Prospects for Future EU Legislation on Crowdfunding and Initial Coin Offerings

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Abstract

With its recent proposal regarding a new regulation on European Crowdfunding Service Providers (ECSP) for Business, the European legislator made a first important step toward the implementation of a new regulatory framework for Crowdfunding in Europe. This article aims to provide an overview and to discuss certain major European aspirations to reform the European legal framework on Crowdfunding and its potential application to Initial Coin Offerings (ICOs).

Introduction

With the rise of the Internet and new Internet-based technologies, alternative forms of business financing gained rapid popularity among small and medium-sized enterprises (SMEs) and start-ups especially. In recent years, practice has introduced many different models to meet the increasing demand for alternative business financing sources. Crowdfunding and ICOs have been two of the most successful concepts. Recent cases of fraud and other irregularities in the Crowdfunding and ICO market, however, have proven that new Internet-based technologies do not only provide for vast opportunities, but also involve a wide range of risks and dangers for the investors and other involved stakeholders. Especially virtual currencies and ICOs have generated extensive and mostly negative media coverage. Hence, it is not surprising that the European legislator as well as the national legislators in the EU member states are constantly debating and assessing the potential implementation of tailored legislation and/or the amendment of existing European or national statutes applicable on these concepts.

Market Developments in Europe

General Remarks

To comprehensively assess the importance of Crowdfunding and ICOs within the European alternative business financing market and identify the main challenges for the European legal framework, the following section shall provide a brief overview of the latest developments and certain significant legislative aspirations in Europe.

Crowdfunding

Business financing through Crowdfunding has developed to a well-established alternative to classic financing concepts in Europe. The European legislator duly noticed the increasing importance of Crowdfunding for the economic growth in Europe and intensively explored the potential implementation of specific EU-level statutes. In 2017, the European Commission initiated a major advance and conducted an impact-assessment on a legislative proposal for an European legal framework on crowd- and peer-to-peer financing (Impact Assessment). The Impact Assessment introduced different options to reform the current legal environment for Crowdfunding in Europe and invited interested stakeholders to actively engage in future consolidation efforts. In March 2018, the European Commission followed-up on its ongoing deliberations and proposed a regulation on European Crowdfunding Service Providers (ECSP) for Business (Commission Proposal) as part of its objective to deepen the Capital Markets Union. The Commission Proposal addresses the business conduct of investment- and lending-based crowdfunding platforms and seeks to provide an encompassing regulatory framework, especially, in relation to potential cross-border activities. Besides these EU-level aspirations, several EU member states (such as Italy, the UK, Belgium, France, and Austria) already implemented their own national
legislations covering various regulatory and/or civil-law aspects of Crowdfunding.\textsuperscript{6}

**Initial Coin Offerings**

ICO\s, on the other hand, can be considered as a rather recent but also very successful development. In 2017, Europe even evolved to the leading market place for ICOs in the world.\textsuperscript{7} The European legislator, however, seems to remain rather reserved toward virtual currencies in general and their usage for ICOs in particular. In 2016, the European Commission adopted proposals for the amendment of the 4th Anti-Money Laundering Directive (AML Directive) to include virtual currency exchanges and online wallet providers in the EU’s anti-money laundering framework.\textsuperscript{8} The European Securities and Market Authority (ESMA) issued an investor warning regarding the high risks of ICOs as well as a reminder for involved stakeholders regarding the potential application of existing EU-level statutes.\textsuperscript{9} The recent collapse of Optioment in Austria is a good example to illustrate the imminent dangers of cryptocurrency investments for consumers. Optioment operated as a Bitcoin investment scheme involving a multilevel marketing structure with (promised) returns between 1.5 and 4 percent for its investors.\textsuperscript{10} The operators of the website allegedly stole around 12,000 Bitcoins from investors in Austria, Germany, Poland, Romania, and other Eastern European countries.\textsuperscript{11} The Optioment collapse coincided with national discussions in Austria to expand its national anti-money laundering framework and trading rules on gold and derivatives to virtual currencies.\textsuperscript{12} In 2017, the French Financial Markets Authority (AMF) conducted a public consolidation regarding the potential implementation of a national statute on ICOs.\textsuperscript{13} The outcome of this consolidation covered various proposals on civil-law aspects (such as the utilization of escrow accounts) as well as regulatory aspects (such as the licensing and supervision of involved stakeholders or a prospectus requirement).\textsuperscript{14} As a first step toward (specific) national rules on ICOs, the French legislator recently allowed trading of unlisted securities on Blockchain-based trading platforms.\textsuperscript{15} Despite these developments and the apparent urge of the EU member states to adapt and/or expand their national legislations, neither the European legislator, nor the national legislators in the EU member states have yet implemented a specific and encompassing legal framework on ICOs.

