



**TILBURG UNIVERSITY**  
**MASTER IN INTERNATIONAL BUSINESS LAW**  
**LAW SCHOOL**

**IS EQUITY CROWDFUNDING VIABLE IN COLOMBIA?**  
**CASE STUDY: Nemo: A legal structure that allows equity platforms to operate under**  
**the existing regulation**

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## INTRODUCTION

Nemo is a project to launch the first equity crowdfunding platform in Colombia. This project was born with the idea of transmitting knowledge and business insight to entrepreneurs in order to help them fill the funding gap existing in the entrepreneurial cycle. The founders of this project created Nemo as a tool to enhance the ecosystem that seems stagnant when it comes to financing, giving the entrepreneurs the opportunity of realizing their business ideas and having a social impact in Colombia's economy and society.

Colombia has a history full off difficulties that has affected every sector in the country (social, economic and cultural). Due to the existing economical need in the country, the inequality and the high rates of unemployment, which are determining factors for the country and its citizens to focus its efforts towards prosperity, the concept of progress is changing. Thus, the creation of business and innovative ideas are becoming a main strategy in order to obtain income and economic growth. However, the success of these new companies is going to be dependent on the services and the quality of their products and the hard work of the entrepreneurs, not so much on the government's support<sup>1</sup>.

The concepts of entrepreneurship and innovation in a country as Colombia are not a novelty; in fact the government has focused its efforts on developing strong institutional frameworks to improve the entrepreneurial ecosystem, recognizing that innovation is the engine that moves the economies all around the world. For countries that are considered third-world or developing countries like Colombia, innovation and entrepreneurship can open the door to progress, increase the countries' development and their economic indicators. Entrepreneurship and innovation could also give the countries a greater chance of growth through the creation of new jobs and innovative ideas that eventually will give them the opportunity to compete in different markets in a more sophisticated level<sup>2</sup>.

However, financing is a key element for the entrepreneurship and innovation, especially when the entrepreneurs are at the initial phase of their projects where in most of cases they do not have access to traditional credits or the credits offered to them do not match their business structure. It is in this moment, when Colombia's government needs to face the challenge of creating a legal framework that regulates alternative financing methods, like crowdfunding, in order to keep the cycle of this new playground going.

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<sup>1</sup> Hung Manh Chu, Cynthia Benzing, and Charles Mcgee, "Ghanaian and Kenyan entrepreneurs: a comparative analysis of their motivations, success characteristics and problems" (2007), Journal of Developmental Entrepreneurship 12(03), pp. 295-322 and <https://doi.org/10.1080/10835410701606910> accessed September 2016.  
<sup>2</sup> Fernando Gómez Gil, Daniel Sánchez, and Daniel Sánchez, "Innovación y emprendimiento en Colombia: Balance, Perspectivas y Recomendaciones de Política, 2014-2018" (2014) Fedesarrollo. Edición Convocatoria Germán Botero de los Ríos. Presidential Debates. P7. ISBN: 978-958-57963-8-6 < <http://hdl.handle.net/11445/149> > accessed 15 January 2016.

Nowadays, crowdfunding is a mechanism used in order to raise money and finance certain projects regardless of whether the projects profit or not. This financing method is considered very innovative because its use of the Internet and social networks, giving the opportunity to many entrepreneurs who do not have the economic sources to catalyze their ideas reaching a large number of stakeholders to raise the funds needed and to become an important alternative funding method for entrepreneurs that disrupts the traditional financial market.

According to the CF2015 Crowdfunding Industry Report “*Global crowdfunding experienced accelerated growth in 2014, expanding by 167 percent to reach \$16.2 billion raised, up from \$6.1 billion in 2013. In 2015, the industry is set to more than double once again, on its way to raising \$34.4 billion*”<sup>3</sup>. Hence, crowdfunding has become a trending phenomenon in the developed world, but the developing countries have a lot of potential stimulating entrepreneurs to innovate, to create jobs and therefore to increase their economies’ growth through this mechanism. Consequently, crowdfunding can be part of the competitive world with high-technology products<sup>4</sup>.

In this scenario, where most of the innovative projects and initiatives are blocked due to the lack of resources, where the entrepreneurial ecosystem gets paralyzed and the economy stagnant, Nemo, the first equity crowdfunding platform in Colombia was created. The platform has the intention of becoming the most useful tool for entrepreneurs and small and medium enterprises (*Micro, medianas y pequeñas empresas* “MIPYMES”<sup>5</sup> for its name in Spanish) to obtain the resources needed. Nonetheless, the creation of Nemo has not been an easy project; during its creation its founders faced several difficulties, especially due to the restrictive regulation of the financial system in Colombia and the lack of regulation regarding the crowdfunding.

Nemo was created and its main objective is to help entrepreneurs to get the funds required and provide legal and financial advice to them during the whole process. The platform is going to be launched in the first semester of 2016 with an outstanding business model that would allow it to operate if is not declared illegal according to the existing regulation.

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<sup>3</sup>CF2015 The Crowdfunding Industry Report <<http://www.crowdsourcing.org/editorial/global-crowdfunding-market-to-reach-344b-in-2015-predicts-massolutions-2015cf-industry-report/45376>> accessed 25 March 2016

<sup>4</sup> Crowdfunding’s Potential for the Developing World. 2013. infoDev, Finance and Private Sector Development Department. Washington, DC: World Bank p.14 <[http://www.infodev.org/infodev-files/wb\\_crowdfundingreport-v12.pdf](http://www.infodev.org/infodev-files/wb_crowdfundingreport-v12.pdf)> accessed 25 February 2016

<sup>5</sup> Defined in the Law 905 of 2004, Article 2: 1. Medium Enterprises: a) Personnel between fifty-one (51) and two hundred (200) workers, or b) Total assets worth between five thousand and one (5.001) to thirty thousand (30,000) monthly legal minimum wages. 2. Small Enterprises: a) Personnel between eleven (11) and fifty (50) workers, or b) Total assets valued between five hundred and one (501) and less than five thousand (5,000) monthly legal minimum wages. 3. Microenterprise: a) Personnel not exceeding ten (10) workers or, b) Total assets excluding property worth less than five hundred (500) monthly legal minimum wages.

We selected Nemo to be our case study in order to explain the cultural, economic and legal context in which it is developed, which leads us to the following question: Is equity crowdfunding viable in a country like Colombia? What solutions can we suggest to make equity crowdfunding work?

In order to answer the previous questions, throughout this thesis we will expose Colombia's situation regarding entrepreneurship, innovation and technology. We will describe the advantages and risks of having an alternative financing method like crowdfunding, the existing legal barriers in the financial system. Finally, we will compare the legal requirements for platforms in different legislations such as United States, Italy and Spain and we will suggest what we consider necessary in order to create a legal framework that allows equity crowdfunding to operate. All this analysis will be applied to Nemo and its business model in the Colombian market.

In summary, the purpose of this thesis is to describe the Colombian context regarding entrepreneurship, innovation and technology in order to analyze the implementation and viability for equity crowdfunding in the country and to expose the creation process of Nemo. While reading this document, readers will have access to a more complete overview of Colombia's reality regarding entrepreneurship and crowdfunding. Therefore, this thesis is aimed at all the entrepreneurs who would like to use crowdfunding as a method to raise money in Colombia, to all the venture capitalists and to all the investors who are planning to expand their portfolios in the country.

## **CHAPTER 1: Case Study: Nemo**

Nemo is the first equity crowdfunding platform created in Colombia that connects entrepreneurs with investors. Nemo's founders created this platform in an attempt to provide a complete assessment to start-ups and MIPYMES with the objective of changing the entrepreneurial industry in Colombia.

Creating Nemo has been a real challenge, the first thing that Nemo's founders decided to do was to quit their jobs and get out of the comfort zone they were used to, and start their path into what they call an adventure.

Nemo is created to support entrepreneurs in a complete manner giving them financial and legal assistance if required, accelerating their productivity and competitiveness and subsequently making the projects attractive for investors. The whole project is based on a friendly notion of funding, opposite to the "*shark*" concept existing in the industry.

Throughout Nemo's creation process, its founders have faced a lot of difficulties and barriers. To begin with, in Colombian's context distrust is one of the greatest threats to the emergence of new financing alternatives due to several scandals that have arisen in the past years involving pyramids or Ponzi schemes. Consequently the investment culture has been affected.

On the other hand, the lack of regulation in the country for this type of funding; the absence of knowledge about crowdfunding itself; the existing legal restrictions and the lack of support from the government have made Nemo's development a real defiant project.

Therefore, we will expose how was Nemo's creation process, its business model and we will give readers a closer vision about the Colombian context in terms of entrepreneurship.

### **1.1. How was Nemo created?**

Two years ago, Nemo's CEO a business manager who has been working most of his life as a stockbroker and inside the financial market and Nemo's Legal Manager, a lawyer who has worked in M&A transactions and as a corporate lawyer, decided to be part of the entrepreneurial ecosystem and transfer all their knowledge and experience to entrepreneurs making a major impact in society.

Nemo's aim is to become the most important ally for entrepreneurs at a seed stage that are looking for capital, marketing and assessment, leading to the productive development of the country and to its entrance into more competitive markets with stronger and more productive companies.

The idea of creating Nemo started with Nemo's Legal Manager experience while he was working for the Productive Transformation Program managed by Bancoldex<sup>6</sup>. During this experience Nemo's Legal Manager had a better approach to different sectors of the economy and he was able to analyze their needs, its potential and all the difficulties that entrepreneurs have to deal with when it comes about finding the economic resources needed, notwithstanding the educational and innovative context of the country.

Therefore, the best way to achieve their objectives was to take a look at the global market and observe which one was the best method for entrepreneurs at a seed stage to finance their projects. So, the initial idea was to create a lending-based platform, however once the project was validated and analyzed into Colombia's reality they decided to change the model to equity crowdfunding. However, changing the model from lending-based to equity-based crowdfunding has not made Nemo's development easier. Understanding Colombia's cultural, financial, educational and legal background was their first step.

