, which have not been designed bearing crowdfunding in mind. Legal entities are established and governed in Estonia in accordance with the Commercial Code. The relevant regulatory framework in Estonia is based on among others the Directives on Prospectus, Payment Services, Markets in Financial Instruments (MiFID), Capital Requirements (CRD IV) and Distance Marketing of Financial Services.

Some European countries such as Germany, the Netherlands, Belgium and Finland have addressed the concerns around crowdfunding through guidelines, and many others (Italy, the UK, France and Spain) are considering or have taken regulatory action. The Estonian Financial Supervision Authority (FSA) has not provided any guidelines on crowdfunding.

There are no equity crowdfunding platforms actively operating in Estonia today, which has resulted in Estonian companies seeking investments through international platforms using international holding companies for such purpose. Fundwise, crowd investment platform created in 2014, is still in the early testing stage and has not yet launched for wider public. There are crowd sponsoring (Hooandja), crowd lending (Bondora) and crowd debt financing (Investly) platforms operating in Estonia.

A typical equity crowdfunding platform allows to raise and invest capital as described below:

- entrepreneurs create campaigns and seek funding through platform, such entrepreneurs (the target companies to be financed) are called campaigners. The campaigners are allowed to start campaigns after approval from the platform;
- the campaigners are required to disclose certain information (financial information, information on products etc.) in order to start and run a campaign;
- the campaigns are actively marketed by campaigners through social media and other channels;
- the platform is a meeting place for the campaigners and investors allowing them to exchange information through Q&A sections or otherwise;
- during the campaigns the investors commit to invest or are alternatively required to transfer the funds in order to participate;

- there is no investment obligation and already transferred funds will be returned if the campaign is underfunded and fails;

- the campaigners are allowed to choose the investors or accept any amount beyond the initial target if the campaign is overfunded;

- some platforms mediate payments, i.e. by collecting, holding and transferring the investment amounts to campaigners. In such case the investors are required to use special accounts opened with the platform;

- some platforms serve only as a meeting place and all payments are made without the platform's involvement. In such event the campaigners provide the investors with transfer instructions. Sometimes third-party payment services are used (e.g. PayPal);

- depending on the platform the investors receive the shares directly or hold those through the platform acting as a nominee.

While most equity crowdfunding platforms do not provide advanced syndication solutions, lead investors operate in the context of equity crowdfunding similarly to other means of financing. Semi-crowdfunding platform AngelList specifically enables investors (called backers) to co-invest with other notable investors (called leads). Such solution is called syndication and through this the backers get access to the leads' dealflow and benefit from their experience in picking and managing investments. In return the leads get fees from backers and leverage on their personal investments. However, AngelList is not a typical crowdfunding platform as it accepts only high net-worth individuals or professionals to join the platform. On most other platforms syndication may be arranged in a less organised manner.

The purpose of this memorandum is to provide a summary of the legal and regulatory framework applicable to campaigners, investors and equity crowdfunding platforms in Estonia, highlighting and addressing problematic areas. The memorandum will help to determine the best form and method for raising capital through a platform in Estonia. In addition, the memorandum includes proposals to amend legislation in order to facilitate raising capital through local crowdfunding platforms.

The memorandum is divided into four sections. The first section concentrates on campaigners, the second addresses investors, the third focuses on platforms and the fourth sets out the main conclusions.

1 THE CAMPAIGNER

In order to attract equity crowdfunding type of financing for a business or project, the entrepreneurs need to incorporate an entity. The most common forms of corporate entities in Estonia are private and public limited companies. The key characteristics of such companies from equity crowdfunding perspective have been discussed below. We have also considered certain alternatives to these commonly used corporate forms.

1.1 PRIVATE LIMITED COMPANY

1.1.1 General

A private limited company (in Estonian: *osaühing*) is a company which has share capital divided into private limited company share units. It is the most common form of business in Estonia due to its simple and rapid registration and more liberal legal requirements compared to public limited companies (in Estonian: *aktsiaselts*).

1.1.2 Share capital and share units

General

A private limited company is required to have a share capital of at least EUR 2,500 compared to a public limited company, which has to have a share capital of at least EUR 25,000. This is one of the reasons practically all start-ups are formed as private limited companies.

However, the shareholders' participation in private limited companies are not represented by shares but share units, which is an unknown concept for many foreigners and may need to be explained in case a campaigner looks for international funding as a private limited company. The main difference is that each shareholder is able to hold only one share unit and the proportions between the shareholders are determined by the nominal value of share units that will change if an additional share unit is acquired or part of it is sold.

From the crowdfunding perspective a share unit has one considerable downside – it must be a multiple of EUR 1. This in result may limit the number of investors and may give too high percentage in the company's share capital depending on the amount of company's share capital before the funding round. For example, if the campaigner's share capital is EUR 2,500 and it raises additional capital in exchange for approx. 16.67%, then the campaigner can raise funds from maximum of 500 investors and minimum shareholding can be 0.03% (the minimum share unit of EUR 1 represents 0.03% of the total share capital of EUR 3,000).

Therefore, in order to facilitate crowdfunding through private limited companies, decreasing the minimum nominal value requirement of a share unit is desirable. Another (more radical) solution would be to abandon the nominal value requirement entirely (requires abandoning share unit concept as a whole – see the following paragraph). In practice nominal value of a share unit has little relevance and abandoning minimum nominal value requirement would offer more flexibility in relation to funding. The same applies to public limited companies.

It should also be considered whether there is a need to maintain two different solutions to represent shareholders' participation in similar legal forms while the shares could be also used by private limited companies. Different capital and corporate governance

requirements could be established for private and public limited companies irrespective of the equity instruments used by such legal entities. From start-up industry standpoint it is strange that private limited companies having more liberal regulation compared to public limited companies need to comply with stringent and inflexible rules concerning the share units.

As to keeping records of shareholders, generally the share unit register of a private limited company is kept by the management, but the register may be also kept by the Estonian Central Register of Securities (ECRS), which is the only option available for public limited companies. Keeping the share unit register by the management or ECRS entails different procedure for transferring the share units, as further described below.

Issue of share units

Share capital of a private limited company has to be increased in order to provide the investors with new share units in return for their investments. This can be carried out under a resolution of shareholders supported by at least 2/3 of the share units represented at the shareholders' meeting or 2/3 of all votes if the decision is adopted without convening a meeting. The same applies to a public limited company. Having necessary votes in place for the increase is not a likely problem to a campaigner run and owned by founders, but it may be difficult after raising several rounds of funds from angels, VCs or through crowdfunding.