**The Commission Proposal on Crowdfunding**

**General Remarks**

In its Impact Assessment, the European Commission explicitly addressed the regulatory environment for Crowdfunding platforms in Europe and introduced several (alternative) legislative proposals, reaching from the maintaining of the status-quo of European and national legislations to an encompassing stand-alone legal framework.\textsuperscript{16} The Impact Assessment served as basis for the Commission Proposal, which has been introduced by the European Commission in March 2018 and is now discussed by the European Parliament and Council (see below). In relation to ICOs, the European Commission did not consider whether its proposals could serve as a basis for future European legislations on this concept. As ICOs could generally be qualified as a further developed version of Crowdfunding,\textsuperscript{17} it can nevertheless be argued to draw the line from Crowdfunding to ICOs and vice versa.

**National Legislations (status quo)**

The first proposal by the European Commission suggests leaving the European regulatory framework in its current state.\textsuperscript{18} This proposal would involve ongoing deliberations with the national authorities in the EU member states and a continuous observation of market developments.\textsuperscript{19} The main reasoning for this approach has been identified in the potentially large variety of standards in the different EU member states, which would make the transformation of the industry rather difficult and costly.\textsuperscript{20} The proposal could further be reasoned by the advanced efforts of many EU member states, who have introduced targeted national laws on Crowdfunding.\textsuperscript{21} Austria, for instance, implemented its federal act on alternative investment forms (\textit{Alternativfinanzierungsgesetz}, AltFG) to cover most legal aspects of Crowdfunding and the role of Internet-based Crowdfunding platforms.\textsuperscript{22} The AltFG shall serve as an example for the endeavours of the EU member states to develop national laws embedded in the existing European legal environment. The AltFG is generally limited to the issuance of specific instruments, such as shares, bonds, equity in limited companies and cooperatives, profit participation rights, silent partnership shares, and subordinated loans.\textsuperscript{23} The key aspect of the AltFG, however, concerns the disclosure and information obligations of the capital-seeking company toward
the crowd investors. In this connection, the AltFG takes advantage of the general exemption to the Prospectus Directive and implements certain scaled information and disclosure requirements depending on the value of the issued instruments and the raised capital. Following the general concept of the legislative precedence of EU statutes, the obligations under the (national implementation of the) Prospectus Directive apply in full scope if the emission value of the capital seeking company within the EU territory exceeds the threshold of EUR 5 million over a period of 12 months.

Concerning the potential consequences of this proposal on ICOs, the EU member states have currently not addressed this issue within their national laws. It can, however, be observed that the EU member states are intensely pursuing plans to introduce national laws covering the regulation of virtual currencies, ICOs, and involved stakeholders. The recent Optioment fraud case in Austria, for instance, triggered major discussions regarding the national regulation of virtual currencies and ICOs. These discussions coincided with the proposal of the Austrian finance minister to include virtual currencies, such as Bitcoins, into the national Austrian anti-money-laundering regime. In detail, it has been suggested to introduce the obligation to report certain cryptocurrency-transactions to the Austrian federal criminal police department (Bundeskriminalamt) as well as identification requirements for virtual currency owners. In addition, it has also been proposed to subject virtual currency exchange platforms under the supervision of the Austrian financial markets authority (FMA). In March 2018, the Austrian finance minister intensified these discussions and announced the convection of a so-called “Fintech Advisory Board”, which should commence its deliberations in April 2018. First items on the agenda of this new panel shall concern the regulatory framework for ICOs in Austria, including the potential implementation of a prospectus requirement or the disclosure of large virtual currency transactions. In France, the French Financial Markets Authority (AMF) launched its public consultation regarding the potential regulation of cryptocurrencies and ICOs. In February 2018, the AMF published a summary document outlining the received responses to the public consultation procedure. In this connection, a great variety of potential legal measures has been proposed. Examples include certain minimum information to be provided to the investors prior to and after the investment, a white paper approval by an authority, professional association or other reference institution, the standardisation of white paper requirements, or the conduct of projects through certain escrow mechanisms. The AMF introduced several suggestions, including the promotion of certain soft-law measures, such as good-practice guides and recommendations, the expansion of existing legislation or a comprehensive new legal framework for ICOs (as compulsory or optional regime). Until today, these suggestions have, however, not been realized.

