



Innovative start-ups and Equity Crowdfunding

The term crowdfunding refers to the process by which a number of people contribute sums of money, even small sums, to finance an entrepreneurial project using internet sites ("platforms" or "portals"). Specifically, the term equity crowdfunding refers to the online investment by which a real and proper shareholding in a company is purchased.

Compared to other countries, Italy has the merit of being the first country in Europe to have a specific and organic regulation on equity crowdfunding. In 2013, Italy regulated the equity crowdfunding market, including through the creation of a special register of authorised online portals. Initially envisaged for innovative startups only, equity crowdfunding was gradually extended first to innovative SMEs, and then, with the 2017 Budget Law, to all Italian small and medium-sized enterprises. Just to have a snapshot of this market according to the MISE report as of 1 July 2021 startups registered in the register exceed 13 thousand, about 3.6 % of all newly incorporated companies.

The instrument falls under the responsibility of Consob, the Financial Markets Supervisory Authority: implementing provisions are given in the Regulation on the raising of venture capital through online portals adopted by resolution no. 18592 of 26 June 2013, updated by resolution no. 20264 of 17 January 2018.

These regulations are of fundamental importance in a country like ours where Small Enterprises represent an important part of the productive fabric. In the same way, these same companies encounter many difficulties in financing their projects and growth by resorting to classic bank financing. These difficulties are even more pronounced for newly established enterprises, better known as start-ups, since the new European rules are making it much more difficult for banks to provide credit to undercapitalised operators, with low profitability and irregular banking relationships.

In order to deal with all this, in the overall design of the legislator, equity crowdfunding is seen as a tool that can foster the development of innovative start-ups through rules and funding methods that can exploit the potential of the internet.

In order to obtain the information necessary to decide whether to invest in financial instruments issued by innovative start-ups, investors consult online portals dealing with equity crowdfunding. These are platforms, supervised by Consob, that facilitate the raising of venture capital for innovative start-ups.

The portals provide investors with information on start-ups and individual offers by means of special forms indicating basic information about the company and in particular the business idea, the people who make it up and the plans they intend to pursue with the investment sought.

Precisely because of the crucial role they play, the legislator has deemed it necessary to guarantee the 'reliability' and 'quality' of the service provided by portals. For these reasons, the management of portals is reserved to two categories of subjects

subjects authorised by Consob and registered in a special register kept by the same Authority; the banks and investment companies (SIM) already authorized to provide investment services (the so-called "managers of right", registered in the special section of the register kept by Consob).

It is important to know that those who manage the portals cannot, in any way, hold sums of money pertaining to the investors, nor directly execute the orders for the subscription of the financial instruments offered on their portals, having to transmit them, for this purpose, exclusively to banks or SIMs. Managers may not provide financial advice to investors in any way.

In summary, the Consob Regulation provides that the investor must be put in a position to acquire adequate knowledge regarding the three main aspects and risks of equity crowdfunding. In particular, the investor must know: who manages the portal; the activities carried out by the portal; how the orders for the subscription of the financial instruments offered are managed; the costs borne by investors; the measures that the portal has put in place to manage the risks of fraud, conflicts of interest, complaints and the proper processing of personal data; the aggregate data on the offers carried out by the portal and the results achieved; the reference legislation.

Let us now summarise the negative and positive aspects of this type of investment.

Clearly, investment in innovative start-ups has special characteristics and higher economic risks than traditional investments, since a start-up offers an idea and a project to realise it. The decision whether or not to invest is therefore not based, as is traditionally the case, on economic and rational elements. All studies dealing with crowdfunding underline the importance of the emotional factor in the choice of the project to be financed. The investor becomes a shareholder to all intents and purposes and therefore participates fully in the economic risk that characterises all entrepreneurial initiatives and since, as mentioned, these are newly established companies operating in innovative sectors, the risk that the entrepreneurial project will not succeed is even greater than for companies that have already been operating in a given sector for some time, which obviously also affects the investors' risk of losing the entire capital invested.

The investor also does not have an immediate financial return because it is not easy for a newly formed company to produce profits in the first few years of life and in addition, the "Growth Decree bis" has even placed a ban on the distribution of profits. Any profits will therefore necessarily be reinvested in the company, increasing the value of the shareholding if the start-up company achieves positive results over time.

In addition to this, there is the risk of illiquidity, as the instruments issued by innovative start-ups are not traded on organised markets, and the Growth Decree prohibits trading on organised markets for as long as the company can be considered an innovative start-up (Article 25, paragraph 2 of the "Growth Decree bis").

But let's see now the advantages of Crowdfunding. First of all, there is the flexibility and the possibility of involving a large number of people even with small investments. In addition, start-ups have the opportunity to check whether their project has immediate market appeal and therefore a non-economic marketing return that would otherwise be difficult to achieve.

Recent studies have shown that crowdfunding is increasingly becoming a springboard for start-ups and new business ideas and a valid alternative to other more traditional forms of financing. But not only that, crowdfunding often represents a valid alternative to other ways of raising funds that are often precluded to those who do not have a track record of loans or entrepreneurial activities.

In the specific case of the equity-based model, raising capital (if successful) could have several advantages, such as paving the way towards obtaining other resources even on real stock exchanges, i.e. - for example - within regulated markets.

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