The procedure for increasing share capital is similar for private and public limited companies. However, the legislation currently in force states that in case of a private limited company the resolution on capital increase has to list the investors personally. As a result, the capital increase could be resolved only after the investors are known. It is not entirely clear if the entire increase procedure must be cancelled if one of the named investor fails to participate in the capital increase. Consequently, in practise the increase should be resolved based on a resolution adopted after the contributions have been paid to the campaigner. This opposes to the capital increase of a public limited company, which can be arranged based on a resolution adopted in preparation of the campaign with possibility to delete any unsubscribed shares.

Beginning from 1 July 2015 the resolution of a private limited company may refer to persons who have the right to subscribe the share units generally. The management board may, by a resolution of the general meeting, be granted the right to extend the subscription term or to cancel share units which are not subscribed for during the subscription term. This allows private limited companies to arrange capital increase based on a resolution adopted in preparation of the campaign.

However, in any event the capital contributions have to be made before receiving share units. This is because the share units will be considered issued after recording the increase with the Commercial Register. The recording, however, will be made only after a bank confirmation on the receipt of funds has been presented to the Commercial Register. The principle is the same for private and public limited companies and means that the investors must transfer the contributions to the campaigner before receiving any share units or shares.

The capital increase resolution has to be presented to the Commercial Register within 6 months as of its adoption. This in turn sets a time limit to preparation, campaign and investment periods.

Note that if the share units of the company are registered with the ECRS, the investors need to have a cash and securities account opened with an Estonian bank or use nominee services in order to carry out the increase (please see section "Transfer of share units" for more information). This in turn may delay issuing share units until all the necessary accounts are opened or arrangements for nominee services made.

In addition, private limited companies may be founded without paying in the contributions. However, until the complete payment of contributions by all the shareholders, the private limited company may not increase nor decrease the share capital, or make any payments to the shareholders. In order to avoid problems with issuing new share units, all contributions should be paid in by the founders in preparation of the campaign.

Beginning from 1 July 2015 it is possible to give the supervisory or management board the right to increase share capital up to 50% within 5 years by including such right in the articles. This allows increasing the share capital without organising a shareholders' meeting.

Classes of share units

As opposed to public limited companies, private limited companies are not currently allowed to establish different classes of share units. As a result, different rights have to be laid out in the articles either (i) personally in respect of an investor (e.g. Mr. J. Smith has the following rights) or (ii) with reference to the size of share units (e.g. the owners of share units with nominal value less than EUR 100 have the following rights). This in turn means that establishing different rights is cumbersome and does not provide necessary flexibility compared to the shares of a public limited company where different classes of shares can be issued.

Beginning from 1 July 2015 private limited companies are allowed to establish different classes of share units, similarly with public limited companies. Different rights have to be laid out in the articles. If a private limited company wishes to change the special rights of the shareholders holding certain type of share units, all shareholders holding that type of share units must agree to the change.

Transfer of share units

In principle the share units may be freely transferrable similarly to the shares of a public limited company. However, the articles may establish conditions that must be satisfied in order to transfer the shares. For example, the articles may establish that the consent of the shareholders' meeting, the management board or any other person is required. Without satisfying the established conditions the transfer of a share unit is void. If any such condition is established in the articles and not clearly stated during the crowdfunding process, the investors may unknowingly end up owning a share unit which is not freely transferrable. This in turn may harm investors' confidence to invest through crowdfunding. Therefore, it is in platform's interest to require that the campaigners disclose such conditions clearly during campaigns or not allow such campaigners to participate.

It should be also noted that under the law the other shareholders have the right of pre-emption upon transfer of a share unit to a third person during one month period after presentation of the transfer agreement to them. The articles may also exclude the pre-emption right and this is recommended in order to facilitate exit possibilities and keep

the transfer procedure simple. On the other hand the majority shareholders may want to retain such right.

While issue of shares can be arranged without involving a notary, share unit transfer agreements must be notarised. This means that the signatures of the parties must be certified and also the contents must be explained by a notary. For this reason the transfer agreements can be concluded only before Estonian notaries where all parties or their representatives have to be present. Note that notaries are entitled to their fees based on transaction value. Therefore, transferring a share unit is very cumbersome and potentially costly, which may serve as another hurdle to attracting investments. This applies especially for foreigners as they need to travel to Estonia or authorise someone in Estonia to carry out the sale under notarised power of attorney.

The notarisation obligation will not apply if the share units are registered with the ECRS, which is mandatory for public limited companies. In such case the sale can be carried out by submitting a transfer order without signing any agreement. It seems to be a good alternative, but it may also hinder seeking financing as registering share units with the ECRS requires all shareholders to have cash and securities accounts with an Estonian bank. Opening such accounts is a straightforward matter for persons in Estonia. However, it takes several weeks to open accounts for foreigners. Therefore, it is quite difficult for a foreigner to acquire share units registered with the ECRS.

An alternative is to hold registered share units through a nominee account administrated by the foreigner's home bank if such bank has access to the ECRS directly or through other banks. The downside is that in such case the foreigner must conclude a separate agreement with his or her home bank for holding the share units.

From crowdfunding perspective both notarising the transfer agreements and having the share units registered with the ECRS will limit seeking investments from international investors. If share units are not registered, foreigners can easily acquire them but may face problems upon sale. Transferring share units is easier if the share units are registered but foreigners cannot acquire and hold them without opening necessary accounts or concluding required nominee agreements.

1.1.3 **Governing bodies**

Private limited companies have similar governing bodies as public limited companies: shareholders' (general) meeting, supervisory board and management board. The main difference is that a supervisory board is mandatory in case of public limited companies and optional in case of private limited companies. This is also one of the reasons why the majority of start-ups are founded as private limited companies – it enables to avoid involving additional persons for forming a supervisory board as well as additional bureaucracy accompanied.

1.1.4 **Shareholders' meeting and voting**

A successful crowdfunding campaign will often bring along many new shareholders and this will affect organising a shareholders' meeting which was not as complicated a task with a smaller number of shareholders. Although a crowdfunded company has to convene and hold shareholders' meetings strictly by the book, the rules are nevertheless suitable for a company with many local and foreign shareholders.

Both private and public limited companies are required to hold a shareholders' meeting at least once a year to approve the annual accounts. Naturally, the meeting may be

convened as often as required. Generally the meeting is convened by the management board and is allowed to adopt resolutions if more than 1/2 of the votes are present. The articles may set forth a higher quorum, which may not be in the interest of the campaigner, depending on the structure of shareholdings.

If the meeting fails to have quorum, the management board is required to call a new meeting without changing the agenda. The new meeting is allowed to adopt resolutions regardless of the number of votes represented at the meeting. Thus, necessary decisions can be adopted even if the campaigner has many passive shareholders.

At the same time it is easy for the investors to get involved in case of interest as votes can be delivered electronically if allowed under the articles. Further, it is also possible to adopt decisions without convening a meeting. The same applies in case of public limited companies.