European Soft-Law Policies

The second option suggested by the European Commission involves the implementation of certain soft-law policies addressed to Crowdfunding platforms, such as recommendations, nonbinding minimum standards, or best industry practices. At first sight, this proposal seems to qualify as a suitable solution. Applying this concept, it can be argued that the clarification of existing civil-law and consumer protection safeguards has the potential to significantly benefit the involved stakeholders. Capital-seeking companies and Crowdfunding platforms would be able to rely on the legitimacy of their project and navigate through applicable legal requirements when following these recommendations. The introduction of such clarifications could also avoid parallel structures, which are particularly evident in case of consumer/investor protection and information requirements.

Provided that soft-law measures are introduced in addition to the existing European legal framework, they could, however, also have significant negative impacts. In fact, they could likely increase concerns in relation to a legal uncertainty or the lack of transparency for investors. Given the rather dense network of potentially applicable European and national regimes, the implementation of soft-law measures would add an additional layer of policies to be considered during a Crowdfunding project. Further, it must also be emphasized that the concept of soft-law policies disposes of certain imminent downsides, which speak against their implementation. Andersson (2012), for instance, identified three major drawbacks of the current European corporate governance regime. First, corporate governance codes could potentially have negative effects on future legislative endeavours. Since corporate governance codes are typically prepared under the involvement of addressed stakeholders, it would potentially be more difficult to subsequently
enact mandatory legislation to replace ineffective soft-law measures. Second, the common comply-or-explain principle of corporate governance showed significant flaws regarding the actual compliance and quality of potential “explanations” for deviations from best practice rules. Third, it has been observed that many jurisdictions did not provide for sufficient consequences or sanctions in the case of compliance failures. In their article on the Commission Action Plan on European Company Law and Corporate Governance 2012, Böckli et al. (2013) proposed a variety of measures to improve the effectiveness of the European corporate governance framework. These proposals include (1) incentives for the compliance with corporate governance rules, (2) effective sanctions in the case of noncompliance, or (3) the involvement of private and public actors in accompanying inspection and monitoring activities.

Considering ICOs, the soft-law proposal of the Impact Assessment could trigger thought-provoking impulses for future reformatory efforts in Europe. Safe the peculiar tasks of ICO platforms and virtual currency exchanges (such as the provision of online wallet services to investors), the general idea of European soft-law measures and best practices could similarly be applied to the business conduct of ICO platforms and virtual currency exchanges. Hacker (2017), for instance, comprehensively analysed the cryptocurrency environment on its suitability for the implementation of soft-law measures and organisational rules on cryptocurrency transactions. In detail, he suggested the introduction of a so-called Blockchain Governance Code by means of organisational rules for involved stakeholders (such as the instalment of different organs and structures), fiduciary rules, or transparency and reporting requirements. According to Hacker (2017), the initial implementation of the comply-or-explain model should be followed by mandatory legal requirements when stakeholders assume a certain weight in the financial system.

**Mandatory European Legislation**

The final option provided by the European Commission involves the implementation of an encompassing (new) European legal framework on Crowdfunding. In this connection, the European Commission proposed to either implement the concept of Crowdfunding into existing EU-level statutes or to provide for a stand-alone EU-level statute that is specifically targeting the practical operation of Crowdfunding platforms. In addition, the Commission considered the option of a stand-alone framework to which Crowdfunding platforms can voluntarily opt-in to allow an efficient and effective cross-border activity, whereas Crowdfunding platforms operating on a mere national level would then remain under the scope of the potentially applicable EU statutes and their national regimes.