According to the Global Competitiveness Report of 2015-2016 of the World Economic Forum (hereinafter "WEF"), Colombia ranked 61<sup>st</sup> out of 140 countries evaluated, rising 5 positions compared to the last year's report, and its performance throughout the 12 pillars could be generally considered as good compared to the regional standard where Colombia was positioned as the fifth best economy. Nevertheless, the quality of the education, especially in math and science, was ranked as 117<sup>th</sup> and innovation was ranked as 93<sup>rd</sup><sup>7</sup>.

In addition, the WEF report also includes the Executive Opinion Survey where business leaders are interviewed regarding certain topics in order to establish *"the appetite for entrepreneurial risk, the extent of collaboration within a company or with external entities, and the level of corruption—which makes it an essential complement to the more traditional data provided by international organizations and national statistical offices"*<sup>8</sup>

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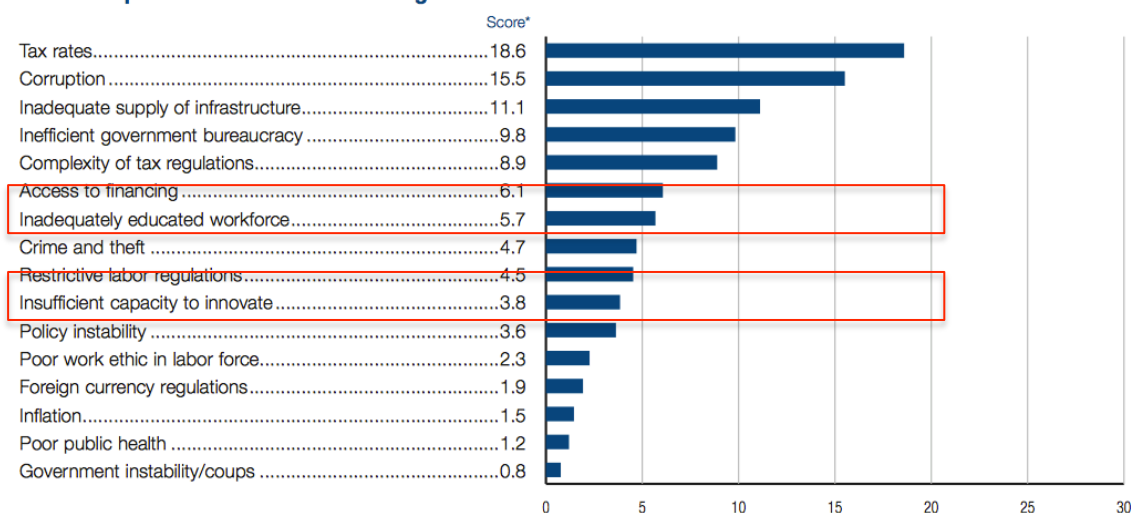
<sup>6</sup> Is the Colombian bank for business development. It designs and provides new instruments, financial and non-financial, to boost competitiveness, productivity, growth and development of micro, small, medium and large Colombian companies, whether they are exporting companies or the belong to the domestic market. (translated from the Spanish by the Author) [*"Es el banco de desarrollo empresarial colombiano. Diseña y ofrece nuevos instrumentos, financieros y no financieros, para impulsar la competitividad, la productividad, el crecimiento y el desarrollo de las micro, pequeñas, medianas y grandes empresas colombianas, ya sean exportadoras o del mercado nacional"*] <<https://www.bancoldex.com/acerca-de-nosotros92/Que-es-Bancoldex.aspx>> accessed 25 February 2016.

<sup>7</sup> Klaus Schwab, World Economic Forum. *"The Global Competitiveness Report 2015–2016"*. (2015) <[http://www3.weforum.org/docs/gcr/2015-2016/Global\\_Competitiveness\\_Report\\_2015-2016.pdf](http://www3.weforum.org/docs/gcr/2015-2016/Global_Competitiveness_Report_2015-2016.pdf)> P.49 accessed 25 February 2016.

<sup>8</sup> Ibid. P. 75

The result of the survey is taken into account to determine the Global Competitiveness Index (GCI), and this year results showed that the most problematic factors for doing business in Colombia are access to financing, inadequate educated force, and the capacity to innovate among others, which are considered as a risk when investing.

#### The most problematic factors for doing business



Source: World Economic Forum. The Global Competitiveness Report 2015–2016<sup>9</sup>. Modification to the graphics made by the Author

The analysis of the report demonstrates that despite the economic growth and the improvement that Colombia has presented over the last years, the education, the capacity to innovate and the limited access to financing are still insufficient in comparison with other countries. In addition, the lack of resources becomes a barrier for entrepreneurs' either to start their businesses or to improve them. Consequently, the existing companies are not competitive enough to enter to the new economies with innovative products, which affect the country's economy and growth.

Therefore, in order to understand the Colombian context regarding entrepreneurship, innovation and technology, we are going to analyze the most important factors that affect the industry today and that could lead us to the conclusion that Colombia needs to open the door to new funding alternatives for the developing business.

## 1.2. Colombia's indicators regarding science, technology and innovation.

The purpose of this section is to emphasize the importance of science, technology and innovation for the entrepreneurial culture and Colombia's development. These factors must be interrelated, since

<sup>9</sup> Ibid. P.142



their joint function allows the entrepreneurship to create impact in a competitive and in a productive level. Nonetheless, Colombia's indicators are still low compared to other countries, which create a barrier that prevents the mobilization and the dynamism of the market that nowadays orbits around technology and innovation.

According to the report "*Innovación y Emprendimiento in Colombia: Balance, Perspectivas y Recomendaciones de Política, 2014-2018*"<sup>10</sup>, Colombia presents an evident lag in science, technology and innovation compared with countries in similar situations. This low level of development is caused by the three following factors:

1) Human capital: People do not have a high-level of education, so there are not enough technicians and professionals in science to create innovative products. During the period of 2002 and 2011 Colombia's education presented a slow increase regarding graduates from high-level institutions going from 133.442 to 267.708<sup>11</sup>.

2) Financing channels: Due to the low investment in research and development made by the Government. In 2012 Colombia's investment on research and development was of 0.17% of the Gross Domestic Product (GDP) while Chile, Mexico and Argentina invested almost 0.5% of their GDP. Of these investments the private sector invested around 40%<sup>12</sup> while other countries like Israel and South Korea invested 75%. However these figures did not include the investments that were going to be destined to science, technology and innovation through the General System of Royalties (*Sistema General de Regalias*)<sup>13</sup> that would have reached by 2014 0.6% of the Gross Domestic Product (GDP)<sup>14</sup>.

3) Scientific production and innovative culture: Since there is no entrepreneurial culture that leads to the creation of innovative business recognized through patents and publications, Colombians are not

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<sup>10</sup> Hernando José Gomez y Daniel Mitchell, "*Innovación y Emprendimiento in Colombia: Balance, Perspectivas y Recomendaciones de Política, 2014-2018*" (2014) Fedesarrollo. Edición Convocatoria Germán Botero de los Ríos. Presidential Debates. P13. ISBN: 978-958-57963-8-6 <<http://hdl.handle.net/11445/149>> accessed 15 January 2016.

<sup>11</sup> Ibid., p 17.

<sup>12</sup> According to the Statistics Administrative Department (*Departamento Administrativo Nacional de Estadísticas* "DANE" for its name in Spanish) and the Colombian Observatory of Science and Technology (*Observatorio Colombiano de Ciencia y Tecnología* "OCyT" for its name in Spanish) the expenditures of private firms in science, technology and innovation by 2014 was of 36.36% equivalent to a USD\$1.157.178 which not a high figure for the size of the country.

<sup>13</sup> Is a system that was created by the transitory Decree Law 4923-2011, which determines the distribution, objectives, goals, management, execution, control, efficient use and allocation of revenues coming from the exploitation of non-renewable natural resources and specifies the conditions of participation of its beneficiaries. [*"Sistema creado por el Decreto Ley Transitorio 4923-2011 el cual determina la distribución, objetivos, fines, administración, ejecución, control, el uso eficiente y la destinación de los ingresos provenientes de la explotación de los recursos naturales no renovables precisando las condiciones de participación de sus beneficiarios"*] <<https://www.sgr.gov.co/Qui%C3%A9nesSomos/SobreelSGR.aspx>> accessed 3 March 2016.

<sup>14</sup> *Innovación y Emprendimiento en Colombia* (n 10). P, 14.

prepared to face the challenges of a modern economy moved around innovative start-ups, especially high-technology start-ups<sup>15</sup>.

When being stalled, the country's possibilities of entering into new markets are reduced, since there is no creation of innovative products or services. Therefore, without the right support either from the government or from the private sector, in order to foster science, technology and innovation, the entrepreneurship is not able to arise and Colombia's rates of growth would be small.

### 1.3. Regulatory framework for entrepreneurship

As describe in the previous section, science, technology and innovation are essential to entrepreneurship's development. Colombia is aware of the necessity of supporting these areas in order to stimulate the country's economic and social growth. Thus, the State has focused its efforts on developing legal frameworks to increase the number of innovative start-ups and stimulate the innovation towards economic growth.

Colombian government has approved different laws that encourage and stimulates entrepreneurship and business creation<sup>16</sup>:

- Law 590 of 1999, modified by Law 905 of 2004 and Law 1151 of 2007, the main purpose of these regulations is to promote the development of the MIPYMES.
- Law 1014 of 2006, its objectives are to promote the entrepreneurial culture establishing regulatory principles that lay the groundwork for a state policy and a legal and institutional framework to promote entrepreneurship and business creation; to create a link of the education system and national production system through training in basic skills, job skills, citizenship skills and business skills through a cross-chain of entrepreneurship; to encourage better conditions of institutional environment for the creation and operation of new businesses, in order to stimulate and address the country's economic development.
- Law 789 of 2002 through which was created *Fondo Emprender*, which is a capital seed fund subscribed to the National Learning Service (*Servicio Nacional de Aprendizaje* "SENA" for its name in Spanish), there this entity is in charge of the management of the fund and its main objective is to finance business ventures developed and proposed by the SENA apprentices, the students or professionals who studied in a recognized institution of education. In order to

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<sup>15</sup> Ibid., p 17-20.