In terms of convening meetings, the main difference between private and public limited companies is that private limited companies have to send notices on convening meetings to the addresses or e-mail addresses entered in the list of shareholders. Public limited companies are required to deliver notices by registered mail if there are less than 50 shareholders or by publishing notices in a daily national newspaper if there are more than 50 shareholders. Therefore, it is easier for private limited companies to convene meetings compared to public limited companies if there are less than 50 shareholders and the other way round if there are more than 50 shareholders. However, in the latter case the shareholders (especially international investors) will not be probably informed about the meeting.

The notice must be sent in such manner that under normal conditions of delivery it would reach the addressee at least one week before the meeting in case of private limited companies, and three weeks (or one week for convening extraordinary meeting) in case of public limited companies. Reference to "normal conditions of delivery" may in practice mean that the deadlines are considerably longer if there are foreigners involved as delivering a letter may take from days to weeks.

A resolution of private or public limited company shareholders is adopted if over 1/2 of the votes represented at the meeting are in favour. In certain circumstances 2/3 majority applies, e.g. for increasing share capital, changing the articles, merger and division. Thus, the initial shareholders should keep sufficient majority of shares also after the successful campaign in order to stay in control of the company.

1.1.5 **Audit obligations**

A private limited company must organise auditing of its annual accounts only if certain high thresholds are exceeded (e.g. revenue of at least EUR 6,000,000 or number of employees of at least 90) whereas auditing is always mandatory for a public limited company. This is yet another reason why most start-ups are formed as private limited companies as the thresholds will probably not be exceeded and auditing costs could thereby be avoided before the business grows to a considerable extent.

1.2 PUBLIC LIMITED COMPANY

1.2.1 **General**

A public limited company (in Estonian: *aktsiaselts*) is a company which has share capital divided into public limited company shares. Public limited companies are rarely used by

start-ups due to more stringent requirements compared to private limited companies. Nevertheless, public limited companies offer flexibility in terms of shares often necessary to regulate shareholders' relations as desired.

1.2.2 Share capital and shares

General

As already noted above, a public limited company is required to have a share capital of at least EUR 25,000 while a private limited company must have a share capital of at least EUR 2,500. The capital requirement is one of the reasons only a small number of start-ups are formed as public limited companies.

However, the shares of public limited company provide more flexibility compared to the share units of private limited company. First, unlike the concept of share units, the concept of shares is well-known for investors from all jurisdictions and it does not require any further explanation. Second, the minimum nominal value of a share can be EUR 0.1 instead of EUR 1 requirement applied to share units. Therefore, it is possible to involve 10 times more investors for the same shareholding in contrast to private limited companies.

As opposed to private limited companies, the share register of a public limited company must always be kept by the ECRS. This has effect on holding and transferring the shares as further described below.

Issue of shares

Share capital of a public limited company has to be increased in order to provide the investors with new shares in exchange for their investments. This can be carried out under a resolution of shareholders supported by at least 2/3 of the shares represented at the shareholders' meeting or 2/3 of all the shares if the decision is adopted without convening a meeting. If the public limited company has several classes of shares, at least 2/3 of each class of shares must be in favour.

The procedure for increasing the share capital is similar for private and public limited companies. The share capital increase resolution may be adopted in preparation of the campaign and the issue of new shares may be carried out based on such resolution with the possibility to delete unsubscribed shares. Hence, it is possible to present the capital increase resolution to the investors before they make contributions.

However, for the reasons explained above (bank confirmation required for recording the increase with the Commercial Register), the capital contributions still have to be made before receiving shares.

It is important to note that the capital increase resolution has to be presented to the Commercial Register within 6 months as of its adoption. This in turn sets a time limit to preparation, campaign and investment periods.

It is also possible to set out in the articles that the supervisory board may increase share capital up to 50% within 3 years from adopting the articles. This option provides public limited companies with a possibility to increase the share capital without a need to organise a shareholders' meeting immediately before or after a successful crowdfunding campaign.

Classes of shares

A public limited company may issue different classes of shares. This allows a public limited company to effectively involve investors with different rights. Shares with the same rights form a class of shares.

Different rights may relate to distribution of profits and liquidation proceeds. It is also possible to vary voting power by establishing different nominal value for shares belonging to each separate class of shares.

In addition, a public limited company may issue non-voting shares with preferential rights to profits and liquidation proceeds, i.e. preferred shares. Note that preferred shares may be issued only up to 1/3 of the share capital. There is no such limit in relation to other classes of shares.

Transfer of shares

The shares of a public limited company are freely transferrable and the only limitation could be the pre-emption right of other shareholders, if so established in the articles. It is not possible to set out conditions for the transfer in the articles as in case of a private limited company.

The shares have to be registered with the ECRS and this requires that each shareholder has a cash and securities account or nominee arrangement in place which, as already noted above, means in effect that a campaigner can mainly seek financing from investors based in Estonia. This clearly limits using public limited companies for crowdfunding purposes and may turn campaigners to use legal forms available in other jurisdictions.

1.2.3 Governing bodies

See section 1.1.3 above.

1.2.4 Shareholders' meeting and voting

See section 1.1.4 above.

1.2.5 Audit obligations

As explained above, a public limited company must organise auditing of its annual accounts in any case while a private limited company must audit them only if certain high thresholds are exceeded.

1.2.6 Squeeze-out

It may be difficult to arrange a trade sale of a crowdfunded company as some purchasers may only be willing to acquire 100% of the shares and not deal with the hassle of maintaining large number of minority shareholders.

The majority shareholder of a public limited company can squeeze out the minority shareholders for fair compensation. This option can be used by a shareholder representing at least 90% of the share capital. Squeeze-out can be carried out only under the shareholders' meeting resolution approved by 95% of the votes represented by the shares.

For a crowdfunded company it enables to buy out the crowd investors at a later stage if those investors hold less than 5% of the shares.

1.3 OTHER LEGAL FORMS

In addition to private and public limited companies the campaigners could also form themselves as general or limited partnerships. These are contractual based entities which means that there are no shares and each investor would become a party to the partnership agreement. The investor would not be able to sell its participation in the partnership, it would have to hand over its rights and obligations under the partnership agreement.

However, general partnerships are not suitable for equity crowdfunding purposes due to unlimited liability of investors and both forms of partnerships involve legal regulations that make the participation interests unattractive for investors. It is not realistic that many businesses would be willing to use the unfamiliar corporate form of an Estonian partnership even if it would enable to overcome any of the downsides related to private and public limited companies.