In March 2018, the European Commission decided to further pursue its proposal regarding the implementation of an encompassing opt-in framework regulating the business conduct of certain Crowdfunding platforms active on a cross-border scale in Europe and introduced its Commission Proposal. Consequently, the European Commission discarded the other proposals included in the Impact Assessment: (1) The status-quo of the current legal framework on Crowdfunding in Europe has been qualified to not solve the contemporary issues identified by the European Commission. (2) The proposed soft-law policies would have been implemented in addition to existing (European and national) statutes providing for an even denser network of policies to be considered. (3) The expansion of existing (European) statutes applicable on Crowdfunding would have neglected the raised concerns in relation to the legal certainty and transparency of the European legal framework and would have not been as cost effective as other solutions.

The final option of the Impact Assessment specifically targeted the European dimension of Crowdfunding and (potentially) ICOs and addresses the main argument of the European Commission, whereas Crowdfunding platforms and capital-seeking companies regularly face significant difficulties to scale their cross-border activity under diverging national regimes. This situation is further enhanced by the fact that the national legislations in the EU can only fill gaps left by applicable EU-level statutes (such as in place of the various exceptions from the Prospectus Directive). As a result, it is evident that the EU member states provide for different levels of protection for crowd investors and, therefore, different levels of organisational and financial burdens for involved stakeholders. Further, it is apparent that the current legal framework of diverging national regimes imposes a substantial risk of Crowdfunding stakeholders choosing the jurisdiction by the severity of the respective regulatory environment (in the sense of forum
shopping practices), which could be mitigated by the implementation of a uniform legal framework in all EU member states. Another important argument can be seen in the transparency of applicable laws and the general demand for legal certainty. The fact that the existing legal framework in Europe is mainly dependent on the parameters of the individual project, makes it difficult for the involved stakeholders to comprehensively assess their rights and obligations.

In a nutshell, the Commission Proposal seeks to implement a (directly applicable) regulation for uniform European rules in relation to (i) the operation and organization of Crowdfunding service providers, (ii) the authorization and supervision of Crowdfunding providers, as well as (iii) certain rules on transparency and marketing communications for the provision of Crowdfunding services in the EU. The application of the Commission Proposal is further limited to Crowdfunding offers exceeding the amount of EUR 1 Mio over a period of 12 months. The Commission Proposal has been limited to legal persons, which are established in one of the EU member states and are acting as Crowdfunding platforms in the field of lending-based Crowdfunding models, where the investor is granting the capital-seeking company a loan against interest rates, and investment-based Crowdfunding models, where the capital-seeking company is issuing transferrable securities to its investors. The exclusion of other common types of Crowdfunding, such as reward-based, pre-sales models or peer-to-peer lending, has been argued with the main concern of “over-regulation” and the existing civil-law framework on investor protection in the EU. Examples of potentially relevant EU statutes could include Directive 2000/31/EG (E-Commerce Directive), Directive 2011/83/EU (Consumer Rights Directive), or Directive 2006/114/EC (Misleading or Comparative Advertising Directive). Further, it must be emphasized that the Commission Proposal seeks to introduce a subsidiary set of rules only. The Commission Proposal shall only be applicable if a Crowdfunding platform in the EU chooses to seek an authorization under the proposed framework. Consequently, the Commission Proposal shall not cover private project owners (i.e., capital-seeking individuals), Crowdfunding platforms already authorized as investment firms under the framework of Directive 2014/65/EU (Directive on markets in financial instruments, MiFID II) as well as Crowdfunding platforms operating under the national regime of their EU member state. The voluntary character of the Commission Proposal has been argued with the objective to increase the cross-border activity of Crowdfunding platforms in the EU. If a Crowdfunding platform is offering its services to capital-seeking companies and investors from different EU member states, it shall be ensured that the services are provided in line with the same principles and the same level of protection throughout all EU member states.

