

# Association of Accounting Technicians response to ISA qualifying investments: consultation on whether to include investment based crowdfunding

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## 1. Introduction

- 1.1. The Association of Accounting Technicians (AAT) is pleased to have the opportunity to respond to the consultation paper on ISA qualifying investments: consultation on whether to include investment based crowdfunding (condoc), released on 8 July 2015.
- 1.2. AAT is submitting this response on behalf of our membership and from the wider public benefit of increasing the choice of investments available to ISA investors, as a trusted and effective savings product.
- 1.3. AAT has added comment in order to add value or highlight aspects that need to be considered further.

## 2. Executive summary

- 2.1. AAT shares the government's view in being "pleased in seeing the continuing success of crowdfunding in the UK and notes the impressive annual growth rates of 201% for equity crowdfunding and 63% for debt crowdfunding" (1.2, condoc); the alternative finance market is contributing to the growth and vitality of the UK economy as well as having a positive social impact on philanthropic giving and volunteering.
- 2.2. AAT welcomes any move by the government to further encourage investment in crowdfunding platforms, including the inclusion of the platforms as ISA qualifying investments (para 5, section 4, condoc).
- 2.3. AAT is mindful that any proposed changes must be consistent with the reputation of ISA as a trusted, flexible and appropriately-regulated savings and investment product, and any changes should support a sustainable tax system and should be simple to apply (para 4, section 2, condoc).
- 2.4. As a means of safeguarding debt-based crowdfunding, AAT recommends that consideration should be given for this type of security to be within the remit of the Financial Services Compensation Scheme (FSCS) (3.10, below).
- 2.5. AAT is cautious of the FCA ruling that a platform is regulated depending on the type of product it offers, rather than the risk profile of the business invested in (3.13, below).
- 2.6. The 14 day cooling off period and access to financial ombudsman is welcomed by AAT (3.14, below).
- 2.7. AAT recommends that safeguards are introduced to encourage investors to take time to carry out research if they are interested in a non-regulated platform, as the platforms may not have signed up to safe practices (3.20, below).

## 3. AAT response to the consultation paper on ISA qualifying investments: consultation on whether to include investment based crowdfunding.

- 3.1. The following paragraphs outline AAT's response to the proposals contained in the consultation paper.

**Question 1.**

**Do you agree with the proposed principles for assessing whether to extend ISAs to equity and debt securities offered via a crowdfunding platform?**

- 3.2. As a representative body, AAT does not have direct experience of ISAs although AAT agrees that any proposed changes must be consistent with the reputation of ISA as a trusted, flexible and appropriately-regulated savings and investment product; consumers should be treated fairly, with a proportionate level of risk that is communicated fully and transparently. Market or regulatory safeguards should be in place to promote competition and prevent market abuse that could detriment the consumer.
- 3.3. Changes should support a sustainable tax system and should be simple to apply and provide certainty without excessive administrative burdens on ISA managers or HMRC in terms of compliance, reporting and monitoring requirements.

**Question 2.**

**Specifically, could respondents provide views on the key characteristics of:**

- Crowdfunding Platforms
- 3.4. Understanding Alternative Finance: The UK Alternative Finance Industry Report 2014<sup>1</sup>, a publication produced by University of Cambridge and NESTA, identifies that crowdfunding has given individuals more control over their money. At the same time, entrepreneurs, SMEs, charities and community organisations are obtaining much needed finance which in many cases they would not otherwise be able to secure. AAT acknowledges that it is evident from the research that the alternative finance market is contributing to the growth and vitality of the UK economy as well as having a positive social impact on philanthropic giving and volunteering.
    - Debt-based Securities
  - 3.5. Lenders are able to provide much needed debt financing and the lender receives a debt instrument that pays interest in return.
  - 3.6. While the exact scope of debt and equity based crowdfunding has not been defined in legislation, AAT supports the proposal to allow crowdfunded debt securities to be eligible for inclusion within ISAs.
    - Equity-based Securities offered via a Crowdfunding Platform
  - 3.7. Bruegel, a European independent and non-doctrinal think tank that specialises in economics, commissioned a report<sup>2</sup> by Wilson and Testoni that suggests that equity crowdfunding may be significantly riskier than business angels or venture capital finance, due to a “lack of adequate pre-investment support and monitoring”, arising from relatively inexperienced investors lacking the required investment know-how. The scale of these potential risks will become better known over time as the performances of a range of crowdfunded investments are observed.
  - 3.8. AAT recognises that the importance of tax incentives, in the form of the Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS), to the incipient equity crowdfunding market is clear. Many crowdfunding platforms have made a concerted effort to promote the tax incentives to investors – indeed some platforms host exclusively SEIS/EIS-eligible companies.

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<sup>1</sup> [Understanding Alternative Finance: The UK Alternative Finance Industry Report 2014](#)

<sup>2</sup> [Improving the role of equity crowdfunding in Europe's capital markets](#)

- 3.9. AAT wishes to clarify that Negligible Value Claims, allowable on capital losses arising from the disposal of shares<sup>3</sup> subscribed for in a qualifying trading company, would be available for offset against income, as a means of mitigating any losses.