<sup>16</sup> Wilmer H. Escobar. "Marco Legal para la Política Nacional de Emprendimiento" (2013) Revista Empeñe. <<http://emprende.co/emprendimiento/marco-legal-para-la-pol%C3%ADtica-nacional-de-emprendimiento>> accessed 4 March 2016, "Política Nacional de Emprendimiento" (2011) <<http://www.mincit.gov.co/minindustria/publicaciones.php?id=16435>> accessed 4 March 2016.

access to the financial aid is necessary to accomplish certain requirements like having a structured plan of business.

- Law 1286 of 2009, whereby the National System of Science and Technology and *Colciencias* are strengthened in order to have a productive model based on science, technology and innovation and to add more value to the products, so as to promote the productive economy and a new national industry.

There are also several programs created by the Government to support entrepreneurs:

- *Innpulsa* was established in February of 2012 and is supported by *Bancoldex* and the Ministry of Commerce, Industry and Tourism to support and promote entrepreneurial culture in order to have a conducive environment for dynamic and innovative entrepreneurship. *Innpulsa* provides co-financing resources to venture proposals in accordance with open calls made by the entity, in which the requirements to be fulfilled are defined. Therefore, those resources are granted only to the proposals that comply with the eligibility and feasibility requirements<sup>17</sup>.
- Apps.co is an initiative of the Ministry of Information, Technologies and Communications and its program *Vive Digital* which aims to promote and enhance business building through the use of IT, focusing on the development of mobile applications, software and content. This initiative also works with open calls regarding specific subjects and the support is only provided to the entrepreneurs who comply the requirements<sup>18</sup>.
- *Emprende Cultura* is a project of the Cultural Ministry that promotes cultural entrepreneurship with a sustainable optic stimulating different management abilities to develop cultural project within the local context<sup>19</sup>.

Despite the efforts made by the government with the creation of these programs and the enactment of the legal framework to promote entrepreneurship, there is still a big percentage of entrepreneurs who cannot access the public resources assigned for their support, because only few are chosen with that purpose. According to José Miguel Benevente, Division Chief of the Competitiveness and Innovation Division at the Inter-American Development Bank (IDB), the public sector has made a lot of efforts supporting the start-ups in the Latin American Region, however one of the main challenges for the region has to do with culture and the flow of ideas taking into account that out of 100 ideas, 10 are financed and only 2 are materialized<sup>20</sup>.

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<sup>17</sup> < <https://www.innpulsa.com.co/es/nuestra-organización> > accessed 4 March 2016.

<sup>18</sup> < <https://apps.co/acerca/appscs/#8> > accessed 4 March 2016

<sup>19</sup> < <http://emprende-cultura.mincultura.gov.co:8060/web/guest/nosotros> > accessed March 4 2016

<sup>20</sup> *Los desafíos del emprendimiento y las start-ups en América Latina. Revista Dinero.* < <http://www.dinero.com/emprendimiento/galeria/los-desafios-del-emprendimiento-y-las-startups-en-america-latina/221391> > accessed 4 March 2016.

## 1.4. Financing Sources to create Businesses

*“The source and the availability of financing for an SME are seen as the major factors behind its development, growth and success. The financial needs and the financing options open to SMEs vary depending on the stage in a firm’s lifecycle. The access an SME has to capital depends on a number of factors, such as its level of development, the availability of finance in its jurisdiction, the nature of its business and its marketing capabilities, and the professional connections of the entrepreneur in charge. The level and the type of demand for financing throughout an SME’s lifecycle depends on its stage of growth, as each stage requires a different financing strategy. This approach enables the business to grow and reach the capital markets, where it can raise long-term financing and sustain its growth”<sup>21</sup>.*

For the entrepreneurs and MIPYMES one of the most difficult barriers to overcome is the access to traditional financing methods, therefore most of them use their own resources (savings) to start their own businesses. Secondly, they resort to family and friends, either through loans or donations. Finally they turn to financial institutions to obtain credit for their business<sup>22</sup>. However most of the entrepreneurs are not qualified to acquire the credit because they do not comply with the requirements requested by the financial institutions, such as guarantees, leverages or because they do not have credit history (which is very common); nor financial or structured business plans.

According with the paper “*Reporte de la Situación del Crédito en Colombia 2015*” published by the Central Bank of Colombia<sup>23</sup> (*Banco de la República de Colombia*), the financial institutions such as banks, financing companies and financial cooperatives take into account different criteria to evaluate the credit granting. Among the features evaluated is possible to find the repayment capacity of the borrower; the activity of the debtor and the lack of information provided by the borrower to the institutions. However, the most important item assessed is the applicant’s projected cash flow and his credit history. The report showed that by December of 2015 small enterprises and microenterprises (first five columns in the graphic) were the companies who had less access to credit while the medium

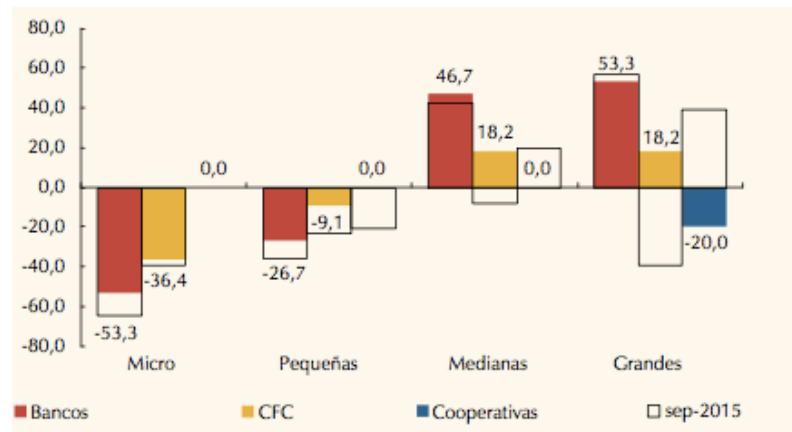
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<sup>21</sup> SME Financing Through Capital Markets Final Report (2015). The Growth and Emerging Markets Committee of the International Organization of Securities Commissions. P 12. < <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD493.pdf> > accessed 15 February 2016.

<sup>22</sup> Maria de los Angeles Briceño Moreno, “*Fuentes de Financiación para el Emprendimiento y su Potencial para Articularse a la Red Nacional de Emprendimiento*” (2009) P. 8 Colegio de Estudios Superiores de Administración. < <http://www.cesa.edu.co/Pdf/El-Cesa/33.red-de-financiacion-para-el-emprendimiento.pdf> > accessed 25 February 2016.

<sup>23</sup> Jorge Hurtado, Angélica Lizarazo, María Fernanda Meneses, Esteban Gómez, “*Reporte de la Situación del Crédito en Colombia*” (2015). Banco de la República de Colombia. P.17 < <http://www.banrep.gov.co/es/encuesta-credito-dic-2015> > accessed 25 February 2016.

and big enterprises (last six columns in the graphic) have a higher rate of credit granting, as it is showed in the graphic below. The color red represents the banks, the yellow represents the financing companies and the blue represents the cooperatives.



Source: *Reporte de la Situación del crédito en Colombia*. Banco de la Republica de Colombia P.17

Therefore, having an alternative method of financing is the solution for entrepreneurs and MIPYMES to access the resources needed in order to start and boost their business.

## 1.5. Data Analysis

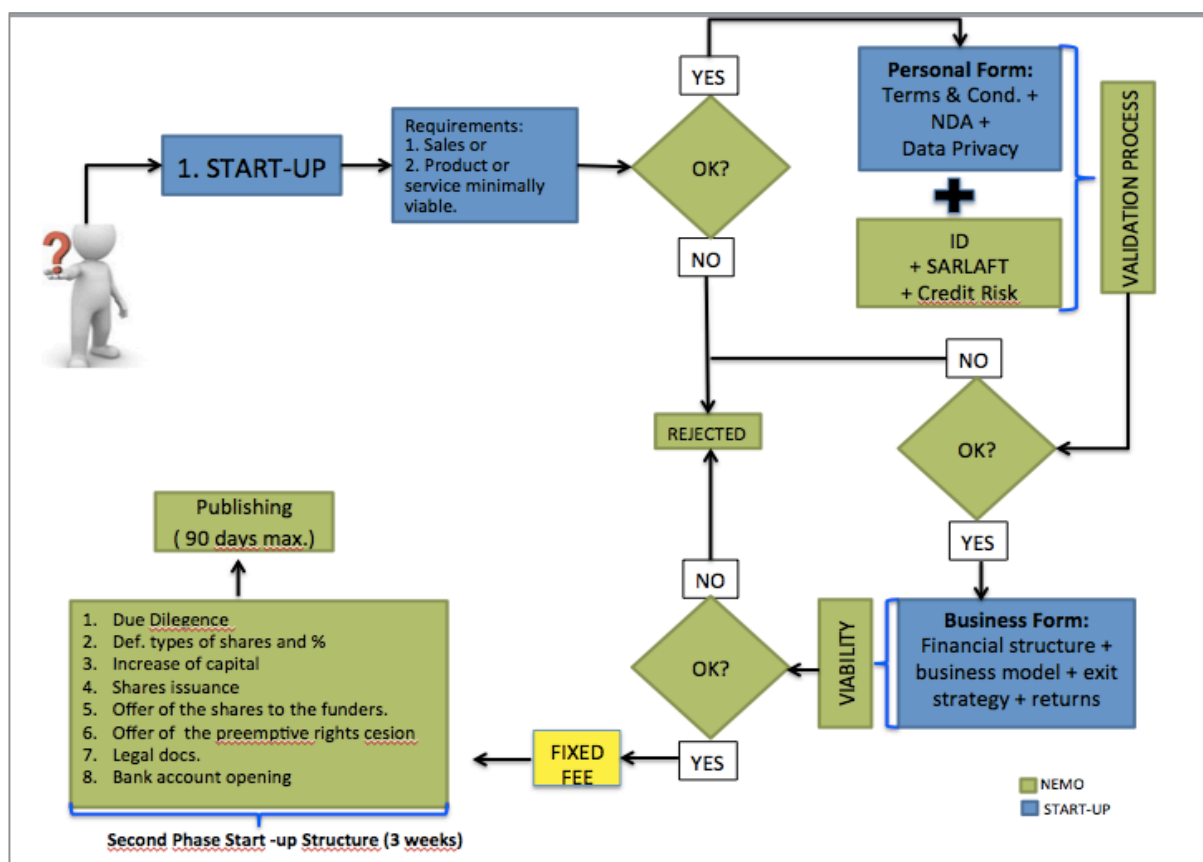
According to the data exposed is possible to conclude the following:

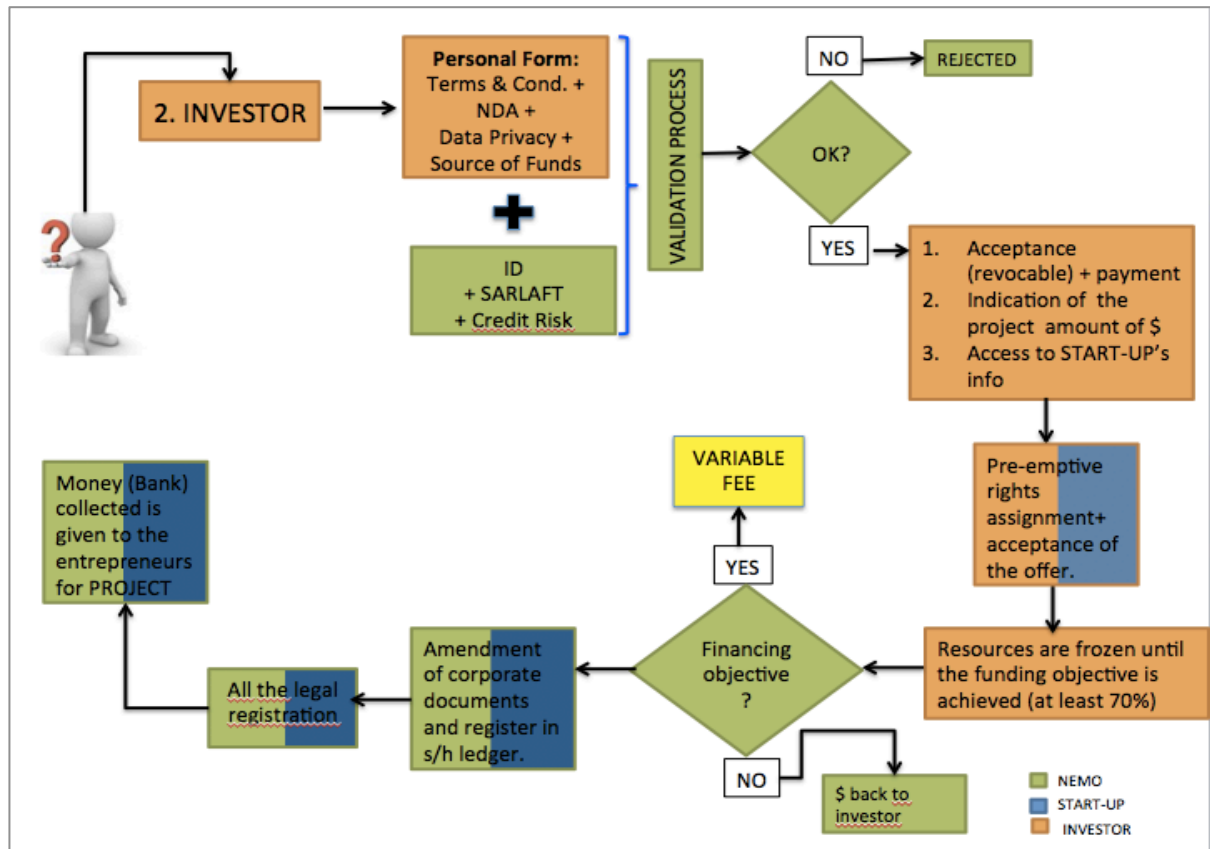
- Despite the economic growth and improvement that Colombia has presented over the last years, the education, the capacity to innovate and the financing access are barriers that need to be overcome in order to have a higher level of competitiveness that allows the country to enter to the new economies based on innovation and technology.
- Colombia's investment on research and development was in 2012 of 0.17% of the Gross Domestic Product (GDP) while Chile, Mexico and Argentina invested almost 0.5% of their GDP. Of these investments the private sector invested around 40% while other countries like Israel and South Korea invested 75%.
- Innovation, science and technology are essential to Colombia's economy growth, therefore is necessary the public sector intervention on those areas not only investing money, but also promoting the proper environment to enhance trust in the industry to diversify the traditional ways of obtaining capital including the participation of the private sector.
- Despite the different laws enacted and the programs created by the government in order to encourage innovation and business creation, not every entrepreneur has access to the resources

granted by those programs, which means that only few projects are selected and financed, reducing the possibilities for the entrepreneurship to acquire funds and grow.

- Small enterprises and microenterprises are the companies who have less access to credit while the medium and big enterprises have a higher rate of credit granting.
- Is necessary to create an alternative method of financing for entrepreneurs and MIPYMES in order to make their projects grow, overcoming all the barriers imposed by traditional credit financing institutions

## 1.6. Nemo's Business Model





Graphic made by the author.

Nemo is the first equity crowdfunding platform created in Colombia, its business model is developed through a bilateral platform in which two different types of clients who are interdependent on each other are connected.

On one hand, we will find seed stage start-ups or MIPYMES that are located initially in Bogota, Medellin, Barranquilla and Cali and that require financial resources, either because they do not have access to traditional financing methods or because the conditions offered by the financial institutions do not match their business plan and structure. Nemo is focused on start-ups that have had a process of incubation or acceleration, either in entrepreneurship centers of universities, through networks of angel investors or private incubators and also those initiatives that had participated in seed stage capital processes or contests held by the government or private institutions, but despite having reached the final stages were not selected.

On the other hand, we find the investors who are willing to acquire equity in these enterprises, if the return on investment is attractive compared to the yields of other traditional products or the project results very attractive for them.

Therefore, the platform allows the interaction of these two types of clients making possible the investment through a validation process on both ways, to assure the success of the deal. This means that Nemo is going to analyze each start-up or MIPYME before its publication online and also is going to study each investor.

In order to be a part of Nemo's published projects, the start-ups or MIPYME may comply with at least one of the following requirements:

- 1) Sales
- 2) A product or a service minimally viable.

Additionally the entrepreneurs shall present a business plan including the growth prospects, the composition of the team and shall determine the purposes for which they will use the raised money. Among the purposes accepted we will find the following:

1. To increase the work capital, either to stimulate the sales or to create new products or to enter into new markets.
2. To expand the existing capacity, whether purchasing more equipment or making improvements to the existing one.
3. Capital restructure, through debt relief.

Nemo has established certain evaluation criteria to select the viable investors; a investor could be any person or company who wants to invest at least COP500.000 (US\$137.00). However, there two types of investors in which Nemo will be focused:

- 1) Private equity funds with the purpose of creating an investors pool. The private equity funds that Nemo will approach are funds that include in their investment policies the financing of emergent enterprises like start-ups and MIPYMES.
- 2) Private investors with risk aversion with incomes higher than COP.2.000.000 (US\$667.00)

### **1.6.1. Platform**

Nemo's business model is based on a platform as a principal channel to communicate with their clients and as a main tool to execute its operations. The users will find a module with a definition of all the terms that the participants might find in the forms and they will also be able to make claims through it.



The platform is a white label platform acquired from a recognized provider in United States, it is custom made for Nemo, and therefore it contains and complies all the requirements in the United States for this type of platforms. The platform will be presented in two languages: Spanish and English and eventually an application will be developed for mobile technology. Additionally, it will include analysis, storage and data handling tools for all the corporate and contractual information of each transaction and there will be also monitoring and communications tools between the start-up and its investors after the deal is closed.

### **1.6.2. Financial Structure**

Nemo's revenues come from fixed costs in the structuring stage plus an additional fee that corresponds to a percentage of the amount raised, which is charged to the entrepreneurs only if the deal is successfully closed.

### **1.6.3. Legal Assessment**

In order to enforce the agreement that is generated between the parties within the platform Nemo will provide legal assistance in several aspects. First, the project is assessed in order to determine if is compliant with Nemo's requirements. Once the project is considered viable, the legal assessment starts with the due diligence procedure, therefore all the corporate documents of the company if it exists, are evaluated. In case there is no existing company a simplified joint-stock company (*Sociedad por Acciones Simplificada*<sup>24</sup> (S.A.S.) for its name in Spanish) will be incorporated and if the company exists under other legal form it should be transformed into a S.A.S. to make possible the whole equity acquisition process.

Next, Nemo's legal team and the entrepreneurs shall determine which type of shares will offer to the potential investors and how much percentage of the control are the entrepreneurs willing to give up in order to obtain the funding needed. If the company has shares held in reserve, which are those shares that are not subscribed yet but they are authorized and therefore, they are part of the authorized capital, the general meeting or the competent body shall issue them to bring new shareholders. In the opposite

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<sup>24</sup> Is a type of society that was created by Law 1258 of 2008. Is a capital society essentially commercial that can be constituted by contract or by unilateral act consistent of a private document? The shares and other securities issued by the S.A.S may not enroll in the National Registry of Securities and Issuers (*Registro Nacional de Valores y Emisores* "R.N.V.E" for its name in Spanish) or be traded on the stock exchange. These societies were created with the purpose of making easier the incorporation of societies and therefore stimulate the business realization.

scenario, where there are not shares held in reserve, the authorized capital should be increased by the approval of the shareholders before the whole process starts.