Regarding the connection of the Commission Proposal with existing European statutes, it can be argued that the Commission Proposal would still introduce an additional layer of regulatory requirements for Crowdfunding platforms rather than replacing potentially applicable EU statutes. This conclusion can be drawn from different aspects of the Commission Proposal. On the one hand, it has been shown that the scope of the Commission Proposal would generally exclude Crowdfunding platforms, which have already been licensed under the framework provided by the MiFID II. In this connection, the Commission Proposal notes that any Crowdfunding platform intending to provide services beyond the subject matter of the Commission Proposal would need to comply with the MiFID II framework and should withdraw from the authorization under the Commission Proposal. The same applies for an authorization under the national regimes of the EU member state, whereby the authorization under the Commission Proposal shall also cover mere domestic activities of the concerned Crowdfunding platform. Another important example in this connection concerns the provision of payment services by the Crowdfunding platform. In this connection, it has been clarified that the compliance with the Commission Proposal should generally not entitle the respective Crowdfunding platform to perform payment services for the capital-seeking company and/or the investors. Instead, the Commission Proposal would require any Crowdfunding platform or any assigned service provider to seek authorization under the national regimes in the EU member states implementing Directive 2014/65/EU (Payment Service Directive) and comply with the rules of Directive (EU) 2015/849 (Anti Money Laundering Directive).

The cornerstone of the Commission Proposal concerns its authorization and supervision system. Other than comparable regulatory frameworks in Europe, such
as provided by the Payment Services Directive or the MiFiD II, the Commission Proposal shall be implemented as regulation, which would be directly applicable in all EU member states. Consequently, Crowdfunding platforms intending to operate under the Commission Proposal would need to direct their application to the ESMA as the central European authority. Article 10 of the Commission Proposal provides for an extensive list of required documents and information. The application procedure has been structured in a two-step system: First, the applying Crowdfunding platform shall file a complete set of documents and information. The ESMA would assess received applications within 20 working days and inform the respective applicant of whether the submitted documents and information are complete. Only in a second step, the ESMA shall assess whether the applicant complies with all requirements imposed by the Commission Proposal and issue a reasoned decision (granting or denying the authorization) within further two months. Following the implementation of the Commission Proposal, the ESMA shall establish a central register of all Crowdfunding platforms authorized in the EU, which also indicates withdrawals of authorizations (for a period of five years). Beside the authority of the ESMA to assess applications and grant authorizations, the Commission Proposal would also mandate the ESMA to exercise an extensive set of supervision and enforcement powers. These include wide-reaching notification obligations of the Crowdfunding platform, the right to request (additional) documents and information, as well as the right to conduct on-site visits. Particular attention should be drawn to the extensive scope of powers provided by the Commission Proposal. To conduct its task, the powers of ESMA would not only address the Crowdfunding platform as an authorized entity but also a wide range of other involved stakeholders, such as the persons controlling or being directly or indirectly controlled by the Crowdfunding platform, the involved capital-seeking companies, third parties to whom functions under the Commission Proposal have been designated as well as managers, auditors, and advisors of these actors. Content-wise, the ESMA may—after potentially required permissions by national courts or authorities—review any relevant record, data, or other material, the right to summon and interview any of the mentioned individuals as well as the request of records of telephone and traffic data. To effectively enforce its powers, the ESMA would be entitled to take a variety of enforcement actions against stakeholders violating their obligations under the Commission Proposal. These actions include the issuance of public notices and warnings as well as the imposing of fines in the maximum amount of 5% of the annual turnover of the concerned Crowdfunding platform or periodic penalty payments in the maximum amount of 3% of the average daily turnover in the preceding year (for legal persons) or 2% of the average daily income in the preceding year (for individuals). Periodic payments can be imposed until the respective recipient submits to the orders of the ESMA.