1.4 QUASI-EQUITY SOLUTIONS

A campaigner may also use quasi-equity solutions instead of share units and shares for raising capital through crowdfunding. Quasi-equity is a financial instrument aiming to reflect some of the characteristics of shares such as possibility to benefit from the profit and increase of value of the target company. All such instruments are in essence contractual and therefore subject to contract law principles.

It should be noted that quasi-equity instruments that can be converted into shares or share units cannot be effectively enforced. This is because issuing new share units or shares by the campaigner always requires the respective resolution of the shareholders (or supervisory or management board if so stipulated in the articles). However, the shareholders cannot be forced to vote in favour of capital increase. As a result the holders of such instruments can only claim compensation for damages from the campaigner and also from shareholders, if the shareholders are parties to such instruments. Such compensation claim has a potential to end up in a lengthy legal dispute due to lack of respective legal practice and difficulties in determining the loss of investors.

The public is probably not familiar with quasi-equity solutions and may therefore be distrustful in respect of those instruments, especially if offered by recently formed start-ups. Also, in view of lack of relevant rules and guidance, it should be subject to specific tax analysis how the profit related payments should be qualified and treated for tax purposes. Nonetheless, quasi-equity solutions provide the campaigners with a good alternative compared to the share units and shares that are especially difficult to be owned and/or transferred by foreigners under the legislation currently in force.

An alternative for traditional quasi-equity solutions that do not require issuing the respective share units or shares, a platform could consider holding issued share units or shares on behalf of and for the benefit of investors. In such case the platform would appear as shareholder in the list of shareholders kept by the ECRS (from practical perspective we do not see any reason for not registering share units in case of using the relevant services provided by the platform). The platform should follow the instructions of investors upon voting and transferring the shares. In case the platform mediates

dividend payments and capital gains to investors, the regulatory requirements described in section 3.2 below may be relevant.

Since Estonian laws do not recognise the concept of a trust, the downside of this arrangement is that in case the platform does not act as a licensed provider of investment services (see section 3.1 below), the share units or shares held by the platform on behalf of and for the benefit of investors would most likely be considered as the assets of the platform in case of its bankruptcy. In case the platform is licensed as provider of investment services, such share units or shares would be excluded from the bankruptcy estate.

1.5 THE ARTICLES AND SHAREHOLDERS' AGREEMENT

1.5.1 The articles

The intention to seek financing through crowdfunding does not require any specific requirements to be established in the articles. The articles should reflect the wishes of the shareholders. The shareholders may agree on the articles as they desire, subject to certain limitations established by the law. Although the shareholders may establish different regulations in the articles, the law establishes a set of norms that apply unless provided otherwise in the articles. These norms are different for public and private limited companies. Therefore, it is recommended to establish in the articles:

- whether pre-emption right will apply in case of sale;
- whether share units or shares may be pledged;
- whether to allow and set possibility to deliver votes electronically.

In case of private limited companies, the articles should also set out that the shares may be issued with a premium and also conditions for the transfer of shares, if such should exist.

1.5.2 Shareholders' agreement

Certain matters cannot be set out effectively in the articles, such as drag-along regulations and other exit strategies. This is one of the reasons why shareholders conclude separate shareholders' agreements in relation to companies.

A shareholders' agreement is inevitable if the intention is to get funding from angels or especially VCs as they usually require certain controlling rights and controlled exit mechanisms to protect investments. However, shareholders' agreements are often rather complicated documents and presenting such agreements to crowd investors may put them off as they are not willing to work through complicated documents or adhere to restrictive terms.

The solution would be to have a full shareholders' agreement between the majority and influential shareholders that would give necessary comfort to angels and VCs, and a separate more limited undertaking from the crowd investors. Such undertaking would include only the most important provisions, including the transfer restrictions, drag-along provisions and procedures in the case of new investments, perhaps even a waiver on certain minority rights.

It should be noted that a shareholders' agreement of a private limited company has to be notarised in case it contains an undertaking to transfer share units (such as drag-along) which have not been registered with the ECRS.

1.6 RULES APPLICABLE TO PUBLIC OFFERING OF SECURITIES

As a general rule, any offer of share units of private limited company, shares of public limited company or any other securities requires that the issuer company publishes a prospectus, unless an exemption exists. Prospectus is an information document providing details about the securities and the campaigner.

According to the EU law, no prospectus has to be prepared for rounds of less than EUR 100,000, and for rounds of EUR 5 million or more, an EU prospectus is required. This means that rounds of less than EUR 100,000 are eligible without a prospectus. As for rounds between EUR 100,000 and EUR 5 million, national prospectus rules apply.

In Finland a prospectus under the national prospectus rules needs to be prepared when the size of the round is EUR 1.5 million or more. In Sweden the limit is EUR 2.5 million and in both Norway and Denmark EUR 1 million. Baltic States are more demanding and a prospectus needs to be prepared if the campaigner intends to raise EUR 100,000 or more. It is worth considering if and to what extent raising the threshold in Estonia would facilitate investment activities without constituting serious threat to the interests of the public.

The different prospectus requirements also have a cross-border effect – the campaigner must comply with the regulations of all countries where the shares are being offered to the public. It is difficult to determine whether the shares are offered to Estonians, Finns or anybody else if offered through the Internet. While it is not clear how the FSA will act in such situation, the Estonian prospectus rules will not only affect Estonian start-ups but may also limit the Estonian investors' ability to invest into foreign start-ups as the platforms may limit Estonians to participate in financing rounds of EUR 100,000 or more.

The abovementioned euro limits are calculated over a period of 12 months. As a result the campaigners are able to organise financing rounds without being subject to public offering requirements until up to EUR 99,999 has been raised over a period of 12 months.

In addition to the euro limits described above, there are other exemptions from the prospectus requirements. Most commonly used are the "private placement" exemptions, which allow offering of shares to qualified (or professional) investors or to less than 150 non-qualified investors per EU/EEA member country without a prospectus. However, the mere fact that investors are required to register themselves with the platform in order to fund campaigns is not sufficient to consider offerings private.

An international example of overcoming the complexities associated with exceeding the applicable threshold is the private round function of Invesdor. When a round is private, potential investors are only able to see the teaser box regarding the campaigner. An interested investor needs to send a request to the target company to see the complete pitch, and the target company always decides whether it approves this particular investor to see the complete pitch or not. A round is always private when it is worth more than EUR 1.5 million (the applicable threshold in Finland). Although the rationale behind the private round function has not been described on the site, it obviously enables the campaigner to limit the type and/or number of investors and thereby fall under one of the exemptions of the prospectus rules.

Another example is US-based service AngelList which serves as a meeting place for entrepreneurs and sophisticated investors. The only people who are authorized to create accounts on the site are "accredited investors" as such term is defined by the SEC in its

rules (including wealthy individuals, banks, insurance companies, investment companies, large corporations etc.). An Estonian crowdfunding platform could consider a similar solution if the EUR 100,000 threshold is perceived as substantial limitation and the platform believes that it is possible to attract sufficient number of qualified investors.