Subsequently, the issuance of the new shares will be offered to the incumbent shareholders (pre-emptive rights) but the negotiation of the pre-emptive rights with third parties should be permitted in the articles of association, otherwise the bylaws shall be amended.

Once the capital increase and the issuance of the shares is arranged, the entrepreneurs will offer the shares in accordance with the pre-emptive rights to the other shareholders, but the shares have not been issued yet. This offer is conditioned to a minimal objective of acceptance and subscriptions determined at the beginning of the process jointly with the entrepreneurs.

The investors who are registered in the platform and who already were accepted as such can access the start-up documents and all the legal documents required for the transaction. The investor confirms his interest by accepting to be part of the transaction, after this, the investor will require the shareholders (founders) to subscribe an assignment agreement on their pre-emptive rights through a formal offer. This offer occurs simultaneously with the acceptance of the investor.

The shareholders (founders) accept the offer immediately and the investor becomes an assignee of the pre-emptive rights, therefore the assignment agreement will be effective. Consequently, the investor will pay the right given by the assignment agreement through a bank transfer into the account controlled by the entrepreneurs. This account will be frozen until the objective is met.

Once the funding objectives are achieved, the shares will be issued and the shareholder certificates will be given to the investors, then the transaction's register will be done in the shareholders ledger. In case the initial goals regarding offers and funding are not met, the entrepreneur will give the money back to the investors.

Later, the bylaws amendment if applicable, should be made by the approval of the shareholders via an extraordinary meeting and the shareholders agreement should be signed and deposit in order to register the changes with the Chamber of Commerce according to the law.

Through the amendment of the articles of association and the shareholders agreement all the rules regarding the shares' transfer, the participation of the investors and the exit options should be agreed. However there are some basic items that need to be established:

- The entrepreneur should be willing to give collateral regarding the company's assets or her shares, in case of fraud, not allocation of the economic resources to the objective settled or contractual breaches.
- Exit of the investor, which shall not imply a significant cost for the entrepreneurs.
- Pre-emptive rights and the transferability of the shares.
- Participation in the meetings.
- Rights of information.
- Bad actor
- Tag-along rights
- Drag alone rights

## CHAPTER 2: The importance of Equity Crowdfunding in Colombia

As we mentioned before the major problem for entrepreneurs is the lack of the financing resources to make their business or ideas grow. Therefore, the entrepreneurs are forced to apply for credits granted by financial institutions and in most of the cases the applications are rejected because the entrepreneurs are not compliant with the requirements or because the credit offered is not consistent with the business model proposed by the entrepreneurs. This situation reflects the traditional institutions' closed view regarding entrepreneurship. Banks and financial companies do not comprehend that creating an innovative business takes time and therefore the revenues of the project will not come immediately, which creates an obstacle to access the resources needed.

In order to promote, entrepreneurship and innovation funding becomes an vital element, therefore Colombia and its government need to face the challenge of creating a law that regulates the participation of different categories of investors who are willing to acquire equity in these enterprises, if the return on investment is attractive compared to the yields of other products. Thus, the need to seek alternative methods of funding arises and crowdfunding seems to be the answer.

### 2.1. What is crowdfunding?

*“The concept of “crowdfunding” is related to the one of “crowdsourcing”, which refers to the outsourcing to the “crowd” of specific tasks, such as the development, evaluation or sale of a product, by way of an open call over the internet (Howe, 2008). Through online platforms, the task, traditionally performed by contractors or employees, can be undertaken by individuals for free or in exchange for some specified return, whose value is however generally lower than the one of the contribution made to the firm. Crowdsourcers may in fact have intrinsic motivations, such as the pleasure of undertaking the task or participating to a community, as well as extrinsic motivations, related to monetary rewards, career benefits, learning or dissatisfaction with the current products (Kleeman et al. 2008)”<sup>25</sup>.*

After the financial crisis in United States when entrepreneurs were not able to raise funds to finance their projects or companies, crowdfunding became an alternative method to raise money from family and friends in order to support certain businesses<sup>26</sup>. The term crowdfunding is attributed to Michael

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<sup>25</sup> Lucia Cusmano, “New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments” (2015) Organization for Economic Co-operation and Development (OECD). P, 53 < <https://www.oecd.org/cfe/smes/New-Approaches-SME-full-report.pdf> > accessed 2 April 2016.

<sup>26</sup> Crowdfunding's Potential for the Developing World. (n 4) p.8

Sullivan who launched in 2006 the platform Fundavolg (an incubator of projects linked to videoblog), which provided the possibility of online donations; perhaps because the platform did not succeed, the term became better known after the introduction of the American platform "Kickstarter"<sup>27</sup> which is the most popular platform for donation-based crowdfunding and it has channeled over US\$815 million from 4.9 million backers (29 percent of which have invested in more than one project) to nearly 50,000 projects throughout the world since 2009<sup>28</sup>.

This method is based on social, economic and technological features that make crowdfunding an accessible source of funding, therefore through crowdfunding platforms is possible to access a community or a wide range of investors that can directly support certain business or project that has caught their attention, giving them the possibility to obtain profits or benefits and for the entrepreneur to exploit and expand his business. *“Moreover, through this method the cooperation principle is emulated and technology has triggered the multiplier and efficiency of the underlying economic principle in financing mass effect: risk sharing (translation made by the Author) [Por tanto, la tecnología ha disparado el efecto multiplicador y de eficiencia del principio económico subyacente en la financiación en masa: la distribución del riesgo]”*<sup>29</sup>.

Crowdfunding has different types such as donation-based, reward-based, lending-based and equity-based, however this thesis is focused on the necessity of the last category of crowdfunding. Equity crowdfunding is defined by the Organization for Economic Co-operation and Development (OECD) as a mechanism *“whereby privately-held company offers securities to the general public, through the medium of an online platform. Investors receive a share in the business and may acquire “voting rights”*<sup>30</sup>.

Thus, equity crowdfunding creates value for two interacting groups (entrepreneurs and investors) allowing the entrepreneurs to achieve the financial goal of their businesses in order to grow and allowing any type of investor to be part of the market by becoming a shareholder in a start-up company that she chooses, changing therefore, the traditional model of financing. This alternative method of financing has several advantages that will be exposed in the next section.

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<sup>27</sup> Daniela Catastraro, “A social History of the Crowdfunding” (2011) < <http://socialmediaweek.org/blog/2011/12/a-social-history-of-crowdfunding/> > accessed 4 April 2016.

<sup>28</sup> Crowdfunding’s Potential for the Developing World. (n 4) p.8

<sup>29</sup> Teresa Rodríguez de las Heras Ballell, “El Crowdfunding como Mecanismo Alternativo para la Financiación de Proyectos”, Universidad Carlos III de Madrid, Revista de Derecho Empresarial. San José, Costa Rica. No.1. Págs. 121-140. ISSN 2215-373X, p. 123 < <http://www.redemcr.org/contenido/el-crowdfunding-como-mecanismo-alternativo-de-financiacion-de-proyectos/> > accessed 15 March 2016.

<sup>30</sup> New Approaches to SME and Entrepreneurship Financing (n 25) P. 54

## 2.2. Benefits of Equity Crowdfunding

As it was mentioned before one of the greatest benefits of equity crowdfunding is that changes the traditional methods of financing new business, opening the door to growth based on innovation and using the internet as the main tool of development. Through this method the investors will get the opportunity to become owners of a business in the proportion established by the entrepreneurs or at least will allow investors to obtain dividends from the business they decided to support.

It is important to mention that crowdfunding as a mechanism to obtain financial resources is been used more frequently in developed countries such as United States, United Kingdom and Europe than in developing countries, however *“developing economies have the potential to drive growth by employing crowdfunding to leapfrog the traditional capital market structures and financial regulatory regimes of the developed world”*<sup>31</sup> and therefore being able to have all of the following benefits<sup>32</sup>:

- Use internet as a tool to finance entrepreneurship: Taking into account that internet has become the most important way to connect people from all over the world, using internet to develop platforms in order to support innovative ideas changes completely the traditional capital market system, making the effort to search for resources more efficient and simple.
- Crowdfunding is beneficial for investors: avoiding the traditional capital markets, investors can be able to connect with a project or several ones and therefore they will be able to diversify their portfolios without investing big amounts of money. As was explained before equity crowdfunding allows investors to be part of a company, becoming shareholders with all the correspondent rights and obligations.
- Helps the financial cycle of the start-ups: as noted previously early stage funding comes in most of cases from savings, family or friends because getting access to traditional financing is not feasible and looking for angels or venture capitalists is difficult at this stage, therefore, crowdfunding platforms and social networks become an useful method to promote and get exposure. *“Validation from other investors may lower the perceived risk, and possibly the actual risk, of early-stage investment. However, crowdfunding does not displace the role of the angel or VC in providing later-stage or larger-scale funding”*<sup>33</sup>.
- Promotion, market testing and exposure: through crowdfunding platforms is possible for the entrepreneurs to see how the public reacts to their products or projects, therefore if the

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<sup>31</sup> Crowdfunding's Potential for the Developing World. (n 4). P. 9

<sup>32</sup> Ibidem. P. 26

<sup>33</sup> Ibidem, p. 26.

proposal is accepted by different investors, the platforms can be used as an indicator of the quality of the project and therefore encourage other investors to invest.