Within its scope of application, the Commission Proposal would impose a rather complex set of rules for the operation and business conduct of Crowdfunding platforms. Covered matters include, inter alia, detailed operating, and organizational requirements (such as the implementation of adequate procedures and policies, the segregation of duties or the avoidance of conflicts of interests), encompassing transparency and reporting obligations toward the ESMA and the involved investors as well as rules of conduct in relation to marketing activities and other communications (such as the requirement for a key investment information sheet, information requirements, and marketing communication rules). Although the actual implementation of the Commission Proposal has not yet been approached, it can be assumed that it would result in significant (financial and organisational) burdens for Crowdfunding platforms authorized under the regime, especially regarding the extensive powers of the ESMA. Although the relevant regulatory requirements under European law are primarily targeted at the business conduct of Crowdfunding platforms, these can (indirectly) also affect the capital-seeking company, which would, for instance, be required to prepare extensive information material on its project(s). Further, it can also be in the (contractual) responsibility of the capital-seeking company toward their crowd investors to only engage a Crowdfunding platform, which duly fulfills the regulatory requirements to provide services in relation to a specific Crowdfunding project.

Drawing the line to the potential implications of the Commission Proposal for ICOs, it makes sense to assess whether and to which extent the Commission Proposal could also serve as a blueprint for future European aspirations to regulate the concept of ICOs in Europe. One of the main issues in this connection concerns the rather...
limited scope of the Commission Proposal. As has been shown, the Commission Proposal excludes certain main topics and stakeholders from its application, making it difficult to assess the practical consequences for the European Crowdfunding market and its stakeholders in advance. The further development of the Commission Proposal to include ICOs would likely require an expansion of its scope. This approach can be based on various main considerations. Other than Crowdfunding, virtual currencies and ICOs have not yet been subject to specific national regimes. The voluntary character of the Commission Proposal, however, has been mainly reasoned with the existence of national regimes for domestic activities of Crowdfunding platforms. This argument would, therefore, not apply to ICOs. In addition, it should also be assessed whether the option of a regulation would be suitable for ICOs. Given the lack of specific national rules, it can be argued that a directive would be more suitable to provide for a (uniform) legal framework on ICOs in Europe. Further, ICO projects usually involve comparably more complex structures. Since ICOs are based on the Blockchain as decentralised payment system for virtual currencies, the tokens or coins issued during an ICO are easily transferrable through so-called virtual currency exchanges. The Commission Proposal would, therefore, also need to include the regulation of virtual currency exchanges and the protection of subsequent investors to its scope. The Commission Proposal already touches this issue by implementing information requirements by means of a so-called “bulletin board” but leaves the responsibility for subsequent transfers of issued instruments to the sole discretion and responsibility of the investors. Based on the above, ICO platforms typically offer the investors a wider range of services. One of the best examples of such peculiar ICO services concerns the provision of so-called “wallet services”, where the investor can store, transfer, and receive issued ICO tokens through a personal account on the Web site of the ICO platform. Such wallet services usually require the ICO platform to enter into a continuous service agreement and establish an ongoing business relationship with the investor. This aspect should also be covered by an (extended) Commission Proposal on ICOs. In any case, to ensure a uniform approach on both concepts, it would make sense for the European legislator to expand its legislative endeavors to the regulation of virtual currencies and ICOs on a European scale. The further development of the Commission Proposal toward ICOs could be a first step in the right direction.

The DAICO Proposal

It has been shown that the recent Impact Assessment of the European Commission for an EU framework on crowd- and peer-to-peer financing presents several scenarios, reaching from the maintaining of the status-quo to the implementation of a comprehensive (stand-alone) legal framework. The Commission, however, did not directly address any issues in relation to the contractual (civil-law) relationships between the investors, the capital-seeking companies, and the Crowdfunding or ICO platforms. Although many provisions derived from EU-level statutes could potentially be applicable to these relationships, the European legislator has not yet communicated specific ideas on how to harmonize the civil-law aspects and consumer protection safeguards for Crowdfunding (and ICO) projects across Europe. Given the rather dense framework of civil-law regulations potentially affecting the conduct of Crowdfunding projects in the EU, this approach is understandable. Especially ICOs, however, have recently been subject to a high number of irregularities from a civil-law perspective, involving cases of fraud, theft, misconduct, as well as the occurrence of Ponzi and pyramid schemes.