The prospectus has to comply with the extensive and detailed requirements specified by local legislation and with Prospectus Regulation if the total value of the public offering is at least EUR 5 million. The prospectus must also be registered with and approval received from the FSA before disclosing it to the public. An obligation to follow such rules will clearly limit raising capital for EUR 100,000 or more in Estonia irrespective of the medium used for such financing.

Note that general corporate rules (e.g. share issue procedure, pre-emptive rights) also apply in case of public offerings. Please see sections 1.1.2 and 1.2.2 for more information.

1.7 OTHER APPLICABLE LEGAL REQUIREMENTS

There are no other material applicable legal requirements to be taken into account in seeking financing through equity crowdfunding. However, campaigners must comply with general requirements arising from contract and consumer protection laws.

2 THE INVESTOR

2.1 APPLICABLE REGULATIONS

There are no special regulations applicable to investors but the general company law principles may have different effect on Estonian and foreign investors. Although local and foreign investors are treated equally, it is easier for an Estonian investor to comply with those regulations. This especially concerns holding and transferring the share units or shares as it requires either (i) opening cash and securities account in an Estonian bank or nominee arrangement for holding the share units or shares; or (ii) notarisation of share transfer agreements.

2.2 LEAD INVESTOR

While syndication is not widely used by the crowdfunding industry, it allows less experienced investors (the backers) to benefit from professionals' (the lead) experience in picking and managing investments. For such reason syndication might be a functionality soon to be added to many platforms.

Provision of investment services

In Estonia, the lead investor must apply for an activity licence and is subject to supervision of the FSA in the event the lead is considered to provide any of the investment services set out in section 3.13.1. There is a risk that the lead investor will be considered providing one of the mentioned services, especially providing investment advice or organising an offer or issue of securities. Please see section 3.1 for applicable rules. It is essential that the FSA clarifies whether the activities of a lead investor will be considered as investment services subject to licensing and supervision of the FSA. Until such guidelines are missing, it is advised that the platform confirms envisioned syndication functionalities with the FSA in order to avoid possible sanctions on lead investors using the platform.

Organising a public offering

If the issue of shares or share units is considered a public offering and if in such event the lead investor offers investment opportunities to its backers during the syndication, it may potentially act as an offeror of a public offering. This in effect means that the lead is treated similarly to the campaigner and the lead is not entitled to offer such shares without a prospectus unless exceptions exist (see section 1.6). Likewise, the lead must follow the rules applicable to public offerings and may be held liable for information disclosed with regard to the campaigner or the offered securities (e.g. information in the prospectus).

Investment fund activities

In the event the lead investor collects investments from its backers and invests those on their behalf, the lead investor may be required to meet the regulation set forth for investment funds and their management companies, including obtaining an activity licence from the FSA and complying with the relevant extensive requirements and procedures. This is especially the case when the money is collected through the issue of securities in the lead investor vehicle.

An international example of crowdinvesting on behalf of others is Crowdcube Venture Fund managed by Crowdcube's co-operation partner Strathtay Ventures Ltd, authorised and regulated by the local financial supervisory authority in the UK.

Another example is US-based AngelList where investors may be participants in one or more syndicates set up as funds. Syndicates let investors earn carry when they syndicate their deals and give backers access to investment targets. Backers benefit from the lead's experience in picking and managing investments. Syndicate investors do not invest directly in the campaigner but a special purpose vehicle is created for each specific investment. Each fund is managed by Assure Fund Management and advised by the lead and a wholly-owned subsidiary of AngelList.

Invesdor also refers to lead investors in its process descriptions by saying that after the pitch of a campaigner is approved Invesdor sends the pitch to its lead investors who will then have a week or so to decide whether they will invest in the target company in question. After these decisions the pitch will become public. There is no explanation whether the lead investors are only used as marketing tools, setting an example and attracting the public to invest in the same campaigner, or if and how the leads also syndicate their investments.

3 THE PLATFORM

3.1 PROVISION OF INVESTMENT SERVICES

3.1.1 General

A platform must apply for an activity licence and is subject to supervision of the FSA in the event the platform is considered to provide any of the following investment services:

- reception and transmission of orders related to securities;
- execution of orders on behalf of clients;
- securities dealing on own account;
- securities portfolio management;
- provision of investment advice;
- guarantee of securities or guarantee of the offer, issue or sale of securities;
- organising an offer or issue of securities;
- operation of a multilateral trading facility (MTF) where the interests of different people for acquisition and transfer of securities are brought together under uniform conditions that results in a contract;
- as from January 2017, operation of organised trading facility (OTF), which is a multilateral system not being a regulated market or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract.

The abovementioned requirements arise from the EU law. However, there is no common understanding on whether a typical equity crowdfunding platform is considered to provide investment services. For example, the interpretation currently prevailing is that the crowdfunding platforms do not perform investment services as defined in MiFID (Markets in Financial Instruments Directive), but act as the "media", and are thus free from being licensed and supervised by the local authorities.

The European Commission sees a great potential in crowdfunding and has covered several aspects of crowdfunding in its 27 March 2014 communication,[1] it has not provided any insights on MiFID's application to crowdfunding, although the appropriate guidance has been waited for years. For example, the authors of paper published in association with the European Crowdfunding Network in 2012, asked "/…/ the European Commission to clearly define activities that are mentioned in the annex of the Markets in Financial Instruments Directive (MiFID) directive, to avoid any different interpretations and legal uncertainty as to whether a specific crowdfunding platform setup falls within the scope of such an activity or not."[2]

Lack of mutual understanding is also apparent in Review of Crowdfunding Regulation published by the European Crowdfunding Network in October 2013[3] providing analysis of crowdfunding regulations in EU member states and in other countries – the analysis which would have been unnecessary to a large extent if there had been a common

[1] See http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:172:FIN
[2] See http://www.crowdfundingframework.eu/images/European_Crowdfunding_Framework_Oct_2012.zip
[3] See http://www.europecrowdfunding.org/wp-content/blogs.dir/12/files/2013/12/ECN-Review-of-Crowdfunding-Regulation-2013.pdf

understanding on the underlying regulation (the MiFID). At the same time the review does not provide any clear position as to the application of MiFID to crowdfunding; often simply stating that platform activities may constitute investment services.