- Expansion of the geographic market: as crowdfunding is developed through Internet, investors from all over the world can choose to support any product or project. *“Governments may consider the benefits of remittance dollars flowing through crowdfunding platforms, which provide a digital footprint of the money flows. These digital footprints can help governments understand more about the financial health and level of commitment to their country among members of the country’s diaspora. Crowdfunding platforms can identify the current country of residence of a funder, the types of companies/entrepreneurs that diaspora investors are funding and the level of commitments from those funders”*<sup>34</sup>.
- Crowdfunding can generate innovation, potential growth and job creation. A recent study<sup>35</sup> made by Crowdfunding Capital Advisors (hereinafter “CCA”) surveyed several hundred companies in the North America, Europe and Africa that had completed successful rewards, debt or equity-based crowdfunding campaigns from June 2012 to June 2013 and the results showed that 39% of firms who had success with equity or debt based crowdfunding hired new employees. These firms hired an average of 2.2 new employees, in total, 87% of firms either had, or intended to, hire new employees as a direct result of having raised equity or debt financing via crowdfunding<sup>36</sup>.
- *“The emergence of crowdfunding as a mechanism for financial mediation — ushered in thanks to the needs of the market, to innovation and the regulatory space — represents a disruptive element in a scenario where traditional banking was used to being practically unchallenged”*<sup>37</sup>. Therefore, traditional financing institutions may create new methods in order to adequate their structure to the new demands of this new economy, this will end up in more competitive credit products that will be beneficial for entrepreneurs. Furthermore, the traditional financial market can expand its reach by creating several alliances with crowdfunding platforms through consumer loans destined to entrepreneurs or investors, changing the score assessment and thus allowing more access to resources for participants<sup>38</sup>.

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<sup>34</sup> Ibidem, p. 35.

<sup>35</sup> Crowdfunding Capital Advisors, *“How does crowdfunding impact job creation, company revenue and professional investors interest?”*. <<https://crowdfundingpr.files.wordpress.com/2014/01/how-does-crowdfunding-impact-job-creation-and-company-revenue.pdf>> accessed 4 March 2016.

<sup>36</sup> Ibidem. P. 8.

<sup>37</sup> Carmen Cuesta, Santiago Fernandez de Liz, Irene Roibas, Ana Rubio, Macarena Ruesta, David Tuesta, Pablo Urbiola, *“Crowdfunding in 360°: Alternative Financing for the Digital Era”*. (2015) BBVA Research. Digital Economy Watch. P. 20. <[https://www.bbvaresearch.com/wp-content/uploads/2015/02/Crowdfunding\\_Watch1.pdf](https://www.bbvaresearch.com/wp-content/uploads/2015/02/Crowdfunding_Watch1.pdf)> accessed 4 March 2016.

<sup>38</sup> Ibid.

### 2.3. Risks of Equity Crowdfunding

Like any other investment, equity crowdfunding involves risks for investors, especially considering that all the transactions are conducted via Internet. As we mention previously, one of the main advantages of equity crowdfunding is that any investor (accredited or not) is able to expand his portfolio, so the equity crowdfunding is becoming a way to democratize investment market.

However, the most common risk presented is the business failure, “(...) *publicly available data from the developed world shows that up to 50 percent of start-ups fail within five years*”<sup>39</sup>. Therefore is very important that investors have all the information required in order to make the investment decision, hence platforms play a very important role preventing this risk. They can avoid this problem disclosing all the information possible in order to guide the potential investors to invest in the published projects and it may be very helpful to non-accredited investors to have the proper education that can be provided by the platforms<sup>40</sup>.

Another risk that can be presented during the use of platforms is fraud, however until now the number of fraud committed is very rare according with the World Bank<sup>41</sup> and it would require the intention to deceive the public through the creation of fake platforms, for this reason regulation of these new methods of investment becomes important in order to protect the investors.

An additional way of committing fraud could be through the creation of false projects, so “entrepreneurs” could access the money given by the investors, however this would require a minimal or non-participation at all of the platform choosing the projects published, meaning not having any control at all of the project which is never the case because most of the platforms intervene in the selection process actively because their reputation is on the line as well<sup>42</sup>.

Finally, money laundering can occur, as with any other type of investment in which shares are traded, to prevent this risk crowdfunding platforms must comply with the relevant legislation in order to prevent its use as a mechanism to escape the law<sup>43</sup>.

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<sup>39</sup> Crowdfunding's Potential for the Developing World. (n 4) P. 45

<sup>40</sup> Ibid., P. 45

<sup>41</sup> Ibid., P 47

<sup>42</sup> Ibid., P 45

<sup>43</sup> Ibid., p. 45-47.



## **2.4. How can Nemo prevent equity crowdfunding risks and which is Nemo's added value?**

Nemo is aware of all the risks that are presented in the crowdfunding industry; therefore it has established certain procedures to prevent those risks.

Business failure is a risk that does not actually depend on Nemo or any other equity platform because the success or failure of a start-up depends on the quality of its products or services and also on the commitment that the entrepreneurs put into the promotion and development of their business. Then, what can platforms do to prevent this risk? As we mentioned in Section 2.3., the platforms perform an important role informing the potential investor with material information for them to make informed decisions.

Nemo in the first place, makes legal and financial due diligence of each start-up in order to assure the accuracy and transparency of the information provided to the potential investors. Once the due diligence results are ready and if they are in accordance with the requirements demanded by Nemo the project can be published. This means that Nemo is involved in the selection process of each project studying its structure in order to protect the investors from fraudulent business or losses.

However, there are different external factors that can influence the success or failure of the entrepreneurs and these are not connected with the platform's performance, which is why Nemo established a policy in its procedures regarding the restitution of the raised money to investors in case the start-up does not reach the goals set.

In addition, Nemo's business model establishes a procedure to protect investors through the provision of collateral either on the shares of the company or on the assets thereof, obviously in favor of the investors. If required by the investors and agreed by the founder to register a warrant on the shares, a warranty contract will be signed according to Law 1676 of 2013. Afterwards, Nemo will keep track on the warranties given, if applicable.

Additionally, taking into account that any type of investor (experienced or not) can use crowdfunding as means to diversify his portfolio, Nemo provides to those investors who are not experts on the financial markets a module of financial education and a capital risk tutorial. This is a way to give the potential investors information regarding the market and how the investment will work.

Nemo is prepared to prevent fraud through several practices such as the validation process of the entrepreneurs and investors assuring the identification and profile of the participants of each transaction. This process is completed with the consultancy of government's public databases that include criminal, disciplinary and fiscal record. In addition, Nemo will use products that to verify the identity of the applicants and they will be consulted on DataCredito (credit score database) for which the users must signed an authorization in accordance with the Law 1266 of 2008 and 1581 of 2012.

Finally, in order to prevent money laundering Nemo will consult restricted lists as OFAC in in order and will report to the authorities if necessary. Furthermore, the investors are required to fill and sign a source of funds declaration in which they will announce where their resources came from to make the investment.

#### **2.4.1. What is Nemo's added value?**

Nemo performs certain activities that are essential to differentiate it from its competitors in Colombia's crowdfunding market. The most important activities are:

- a. Validation and verification of all users.
- b. Structure of the projects: this includes due diligence, financial structure, drafting all the documents required for the transaction between the start-up and the investors.
- c. Maintenance and operation of the platform.
- d. Financial education to the users of the platform.
- e. Promoting and marketing online for the projects published in the platform.
- f. Identification of key participants like institutional investors, start-ups with a high potential of innovation and growth.

On the other hand, Nemo's CEO considers that the relationship with clients is the most important value that they can offer to the market. Therefore, Nemo has established two pillars when creating relationships with its customers.

1. Personalized assistance inside the platform: a) to the entrepreneurs, giving them all the support needed during the structure of their projects in order to be launched; b) to the non-experienced investors giving them the educational background needed to invest.
2. Trust: Create trust in the crowdfunding ecosystem through Nemo's policies of transparency, compliance and information provision, which enables the participants to believe in the use of these schemes will allow them to achieve their goals. Making feel the entrepreneurs that Nemo is an ally in their projects is essential to make the difference they have as purpose.

When Nemo chooses a project to be published in its platform, is how Nemo shows to its customers that the company is taking a risk as well, but it relies on the project and on all the benefits that it can have for the market, the entrepreneurs and the investors. Nemo is sure that once the platform is operating and the funded projects begin to be profitable, the market trust will grow and more investors will be attracted to this type of investment.

In addition Nemo has two major benefits:

1. Provides to start-ups and MIPYMES an alternative method to access capital with supplementary products and services that are not available in a traditional financial market, such as legal and financial assessment, in the structure of the business and marketing of their ideas. Additionally, investors will also benefit from this extra services, since they will have educational aid if needed, they will be able to diversify their portfolios investing small amount of money and they will receive profits.
2. Costs reduction: This is given by managing transactions on the platform and direct contact between the start-up and investors. Moreover legal and financial proper structure is very expensive or unattainable for both entrepreneurs and investors. Therefore, Nemo included the financial and legal assessment in its business model that will reflect the best practices in the market regarding mergers and acquisitions and will benefit the entrepreneurs giving them direct access to expert advice and a very low cost. The costs are also reduced in terms of the issuance and placement of the securities as such.

Finally, Nemo's CEO considers that eventually Nemo will generate strategic alliances with different entities from the government and private sector, which will also attract more investors and will increase the market.

Notwithstanding, having a lot of benefits as we mentioned before crowdfunding can also represent some risks as any other investment. Nonetheless, the benefits are greater than the risks, taking into account that this alternative method of financing gives entrepreneurs the opportunity to start their business and overcome their main obstacle in an early stage (lack of resources). Therefore, if entrepreneurship is not stagnated, great and innovative ideas can become real and have an impact in the labor and productive sector. Thus, entrepreneurs will be able to compete in new markets, making the economy of the country grow.

## **CHAPTER 3: Main Legal Barriers for Equity Crowdfunding Platforms in Colombia**

Colombia has no equity crowdfunding platforms at the moment; there are only donation-based platforms. The main obstacles for the creation of the former are the legal restrictions of the stock market and the financial system, and the absence of regulation to these new financing methods. Therefore our case study: Nemo, the first equity platform in Colombia will allow us to assess the legal context of the country and the possibilities for the platform to function.