In January 2018, Vitalik Buterin, founder of Ethereum (one of the most widespread Blockchain networks), reacted to these developments and proposed the so-called “DAICO model” as innovative solution to overcome some of the most pressing concerns against ICOs and make ICOs more secure for involved investors. To avoid the common risks associated with ICO projects, Buterin basically proposed the implementation of a kind of escrow system by means of a so-called smart-contract to initiate the ICO project, collect the investments from participating investors and allocate the collected funds to the capital-seeking company. The term DAICO is composed by the terms decentralised autonomous organisation (DAO) and ICO. A recent article by Chrisjan Pauw of Cointelegraph provides a good summary:

The DAICO contract will have a mechanism where contributors can send funds to the project in exchange for network specific tokens. When the crowdsale period ends, the contract will prohibit anyone from contributing any further, i.e., normal token sale. There is one variable that comes into effect after the contribution period has ended called the tap variable. This tap in the contract can be programmed to predetermine the amount (per second)
that developers can withdraw from the token sale funds. Initially, the limit will be set to zero, but contributors can then vote on a resolution to increase the tap.

When analyzing this system, the proposal disposes of certain similarities with the Blockchain Governance proposal of Hacker (2017). Generally, it means that the investors in an ICO project are organized as kind of an organ with the power to allocate their investments to the capital-seeking company depending on their continuing support of the funded project or business. Initially, investors provide their investments to an escrow account over which the investors redeem control. The collected funds are gradually released to the capital-seeking company to conduct the funded project upon a democratic vote by the group of investors. According to Buterin, the intention is that the voters start off by giving the development team a reasonable and not-too-high monthly budget and raise it over time as the team demonstrates its ability to competently execute with its existing budget. If the voters are unhappy with the development team’s progress, they can always vote to shut the DAICO down entirely and get their outstanding money back.

Like any newly developed system, the DAICO approach has its advantages and disadvantages. Due to the early stage of this proposal, potential implications on future legislative efforts cannot yet be comprehensively captured. In relation to investor protection issues, the proposal, however, may be initially differentiated into two main aspects. First, the proposed escrow structure provides an increased security for investors, as the funds are not immediately released as down-payments and the capital-seeking company does not immediately have access to the collected investments. This approach can be qualified as effective safeguard to prevent fraud, theft, or misconduct by the capital-seeking company and/or its representatives. Second, the participating investors are granted extensive participation rights regarding the utilization of their investments. As a result, the capital-seeking company is forced to act in a transparent manner and retain the trust of their investors. On the other hand, the proposed system could also lead to a significant dependence of the capital-seeking company to the continuous support of the involved investors, which could potentially undermine the effectiveness of the pursued financing project. Neither the capital-seeking company nor its representatives could ultimately rely on the success of their funding endeavors until the project has been successfully completed and available funds depleted. On the other hand, it is apparent that the mere democratic (majority) vote does not consider the evident issue of minority interests. This concern is further intensified in cases where the founders or other involved stakeholders in the capital-seeking company are participating in the ICO or purchasing a significant number of issued tokens during subsequent trading activities on virtual currency exchanges. As soon as a majority of the investors decides to lock-up or withdraw funds, minority investors would need to accept such vote, irrespectively whether the respective approach is well founded or not.

Concluding, the DAICO proposal of Buterin might solve certain major issues in relation to consumer and investor protection and limit the risk of misbehavior by involved stakeholders. To eliminate potential drawbacks (such as the massive dependence of the capital-seeking company on the goodwill of the investors), the European legislator, however, would need to introduce an escrow model that allows contractual limitations to the right of withdrawal or a general fiduciary duty of the investors. The further pursuit of this concept should in any case be supported and adopted by the legislative aspirations on the European level.