While the European Commission refers in its communication that the platforms might be subject to MiFID rules depending on platform's specific business model, it does not specify which activities might constitute investment services under MiFID. Nevertheless, the general position of the European Commission seems to be that the platforms should not be under the supervision of local financial authorities and that crowdfunding should be self-regulated by industry or local authorities by appropriate legislation or guidelines. Note, however, that the European Commission is exploring further the potential and the risks of this relatively new and growing form of finance, as well as the national legal frameworks applicable to it, in order to identify whether there is value added in European level policy action in this field.[4]

The overall situation has been captured well by the Ministry of Finance of Finland in its Report of Crowdfunding Survey published on 13 March 2014,[5] where one of the conclusions provide ironical but practical solution: "One option is voluntary registration of service providers with the Financial Supervisory Authority to determine whether the activities of a certain service provider are covered by the regulation and supervision of the sector." In addition, the survey concludes that the crowdfunding sector must develop self-regulation and good practises while potential state regulation on crowdfunding should be kept as light as possible. At the same time, they also propose to consider requiring authorisation or registration from operators in the sector.

It was accepted consensus in Finland that crowdfunding platforms are not considered providing investment services as defined in the MiFID at the time the Ministry of Finance of Finland published its report. This position has been recently revised by the Finnish Financial Supervisory Agency (FIN-FSA) that published its new guidelines on equity crowdfunding in late June 2014. Under the new guidelines equity crowdfunding platforms are engaged in the "reception and transmission of orders in relation to one or more financial instruments". Depending on the scope of their services, they may also provide other regulated services, such as investment advice and duties typically undertaken by arranger banks. The implementation of these guidelines is not yet clear, especially the effect on foreign platforms.

In the event the platform is considered providing investment services, the platform must follow strict rules on the management, organisational structure and control. In addition the platform must have internal policies (e.g. policies for management of risk and conflict of interest) and internal audit in place. Moreover, the platform must follow numerous obligations when conducting its business activities. These include various information and assessment undertakings, restrictions when entering into transactions etc.

The following sections provide a closer insight as to the investment services the platforms might be considered to provide.

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[4] See http://ec.europa.eu/internal_market/finances/docs/crowdfunding/140416-callforapplication_en.pdf

[5] See http://www.financeministry.fi/vm/en/04_publications_and_documents/01_publications/07_financial_market/20140313Report/name.jsp

3.1.2 Reception and transmission of orders related to securities

European Securities and Markets Authority (ESMA) has opined that though business models can vary, "/…/ the activity most likely to be carried out by mainstream crowdfunding platforms in the absence of regulatory constraints is the reception and transmission of orders."[6] ESMA stated that whilst the notion of "order" is not defined in MiFID, it is to be interpreted widely. This means that there needs to be a real, substantive distinction between the expression of interest and something which could be considered as an order. In our view "reception and transmission of orders related to securities" should not be attributed to platforms merely offering internet infrastructure for promoting equity investments (as opposed to participants in traditional multilateral trading facilities). Typical platforms such as Invesdor and FundedByMe provide web forms for investors for making commitments and send automated emails confirming investments. The platform could be accordingly viewed as receiving orders for acquisition of securities and transmitting the same to the target company (campaigner).

3.1.3 Execution of orders on behalf of clients

The platform could provide this investment service if it intends to act as intermediary between the investors and the campaigners. This is especially the case where the platform collects the investment amounts and transfers those after the minimum funding asked by the campaigner has been committed. While this service provides additional comfort and security to investors, it is probably the licencing reasons why both Invesdor and FundedByMe have not taken such intermediary role compared to Seedrs that executes orders in its name but on behalf of the investors. Seedrs also has the respective authorisation from the UK authorities.

3.1.4 Securities portfolio management

Portfolio management means managing securities portfolios in accordance with mandates given by clients on a discretionary client-by-client basis. As such, portfolio management includes the ability of the manager to decide and carry out an investment strategy, e.g. by deciding the object, type and time of a financial transaction. Accordingly the platforms could not be treated as portfolio managers as the investment responsibility in investment judgement does not shift to the platform but stays with the investor relying on its own judgement, knowledge and skill.

In effect the platforms could hold and provide nominee services, without licensing and supervision of the FSA, enabling the investors to avoid the hassle of being a legal shareholder while the campaigner would benefit from a single party as shareholder instead of incurring the administrative burden of having a large number of shareholders. Such services are provided for example by Seedrs, however, under the permission granted to it by the local financial supervisory authority in the UK.

3.1.5 Provision of investment advice

Investment advice means the provision of personal recommendations to a client, either upon its request or at the initiative of the investment firm, in respect of transactions relating to securities. A personal recommendation is the one which is presented as

[6] See: http://www.esma.europa.eu/system/files/2014-1378_opinion_on_investment-based_crowdfunding.pdf

suitable for the person or which is based on a consideration of the recipient's personal circumstance. As such, a personal recommendation relates only to a particular financial transaction and excludes general recommendations and marketing activities like promoting investments into start-ups.

General practice of the platforms is not to provide any recommendations as to the campaigners. Platforms such as FundedByMe and Seedrs clearly state that they do not provide any advice and that the investors are solely liable for their investment activities.

3.1.6 **Organising an offer or issue of securities (placing)**

Placing of securities is not defined in the MiFID, however, in our view, placing is the service of finding investors for securities on behalf of a seller. The same position has been indicated by the European Commission[7] and the Bank of England.[8]

The European Commission[9] considers the core activities of placing not related to technical means or marketing activities but organising the process in its integrity and ensuring proper pricing of the securities, provision of necessary information and allocating the securities taking into account different actors involved.

Hence, mere provision of technical means to seek investors should not constitute organising a placement of securities on behalf of the campaigner. Accordingly, typical crowdfunding platforms should not be regarded as organisers of placements. Likewise, in our opinion the general marketing activities of a platform should not result in qualifying the platform as organiser of a placement. For example, Invesdor issues press releases, publishes newsletters, involves their partners and investor network, and uses other means to promote their platform and campaigners. Such measures are, however, merely supportive activities and far from services usually offered by licensed corporate finance businesses.

3.1.7 **Operation of a multilateral or organised trading facility**

According to the MiFID an MTF is a multilateral system, which brings together multiple third-party buying and selling interests in financial instruments – in accordance with non-discretionary rules – in a way that results in a contract. The term "multilateral" indicates that the trading venue facilitates simultaneous access by many market participants, allowing them to compete for transactions.[10] The same applies to OTF as it is considered a multilateral system as well. Moreover, OTFs are intended for non-equity instruments and as such crowdfunding platforms should not constitute OTFs as in Estonian context the platforms would typically provide medium for shares or share units.