In order to describe the existing restrictions in Colombia's legal system is important to explain how the majority of equity crowdfunding platforms work. In this type of transactions we will find a triangular relationship between the entrepreneur or start-up, the investors and the platform<sup>44</sup>. Hence, in the first place the start-up or entrepreneur must choose the platform to work with and apply to be published. Then, the platform is in charge of selecting certain projects that are compliant with the platform's requirements, for which the start-up would have to provide all the necessary information regarding the business in order to make the due diligence needed<sup>45</sup>.

Once the entrepreneur's project is chosen he would have to give to the platform all the financial information, the necessary approvals (board of directors or shareholders) and the business plan so that investors can make an informed decision regarding the project. When the investors have made up their minds about the investment, the platform may study the investors to determine if they are qualified to make the investment. After the evaluation process is finished, the investors will provide the money directly to the platform or to the escrow agent selected and previously informed by the platform<sup>46</sup>.

If the period established to raise money is completed and the goals set are achieved, the platform orders to the escrow agent to pay the money to the entrepreneur and the escrow agent gives to the investors the share certificates according to their investments. With this procedure investors become shareholders of the business they sponsored initially. Afterwards, the role of the platform is to promote to the same investors different projects that may interest them.

Now that we exposed the operation of these platforms, in order to analyze if equity platforms operation and its establishment is viable in Colombia, we will analyze what the financial system

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<sup>44</sup> El Crowdfunding como Mecanismo Alternativo para la Financiación de Proyectos (n 29) P 128.

<sup>45</sup> Oscar A Jofre Jr., *"Equity Crowdfunding 101 Guía Mundial Hacia la Revolución Financiera"* (2015) Kore conX P. 18

<sup>46</sup> Ibid., p 18-23

considers as a public offering (Decree 2555 of 2010), the concept of value (Law 964 of 2005), of financial intermediation, of massive and illegal fundraising (Decree 1981 of 1988) which could limit the creation of this type of portals.

### 3.1. What is a public offer in Colombia?

First, we need to understand the concept of offer established in the Colombian legislation. Article 845<sup>47</sup> of the Commercial Code defines the offer as the proposal made by one person to another in order to make a contract or business, which shall contain certain essential elements and shall be communicated to the offer's recipient. The offer has been communicated to the latter when any adequate means is used with that purpose.

According to Article 6.1.1.1.1. of Decree 2555 of 2010<sup>48</sup> an offer is considered public when it meets the following conditions:

- The offer is aimed to undetermined individuals or is aimed to a hundred determined people.
- It aims the subscription, sale or acquisition of securities issued in series or in mass entitling their holders either credit rights, participation rights or certificates representing goods

On the other hand, a private offer (article 6.1.1.1.1. Decree 2555 of 2010) is consider as such when:

- The offer is aimed to less than a hundred determined people.
- The offer of shares or bonds that are mandatorily convertible into shares is aimed to the shareholders of the issuer provided they are less than 500 recipients thereof.
- The offer of shares resulting from a capitalization order given by a competent authority, directed exclusively to shareholders of the issuer, or which is aimed at capitalizing obligations

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<sup>47</sup> Artículo 845 del Código de Comercio: La oferta o propuesta, esto es, el proyecto de negocio jurídico que una persona formule a otra, deberá contener los elementos esenciales del negocio y ser comunicada al destinatario. Se entenderá que la propuesta ha sido comunicada cuando se utilice cualquier medio adecuado para hacerla conocer del destinatario.

<sup>48</sup> Artículo 6.1.1.1.1 (Art. 1.2.1.1. Resolución 400 de 1995). Definición de oferta publica. Se considera como oferta pública de valores, aquella que se dirija a personas no determinadas o a cien o más personas determinadas, con el fin de suscribir, enajenar o adquirir documentos emitidos en serie o en masa, que otorguen a sus titulares derechos de crédito, de participación y de tradición o representativos de mercancías. No se considerará pública la oferta de acciones o de bonos obligatoriamente convertibles en acciones que esté dirigida a los accionistas de la sociedad emisora, siempre que sean menos de quinientos (500) los destinatarios de la misma. Tampoco se entenderá como pública la oferta de acciones resultante de una orden de capitalización impartida por autoridad estatal competente, dirigida exclusivamente a accionistas de la sociedad, o la que tenga por objeto capitalizar obligaciones de la misma, siempre y cuando se encuentren reconocidas dentro de un proceso concursal en el que se haya tomado tal decisión, en ambos casos sin importar el número de personas a quienes se encuentre dirigida. Las ofertas que a la vez tengan por destinatarios a las personas indicadas en el inciso segundo de este artículo y a cien o más personas determinadas serán públicas. Parágrafo. Cuando los destinatarios de una oferta se vayan a determinar con base en una labor de premercadeo realizada entre personas no determinadas o cien o más personas determinadas, la respectiva oferta tendrá el carácter de pública y en tal sentido, su realización sólo podrá efectuarse con observancia de las normas que al efecto se establecen en este decreto.

thereof, provided that they are recognized within a reorganization process in which has taken such a decision. In both cases, regardless of the number of people to whom the offer is directed.

- Increases of authorized capital of domestic public services enterprises when is necessary to make new investments in their infrastructure and up to the value that such rules. In this case, the company can make the offer of the new shares to the users who will be beneficiaries of the investment and they will have to pay the price in installments simultaneously with the service bills, without applying the public offer procedures and regulation.

### 3.1.1. Public Offer Procedure

In order to make a public offer of securities the issuer has to be registered with the Securities and Issuers National Register (*Registro Nacional de Valores y Emisores* hereinafter “RNVR” for its name in Spanish) and if the issuer has the intention of making the offer in the public market, it has to be register with Colombia Stock Exchange (*Bolsa de Valores de Colombia* hereinafter “BVC” for its name in Spanish).

According with Decree 3780 de 2007 the public offer can be completed by the book building system which “*is a mechanism applied internationally to perform a premarketing task of the securities that are going to be publicly offered. It is to probe the intention of the investors interested in titles, as well as price and quantity they would be willing to acquire (translation made by the Author) [Mecanismo aplicado internacionalmente para realizar una labor de premercadeo sobre títulos valores que se ofrecerán públicamente. Consiste en sondear la intención de los inversionistas interesados en los títulos, así como el precio y cantidad que estarían dispuestos a adquirir]*.”<sup>49</sup>. This system has 3 stages: 1) after the offer is presented with the Financial Superintendence of Colombia (*Superintendencia Financiera de Colombia*, hereinafter “SFC” for its name in Spanish) and before having its authorization, the issuer can promote the securities; 2) once the authorization is ready the period for building the book starts, this period is when the issuer receives offers from investors to acquire securities and the offers must be compliant with the requirements set by the issuer in the initial prospectus and 3) the book shall have a daily record of the offers that have been presented including the quantity of the securities and the price offered.

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<sup>49</sup> Superintendencia Financiera de Colombia. < <https://www.superfinanciera.gov.co/SFCant/Glosario/glosario-b.htm#BOOK BUILDING> > accessed 20 April 2016

### 3.1.2. Private Offer procedure

Regarding this type of offer we will find the general authorization scheme, which approves the regulation for the subscription of ordinary shares for those firms who are under the exclusive control and surveillance of the SFC and whose offers meet the following requirements:

- The number of shares to be placed is equal to or less than twenty percent (20%) of outstanding shares.
- The placement of the shares is done according to the pre-emptive rights.
- That the regulation for the subscription of ordinary shares is done in compliance with all the regulation regarding the issuance of shares.
- That the rights of the bondholders that are mandatorily convertible into shares are been protected if applicable.

In compliance with all the regulation the legal representative and the public auditor shall send all the documentation required by the Circular 005 of 2005 to the SFC 10 business days prior the expire date of the offer.

On the other hand, if the conditions mentioned previously are not met, the specific authorization scheme is required, therefore is mandatory to obtain the authorization of the SFC in order to make the private offer.

### 3.2. What is considered a security in Colombia?

Pursuant to Article 2<sup>50</sup> of Law 964 of 2005 a security is defined as any right that is negotiable according to its nature and that is part of one issuance of securities, when it has as its object or as its effect the raise of money from the public.

Therefore a security to be considered as such, according to the Colombian law, requires the following:

1. Be issued to raise money from the public or to work as an investment product.

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<sup>50</sup> Artículo 2 Ley 964 de 2005: Para efectos de la presente ley será valor todo derecho de naturaleza negociable que haga parte de una emisión, cuando tenga por objeto o efecto la captación de recursos del público, incluyendo los siguientes: a) Las acciones; b) Los bonos; c) Los papeles comerciales; d) Los certificados de depósito de mercancías; e) Cualquier título o derecho resultante de un proceso de titularización; f) Cualquier título representativo de capital de riesgo; g) Los certificados de depósito a término; h) Las aceptaciones bancarias; i) Las cédulas hipotecarias; j) Cualquier título de deuda pública.

2. Being essentially negotiable and transferable unless the pre-emptive rights are statute.

Consequently, the following are securities according to Article 2 of the Law 964 of 2005:

- Shares.
- Bonds
- Commercial papers
- Certificates of goods' deposit
- Any title to or resulting from a securitization process
- Any representative title or certificate of venture capital
- Certificates of deposit
- Bank acceptances
- Mortgage bonds
- Any government bond.

### 3.3. Massive and Regular Fundraising

In order to protect investors and their trust in the financial markets, the government of Colombia forbids to raise money from the public freely without the authorization of the SFC, otherwise there will be administrative and criminal sanctions.