**Question 3.**

**Do debt-based securities; and equity-based securities, offered via a crowdfunding platform meet the 'protect the consumer' principles? Would any additional safeguards be required if these securities became eligible for ISA? Please explain your answer.**

- 3.10. Out of recognition that investments made through crowdfunding platforms are currently not covered by FSCS, AAT recommends that additional safeguards should be considered if the securities set out in question 3 became eligible for ISA, including consideration as to whether debt-based securities should be within the remit of FSCS.

**Question 4.**

**How far are debt-based securities and equity-based securities offered via a crowdfunding platform already subject to the safeguards?**

- 3.11. The Financial Conduct Authority (FCA) has taken an active role in monitoring equity crowdfunding activity and provided a regulatory framework to support these developments.
- 3.12. New FCA rules<sup>4</sup> that include measures to provide better investor protection came into force on 1 April 2014 following a period of active consultation.
- 3.13. Under the new rules, investment-based crowdfunding includes firms that deal in 'non-readily realised securities' i.e. debentures and equity investments. AAT is cautious of the decision to regulate a platform depending on the type of product it offers, rather than the risk profile of the business invested in.
- 3.14. AAT welcomes the 14 day cooling off period<sup>5</sup>, which was introduced by the FCA to regulate crowdfunding, and access to the financial ombudsman.

**Question 5.**

**What additional safeguards, if any, would be needed to ensure that debt and equity securities offered via a crowdfunding platform are not susceptible to tax avoidance if made eligible for ISA?**

- 3.15. AAT is of the opinion that current safeguards ensure that the debt and equity securities offered via a crowdfunding platform would not be susceptible to tax avoidance. The General Anti Avoidance Rule (GAAR)<sup>6</sup> may be sufficient to deal with situations where debt and equity securities offered via a crowdfunding platform are being used for aggressive tax avoidance.
- 3.16. At this stage it is difficult to foresee what additional safeguards might be required in addition to the GAAR. Therefore, AAT would recommend that HMRC monitor the usage of crowdfunding and adopt appropriate strategies to deal with aggressive tax avoidance as and when particular issues are identified.
- 3.17. In addition investors must also pass an online appropriateness test<sup>7</sup> to prove they are aware of the risks.

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<sup>3</sup> [Relief under TCGA 1992, s24](#)

<sup>4</sup> <http://www.fca.org.uk/firms/markets/international-markets/mifid-ii/mifid-review>

<sup>5</sup> <http://www.fca.org.uk/news/the-financial-conduct-authority-outlines-how-it-will-regulate-crowdfunding>

<sup>6</sup> <http://www.legislation.gov.uk/ukpga/2013/29/part/5/enacted>

<sup>7</sup> <http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/cobs/examples/app-case-study-1>

- 3.18. Furthermore, the UK crowdfunding scene has also established its own code of conduct through UK Crowdfunding Association (CFA).
- 3.19. The CFA provides strict guidelines to vet platforms before giving their seal of approval – including making sure that the investment is ring-fenced away from the main finances of the company in the event of bankruptcy of the company.
- 3.20. Out of a recognition that companies wishing to raise funds through Crowdfunding are operating in fairly uncharted waters and that they sometimes fall outside of channels regulated by the FCA and CFA.
- 3.21. AAT recommends that safeguards should be introduced to encourage investors to take time to research if they are interested in a non-regulated platform, as the platforms may not have signed up to safe practices.

**Question 6.**

**Are there types of debt security offered via a crowdfunding platform that respondents believe will not be covered by the Personal Savings Allowance?**

- 3.22. AAT recognises that dividends from equity-based securities would not be covered by the Personal Savings Allowance.

**Question 7.**

**Do respondents feel there is a compelling case for extending ISAs to equity offered via a crowdfunding platform in addition to existing tax reliefs?**

- 3.23. AAT supports the proposal inherent in question 7 for extending ISAs to equity offered via a crowdfunding platform in addition to existing tax reliefs, so that dividends received would be tax-free.

#### **4. Conclusion**

- 4.1. AAT welcomes the government move to further encourage investment in crowdfunding platforms, including the inclusion of the platforms as ISA qualifying investments (para 5, section 4, condoc).
- 4.2. Furthermore, AAT supports the proposal to allow crowdfunded debt-securities and equity-based investments to be eligible for inclusion within Individual Savings Accounts (ISAs), on the basis that consideration is given to including crowdfunding within the remit of the FSCS.
- 4.3. AAT recommends that safeguards are introduced to encourage investors to take time to carry out research if they are interested in a non-regulated platform, as the platforms may not have signed up to safe practices (3.20, above).

#### **5. About AAT**

- 5.1. AAT is a professional accountancy body with over 49,300 full and fellow members<sup>8</sup> and 76,400 student and affiliate members worldwide. Of the full and fellow members, there are over 4,100 members in practice who provide accountancy and taxation services to individuals, not-for-profit organisations and the full range of business types.
- 5.2. AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

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<sup>8</sup> Figures correct as at 30 June 2015

## 6. Further information

If you have any questions or would like to discuss any of the points in more detail then please contact AAT at:

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