A crowdfunding platform should not be regarded as an MTF as its purpose is not to match sale and purchase orders resulting in sales agreements, but rather to provide a medium and technical means for negotiation and execution of issue of securities. Furthermore, the investors do not compete to enter into transactions and platforms do not offer immediate execution of the transactions, which might in fact take also place outside the

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[7] See http://ec.europa.eu/yqol/index.cfm?fuseaction=question.show&questionId=152

[8] See Q22 at http://fshandbook.info/FS/html/handbook/PERG/13/3

[9] See p 72 at http://ec.europa.eu/internal_market/consultations/docs/2010/mifid/consultation_paper_en.pdf

[10] For further information please see: L. D. Setten. The Law of Institutional Investment Management. New York: Oxford University Press, 2009, p 250 ff.

platform (without the involvement of the platform). Hence, crowdfunding platforms only provide a gateway for campaigners and investors to form bilateral relations.

3.1.8 **Conclusion**

While in our view most of the platforms fall outside the scope of the MiFID, there is no common understanding or meaningful guidance for interpreting the list of investment services provided by the MiFID. As such, typical platforms such as Invesdor and FundedByMe include functionalities that might be considered providing investment services by authorities. ESMA has opined that the activity most likely to be carried out by mainstream crowdfunding platforms is the reception and transmission of orders, but also admits that it largely depends on the business model and many platforms build their business models as to avoid MiFID regulations. Such legal uncertainty clearly hinders the take-off and development of crowdfunding in Estonia.

Accordingly, in order to promote development of crowdfunding in Estonia, the FSA should provide its interpretation of investment services in light of crowdfunding activities. Until there is no firm understanding on the EU level that an equity crowdfunding platform is considered to provide investment services, in our opinion it is not wise for the FSA to take the toughest position possible as too burdensome and premature regulatory action will clearly hinder the take-off of the currently non-existing equity crowdfunding industry in Estonia. Instead, investor protection should be adressed through guidelines and advice on the information and disclosure obligations to ensure that the small crowdfunding investors really understand the risks they are taking.

3.2 PROVISION OF PAYMENT SERVICES

In addition to potential licensing obligation for providing investment services, the platform may be subject to supervision and licensing of the FSA due to provision of payment services.

Estonian FSA has not provided any guidance on the matter. A platform is likely to provide payment services if collecting, holding or transferring the payments. In such case the platform must follow strict rules on the management, organisational structure and control, have internal policies and internal audit in place, and follow numerous obligations when conducting business activities.

However, the platform could be released from licencing and some other obligations if the platform only transfers the payments. The FSA would authorise the exemption only and until the average total amount of transfer transactions within the preceding 12 months does not exceed EUR 1 million a month. Also, no license for payment services is needed if the platform only transfers payments and already has a license for providing investment services.

To avoid licencing and supervision of the FSA, a platform could alternatively use third party payment services such as PayPal to provide necessary comfort and expected services to investors and campaigners.

Existing platforms in other countries vary in terms of their payment related functionalities. Regulatory considerations may have served as one of the reasons for each platform choosing a particular set-up. For example: FundedByMe has distanced itself from all payment related activities and the campaigner is expected to collect payments directly from the investors; Invesdor co-operates with FIN-FSA supervised Suomen Maksuturva Oy in order to handle payments; Seedrs collects payments from

investors to a dedicated client account (under the permission granted to it by the local financial supervisory authority in the UK).

3.3 OTHER LICENCES AND REGISTRATIONS

In addition to licences referred to in sections 3.1 and 3.2**Error! Reference source not found.**, a platform would potentially require to be registered in the VAT Registry, the Registry of Processing of Sensitive Personal Data and the Employment Registry.

A platform is required to comply with the rules and procedures prescribed in the money laundering rules in the event the platform is subject to FSA supervision or accepts cash payments in excess of EUR 15,000. These rules include notification responsibility as well as certain obligations regarding the establishment and implementation of due diligence measures, such as the obligation to identify the client in presence (may be conducted through third parties) if service is used by the client for the first time.

4 CONCLUSIONS

4.1 LEGAL FORM

Although there are several legal forms available, campaigners should be formed as private or public limited companies in order to seek financing through crowdfunding. A private limited company would be recommended to a campaigner due to more liberal capital and other legal requirements compared to a public limited company. This is one of the reasons practically all start-ups are formed as private limited companies.

However, the mandatory minimum nominal value of a share unit may limit raising capital through crowdfunding while public limited companies offer flexibility in terms of shares often necessary to regulate shareholders' relations as desired. Consequently, a public limited company may often be more suitable for a campaigner.

While both forms are suitable for campaigners, the following differences should be considered in choosing suitable legal form (the table does not reflect differences that will no longer be effective as of 1 July 2015):

Issue	Private limited company	Public limited company
Minimum share capital	EUR 2,500	EUR 25,000
Minimum nominal value of a share unit or share	EUR 1	EUR 0.1
Share transfer restrictions	Different restrictions can be established in the articles	Only pre-emption can be established in the articles
Share registry	Management board or Estonian Central Register of Securities	Estonian Central Register of Securities
Share transfers	Notarised agreements or executing transfers through bank or nominee	Executing transfers through bank or nominee
Supervisory board	Optional	Mandatory (at least 3 members)
Audit	Mandatory if thresholds exceeded	Mandatory
Delivery of shareholders' meeting notices	By post or by e-mail to address indicated in the list of shareholders	By registered mail if less than 50 shareholders or by publishing a notice in a daily national newspaper if more than 50 shareholders

4.2 FINANCING INSTRUMENTS

4.2.1 Share units and shares

The procedure for increasing share capital is similar for private and public limited companies. However, the following differences between share units and shares should be taken into account in determining the suitable financing instrument in a particular case (the summary does not reflect differences that will no longer be effective as of 1 July 2015).

Unlike the internationally well-known concept of shares, the concept of share units is relatively unfamiliar for many foreigners and may need to be explained in case a campaigner looks for international funding as private limited company.

The minimum nominal value of a share can be EUR 0.1 instead of EUR 1 requirement applied to share units. Therefore, it is possible to involve 10 times more investors for the same shareholding of a public limited company in contrast to a private limited company.

While issue of share units can be arranged without involving a notary, share unit transfer agreements must be notarised. The notarisation obligation will not apply if the share units are registered with the ECRS, which is mandatory for public limited companies. In such case the sale can be carried out by submitting a transfer order without signing any agreement. From crowdfunding perspective both notarising the transfer agreements and having the share units and shares registered with the ECRS will limit seeking investments from international investors. If share units are not registered, foreigners can easily acquire them but may face problems upon sale. Transferring share units is easier if the share units are registered but foreigners cannot acquire and hold them without opening necessary accounts or concluding required nominee agreements.

4.2.2 **Quasi-equity solutions**

A campaigner may also use quasi-equity solutions instead of share units and shares for raising capital through crowdfunding. However, the public is probably not familiar with quasi-equity solutions and may therefore be distrustful in respect of those instruments, especially if offered by recently formed start-ups. Also, in view of lack of relevant rules and guidance, it should be subject to specific tax analysis how the profit related payments should be qualified and treated for tax purposes.