**Conclusion**

The European legislator, the national legislators in the EU member states, as well as involved industry experts introduced a variety of different proposals on how to address the abovementioned issues of Crowdfunding on the European and/or national level. With the introduction of its Commission proposal, the European Commission achieved a major advance in this area. Although the Commission Proposal can be criticized for its presumably limited scope of application, the lack of civil-law and contractual issues during a Crowdfunding project and the rather rigorous supervision and enforcement provisions assigned to the ESMA, it can be considered as important step for the future development of an efficient and effective legal framework for Crowdfunding in Europe. In relation to the future regulation of ICOs, the European legislator has not yet attempted to implement an (encompassing) regulatory framework. The efforts of the European Commission in relation to its Impact Assessment and Commission Proposal provide for various thought-provoking impulses to further pursue the objective of specific legislation on ICOs. Although, it is too early yet
to say what the European legislator has abandoned any plans for future legislations on ICOs, the European legislator should already dedicate an active approach to the potential future regulation of ICOs in Europe. Given the fast-paced development in the field of Crowdfunding and, especially, virtual currencies and ICOs, the future European and national legislative aspirations on these financing concepts will likely require the ongoing attention of involved stakeholders and legal practitioners in the future.

**Notes**

9. ESMA alerts investors to the high risks of Initial Coin Offerings (ICO’s), ESMA (Nov. 13, 2017), ESMA50-157-829; ESMA alerts firms involved in Initial Coin Offerings (ICO’s) to the need to meet relevant regulatory requirements, ESMA (Nov. 13, 2017), ESMA50-157-828.
16. Id.
17. Id.
18. Id.
19. Id.
20. Id.
21. See Dushnitsky, supra n. 7.
22. Bundesgesetz über alternative Investmentformen (Alternativfinanzierungsgesetz, AltFG), BGBl. I Nr. 114/2015.
23. AltFG, § 2 (2); Thus, the AltFG is only applicable to certain equity- and lending-based Crowdfunding models. Reward-based projects are regularly not covered. Until July 2018, the application of the AltFG was further limited to capital seeking companies which are qualified as small and medium sized
enterprises in accordance with Commission Recommendation 2003/381/EG regarding the definition of micro-, small-, and medium-sized enterprises. Further, the investments collected by the capital-seeking company had to be invested in its operative business operations.

24. Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC [2003] OJ L 345/64 (Prospectus Directive); Article 1 (2) h of the Prospectus Directive provides, inter alia, for a general exception of application for a public offer where the total consideration is less than EUR 5,000,000 over a period of 12 months.


26. See Groendahl, supra n. 12.


28. Id.


31. AMF, supra n. 15.

32. Impact Assessment, supra n. 5, at 3.

33. Most Crowdfunding projects give rise to the application of the Consumer Rights Directive (for certain reward-based projects) or the Distance Marketing of Consumer Financial Services Directive (for certain equity- and security-based projects). Both regulations additionally impose vast consumer information undertakings by the involved actors.


37. Id., at 35.

38. Impact Assessment, supra n. 15, at 3.

39. Id.

40. Commission Proposal, supra n. 16.


42. Gutkleisch, supra n. 9, at 76.

43. Commission Proposal, supra n. 16, art. 1 (a)–(c).

44. Commission Proposal, supra n. 16, art. 1 (d).

45. Commission Proposal, supra n. 16, art. 4 (1).

46. Commission Proposal, supra n. 16, art. 3 (1) a.


48. Gutkleisch, supra n. 9, at 74–76.


50. Commission Proposal, supra n. 16, art. 2 (2).


52. Commission Proposal, supra n. 16, art. 2 (2) b.


54. Id.

55. Commission Proposal, supra n. 16, art. 9 (2).


58. Commission Proposal, supra n. 16, art. 10 (1).

59. Commission Proposal, supra n. 16, art. 10 (4), art 10 (5).

60. Commission Proposal, supra n. 16, art. 10 (6).

61. Commission Proposal, supra n. 16, art. 11.


63. Commission Proposal, supra n. 16, chapt. 4, sect. 2.

64. Gutkleisch, supra n. 9, at 78.

65. Commission Proposal, supra n. 16, art. 17.

66. Gutkleisch, supra n. 9, at 77.

67. Id., at 3.

68. Such as the contractual implications of the E-Commerce Directive, the Consumer Rights Directive or the Distance Marketing of Consumer Financial Services Directive.

69. Gutkleisch, supra n. 9, at 74–76.

70. De, supra n 1; Groendahl, supra n. 10.


74. See Hacker, supra n. 40, at 25–27.

75. Buterin, supra n. 75.

76. Id.