The Wisdom of Crowds

While there remains some room for doubt as to whether crowdfunding is the fundraising wave of tomorrow or just a passing phase, in the meantime, the industry has grown to over $5.1 billion worldwide, and crowdfunding campaigns are raising large sums for a great variety of projects.

In Israel, access to equity-based crowdfunding has to date been restricted due to the limitations of the Securities Law, 1968 ("the Securities Law"), which with certain exceptions prohibits offers of securities to the public other than by way of the issue of a prospectus approved by the Israeli Securities Authority ("the ISA")..

In recognition of the need to enable start-up companies and small businesses (which generally are unable to bear the costs associated with a public offering) to gain access to such financing, a new proposal to amend the Securities Law has recently passed a preliminary vote. The proposed amendment aims to reduce the statutory limitations on online public offerings (the platform for most crowdfunding), while nevertheless aiming to strike a balance by maintaining certain protections for investors, by way of defining the types of companies which are eligible to benefit from the proposed amendment, and maintaining certain limitations with a view to protecting investors from exposure to risks.

The proposed amendment, entitled the Securities Law (Amendment – Social Business Financing) Bill, 2014 ("the Bill"), proposes that the following types of companies be entitled to operate online fundraising:

1. A company which has received benefits for research and development from the Office of the Chief Scientist of the Ministry of Economy ("the OCS") pursuant to the Encouragement of Industrial Research and Development Law, 1984.

2. A company which has received confirmation from the OCS that it has expended funds on research and development.

3. A company which has received a recommendation for a grant or a loan from a fund aimed to assist small and medium size business from the Business Development Center ("the BDC").

4. A company in respect of which the head of the BDC has confirmed in writing that it meets the minimum conditions determined by the Agency for Small and Medium Sized Businesses at the Ministry of Economy for the carrying out of online fundraising.

5. A company which has received benefits from the Export Assistance Fund of the Foreign Trade Administration at the Ministry of Economy.

In keeping with its aim of creating a controlled environment for online fundraising, the Bill also imposes limits on the amounts which individual investors may invest, which differ based on annual income.

Furthermore, while falling well short of the type of information disclosure required in a prospectus, the Bill requires the provision by the finance-seeking company of certain information and reports, including as to the risks involved in making the requested investment, and establishes liability for the provision of any misleading information.
A further qualification is that a company wishing to carry out online fundraising must be registered in a special registry to be maintained by the ISA, qualification for which includes the requirement that the company, in the opinion of the ISA, has the technological knowledge and wherewithal to operate a fundraising website in such a way as to maintain the integrity of the site and the security and privacy of investors and their information.

While the Bill may nevertheless undergo metamorphoses on its journey to final legislation, it would appear to be a positive first step.