It should be noted that quasi-equity instruments that can be converted into shares or share units cannot be effectively enforced and investors can only claim compensation for damages if the share units or shares are not issued.

Nonetheless, quasi-equity solutions provide the campaigners with a good alternative compared to the share units and shares that are especially difficult to be owned and/or transferred by foreigners under the legislation currently in force.

As an alternative for traditional quasi-equity solutions, a platform could consider holding issued share units or shares on behalf of and for the benefit of investors.

4.3 PUBLIC OFFERING

The campaigners must generally follow the rules applicable to public offerings and draft a prospectus if they seek funding for EUR 100,000 or more. This makes it very burdensome to raise capital over the referred limit and in today's market it seems rather unreasonable. As under the EU law a prospectus has to be prepared for rounds of EUR 5 million or more, it should assessed whether the increase of the threshold would be possible without harming consumer confidence and trust in crowdfunding in Estonia. Clearly, a higher threshold would make it easier for local as well as foreign campaigners to seek funding and market their campaigns fully or partially in Estonia.

4.4 LEAD INVESTOR

While questionable, there is a high risk that a lead investor would be considered providing investment services (such as investment advice or organising a placement) subject to licensing and supervision of the FSA, or acting as an offeror subject to public offering rules while providing investment opportunities. It is essential that the FSA clarify their understanding about the lead investor activities. Until such guidelines are missing, it

is advised that a platform confirms envisioned syndication functionalities with the FSA in order to avoid possible sanctions on lead investors using the platform.

Kindly note that in the event the lead investor collects investments from its backers and invests those on their behalf, the lead investor may be required to meet the regulation set forth for investment funds and their management companies, including obtaining an activity licence from the FSA and complying with the relevant extensive requirements and procedures. This is especially the case when the money is collected through the issue of securities in the lead investor vehicle.

4.5 THE PLATFORM

While questionable, there is a high risk that the platform would be considered providing investment services such as reception and transmission of orders related to securities, organising an offer or issue of securities or operating a multilateral trading facility. In such case the platform would have to apply for an activity licence and be subject to supervision of the FSA. It is essential that the FSA clarifies whether a platform would be considered to provide investment services subject to licencing and supervision of the FSA. Until the lack of such guidelines, each platform is advised to confirm its business model with the FSA in order to avoid possible sanctions.

In the event a platform will mediate payments between campaigners and investors (money remittance), the platform must apply for an activity licence and is subject to supervision of the FSA.

4.6 LEGISLATIVE PROPOSALS

In order to facilitate financing through crowdfunding, above all the following amendments in the Estonian legislation should be considered:

Commercial Code

- decrease of the minimum nominal value requirement of a share unit is advisable. Another (more radical) solution would be to abandon the nominal value requirement entirely (requires abandoning share unit concept as a whole – see the following paragraph). In practice nominal value of a share unit has little relevance and abandoning minimum nominal value requirement would offer more flexibility in relation to funding. The same applies to public limited companies;

- to consider whether there is a need to maintain two different solutions to represent shareholders' participation in similar legal forms while the shares could be also used by private limited companies. From start-up industry standpoint it is strange that private limited companies having more liberal regulation compared to public limited companies need to comply with stringent and inflexible rules concerning the share units;

- allow share units which are not registered with the ECRS to be transferrable not under notarised agreements but under written agreements or in a format which can be reproduced in writing. This would make acquisition and transfer of share units simpler for foreigners as well as local investors. In such case it would make sense for the company to avoid registering the share units with the Estonian Central Register of Securities that requires foreigners to undertake complicated procedure for opening cash and securities account in Estonia or use nominee services;

Securities Markets Act

- increase of EUR 100,000 threshold triggering a campaigner's obligation to prepare a prospectus.

4.7 SUITABLE MODEL FOR CROWDFUNDING

The best way to raise capital through crowdfunding under the current legal regime would be as follows:

- the campaigner should be established as or organized into a private or public limited company before the campaign;
- in order to avoid preparing a prospectus, the investments sought after should be in total less than EUR 100,000;
- before the campaign the campaigner adopts a capital increase resolution for issuing shares in return for capital or the respective resolution should be adopted after the receipt of investments;
- during the campaign the investors subscribe for the shares. The investors should have a cash and securities account opened in Estonia or a nominee arrangement in place for holding the shares. Alternatively, no accounts or nominee arrangement is necessary if the campaigner will issue share units not registered with the ECRS. In such case the share units could later be sold only under notarised agreements;
- the investors will transfer the investments directly to the campaigner. The platform does not mediate the payments but is merely a meeting platform for campaigners and investors. If the platform intends to collect, hold or transfer the amounts, respective license has to be acquired from the FSA;
- after the end of a successful campaign the campaigner notifies the Commercial Register and the ECRS after which the shares will be considered issued.

Quasi-equity solutions serve as viable alternatives to the model described above.

It is essential that the FSA clarifies whether the platform will be considered to provide investment services that are under the licensing and supervision of the FSA. Until the lack of such guidelines, each platform is advised to confirm its business model with the FSA in order to avoid possible sanctions.

BACKGROUND OF MEMORANDUM

We have prepared this memorandum on the basis of the applicable laws of the Republic of Estonia (including the legislation of the European Union, where applicable) valid as of the date hereof. No opinion is expressed or implied as to the laws of any other jurisdiction. We assume no obligation to update or supplement this memorandum to reflect any facts or circumstances that may hereafter come to our attention or any changes in law which may occur after the date hereof.

This memorandum is strictly limited to the matters set out herein and is not to be extended to any other matter, no opinion is expressed on matters of fact. The information set forth herein is being provided as a general overview of the relevant issues and should not be construed as legal advice in regard to any particular situation or concern.

This memorandum has been prepared at the request of and pursuant to the scope of work agreed with Eesti Arengufond.

FURTHER INFORMATION

This memorandum has been prepared by Attorneys at law Borenius. For further information, please turn to:

Kristel Raidla-Talur
Partner
+372 665 1888
kristel.raidla-talur@borenius.ee

Kristel Raidla-Talur advises clients mainly on mergers, acquisitions, and financing transactions. She has advised on a wide range of significant international transactions offering expertise in acquisition and disposal of businesses as well as venture capital and other financing transactions. Kristel also advises on competition law related matters.

Ott Aava
Senior Associate
+372 665 1888
ott.aava@borenius.ee

Ott Aava advises clients mainly on mergers, acquisitions, restructurings, and other general corporate law related questions. Ott has been involved in several M&A projects, advising clients on share and asset deals, strategic and financial investments. Ott has also advised several start-ups on shareholders' relations, motivation packages and other matters.