Pursuant Article 1 of the Decree 1981 of 1988<sup>51</sup> a person or entity is considered to be capturing or raising money from the public when:

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<sup>51</sup> Artículo 1° Para los efectos del Decreto 2920 de 1982, se entiende que una persona natural o jurídica capta dineros del público en forma masiva y habitual en uno cualquiera de los siguientes casos: "1. Cuando su pasivo para con el público está compuesto por obligaciones con más de veinte (20) personas o por más de cincuenta (50) obligaciones, en cualquiera de los dos casos contraídas directamente o a través de interpuesta persona. "Por pasivo para con el público se entiende el monto de las obligaciones contraídas por haber recibido dinero a título de mutuo o a cualquiera otro en que no se prevea como contraprestación el suministro de bienes o servicios. "2. Cuando, conjunta o separadamente, haya celebrado en un período de tres (3) meses consecutivos más de veinte (20) contratos de mandato con el objeto de administrar dineros de sus mandantes bajo la modalidad de libre administración o para invertirlos en títulos o valores a juicio del mandatario, o haya vendido títulos de crédito o de inversión con la obligación para el comprador de transferirle la propiedad de títulos de la misma especie, a la vista o en un plazo convenido, y contra reembolso de un precio. "Para determinar el período de los tres (3) meses a que se refiere el inciso anterior, podrá tenerse como fecha inicial la que corresponda a cualquiera de los contratos de mandato o de las operaciones de venta. "Parágrafo 1. En cualquiera de los casos señalados debe concurrir además una de las siguientes condiciones: "a) Que el valor total de los dineros recibidos por el conjunto de las operaciones indicadas sobrepase el 50% del patrimonio líquido de aquella persona; o "b) Que las operaciones respectivas hayan sido el resultado de haber realizado ofertas públicas o privadas a personas innominadas, o de haber utilizado cualquier otro sistema con efectos idénticos o similares. "Parágrafo 2. No quedarán comprendidos dentro de los cómputos a que se refiere el presente artículo las operaciones realizadas con el cónyuge o los parientes hasta el 4° grado de consanguinidad, 2° de afinidad y único civil, o con los socios o asociados que, teniendo previamente esta calidad en la respectiva sociedad o asociación durante un período de seis (6) meses consecutivos, posean individualmente una participación en el capital de la misma sociedad o asociación superior al cinco por ciento (5%) de dicho capital. "Tampoco se computarán las operaciones realizadas con las instituciones financieras definidas por el artículo 24 del Decreto 2920 de 1982"



1. The money is raised from third parties that are not involved with the collector;
2. The money raised come from loans, agency agreements or any other contract without any obligation on the collector to provide any consideration because of the money received;
3. The liability of the collector consists in obligations to more than 20 people or more than 50 obligations acquired directly or through an intermediary, or when in a period of 3 consecutive months the collector closed more than 20 agency agreements in order to manage money under the form of “self-administration” or to buy bonds or securities according to the agent’s opinion.
4. The operation through which the funds are raised exceed 50% of the liquid assets of the collector (net equity) or the respective transactions have been the result of performing public or private offerings to undetermined people.

Furthermore, all the entities and activities under the inspection, surveillance and control of the SFC are defined in the Decree 663 of 1993 (Organic Statute of the Financial System) and in Law 964 of 2005, therefore these entities are legally authorized to raise money from the public in a massive and regular manner<sup>52</sup> which means that the administrative authorization is required in order to perform this activities. The authorized entities are: Credit institutions, financial services companies and insurance companies.

Therefore, fundraising massively and regularly is considered an activity of public interest in Colombia and “*can only be performed by who have been previously authorized by the State, who shall verify the responsibility and the creditworthiness of those seeking to develop it. Indeed, we must point out that the conduct of business operations cannot engage activities that correspond exclusively to companies that are subject to supervision by the Superintendence, including credit institutions, who by law are expressly authorized for the massive and regular fundraising from the public or insurance companies or insurance intermediaries, in relation to the activities constituting the corporate purpose (translation made by the Author) [... éstas sólo pueden ser realizadas por quienes hayan sido autorizados previamente por el Estado, quien deberá cerciorarse satisfactoriamente del carácter, responsabilidad y solvencia de quienes pretendan desarrollarlas. En efecto, es menester precisar que en la realización de operaciones empresariales y/o comerciales no pueden involucrarse actividades que correspondan exclusivamente a las sociedades que son objeto de supervisión por parte de esta Superintendencia, entre ellos, los establecimientos de crédito, quienes por ley se encuentran*

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<sup>52</sup> Superintendencia Financiera de Colombia. “Captación Masiva y Habitual, Actividad Desarrollada Previa Autorización del Estado” (1994) Concepto 93063173-5. <  
<https://webcache.googleusercontent.com/search?q=cache:86Y0XZSbazgJ:https://www.superfinanciera.gov.co/SFCant/Normativa/doctrinas1994-8/93063173.doc+&cd=1&hl=es-419&ct=clnk&gl=nl> > accessed 20 April 2016.

*expresamente autorizadas para la captación masiva y habitual de dineros del público, o las compañías de seguros o intermediarios de seguros, en relación con las actividades que conforman su objeto social.]”.*<sup>53</sup>

### 3.4. Financial Intermediation

The SFC has defined this term as the activity that involves professional fundraising from the public means passive operations (receiving deposits) in order to place the resources in active operations or lending money, which requires prior authorization and therefore can exclusively be done by entities that are entitled to and that are under the surveillance of such Superintendence<sup>54</sup>.

The financial intermediation is presented when certain transactions have as purpose or as effect approaching the buyer and sellers on the trading systems on their own account or on behalf of third parties in order to<sup>55</sup>:

1. Purchase or sell securities registered with RNVE; buy or sell securities according to agreed agency contract. These transactions can only be done by stockbrokers, independent brokers or brokers that trade agroindustry products.
2. Brokerage transactions. The stockbrokers are defined in the Article 7 of the Law 45 of 1990.
3. Purchase or sell securities according to an escrow agreement, which do not lead to the involvement of the trustee in a collective portfolio managed by the trust fund. These operations can only be done by trust funds.
4. Purchase or sell securities through stockbroker firms according to Article 9 of the Decree 2175 of 2007, which manage collective portfolios in order to obtain joint profits.
5. Purchase or sell securities through pension funds and insurance companies who manage joint portfolios and are regulated by the Decree 2175 of 2007.
6. The placement of securities, guaranteed securities. Stockbrokers, independent securities brokers and financial corporations can carry out these operations. Also by banking institutions, financial corporations and stockbrokers that may act as market makers placing public debt securities issued by the Nation, that may or may not guarantee placement of all or part of such emissions, or taking all or part of the issue to place at your own risk.

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<sup>53</sup> Superintendencia Financiera de Colombia, “Intermediación Financiera, Financiación de Préstamos con Recursos Propios” (2008) Concepto 2008033390-001 <  
<https://www.superfinanciera.gov.co/SFCant/Normativa/Conceptos2008/2008033390.pdf>> accessed 20 April 2016.

<sup>54</sup> Ibid.

<sup>55</sup> Ministerio de Hacienda y Crédito Público. Superintendencia Financiera de Colombia “*Qué es una actividad de intermediación de valores? ¿En qué se deben invertir los excedentes de liquidez de las entidades públicas?*” P.4 <  
<https://www.superfinanciera.gov.co/SFCant/ComunicadosyPublicaciones/cartillamercados.pdf>> accessed 20 April 2016.

7. The purchase and sale of securities executed by its own and directly by the affiliated to a system of trading or to a securities transaction registration system.

According to Colombian law, financial intermediaries are the stockbrokers, the independent brokers, the credit institutions, management companies of collective portfolios and stockbroker of agricultural products and other commodities. In addition, the public entities that according with their legal regime can perform operations on securities directly through trading systems and are not subject to inspection and surveillance of the SFC.

### **3.5. How can Nemo work under the existing regulation?**

As was mentioned before, one of the main obstacles that Nemo had had to deal with is the lack of regulation regarding crowdfunding and the restrictions imposed by the financial system and the stock market regulations.

Nemo has been structured in a way that allows its operation within the exiting legal system through the negotiation of the pre-emptive rights in the issuance of new shares through assignment agreements. Therefore, Nemo is not doing public offerings, its activities do not involve regular and massive fundraising, it does not need to be under the surveillance and control of the SFC; it does not constitute activities of financial intermediation and therefore it does not require governmental authorizations based on the following arguments:

#### **3.5.1. Nemo does not participate in public offerings.**

The transaction made within Nemo's platform is not a public offering of securities since entrepreneur's main purpose using the platform is to offer his/her pre-emptive rights by an assignment agreement that eventually would be sign with the investors. Thus, the offer's object is not to subscribe, to sell or to acquire shares but the main object is to offer an assignment agreement of the pre-emptive rights to subscribe the shares that eventually will be issued if the funding goals are meet. Consequently, when the investor offers to the entrepreneurs the subscription of the assignment agreement on the pre-emptive rights, there is no public offering of shares but merely an offer to sign a contract.

Therefore, the transactions made within Nemo's platform do not give the investors credit rights, participation rights nor certificates representative of goods, the operation gives to the investors only a

right to subscribe an assignment agreement for potential shares negotiating the pre-emptive rights given to the initial shareholders in the bylaws.

In any case, Nemo will make sure that the offers made by the investors to the entrepreneurs in each project do not exceed the threshold of 99 people allowed by the law (Article 6.1.1.1.1. of Decree 2555 of 2010) in order to prevent any risk of being considered a public offer of securities.

However, there are two main risks to be considered:

1. Although the pre-emptive rights have not been defined as a security according to Law 964 (Article 2), it could be possible that under a forced interpretation the assignment agreement of the pre-emptive rights could be considered as such by its effect. Because once the assignment agreement is signed, the investor will subrogate on the rights of shareholder assignor regarding the start-up's shares that will be issued if the goals are met. Thus the assignment agreement of the pre-emptive rights could be considered a title or a certificate of venture capital, which is a security according to the law by its effect because the investors will acquire shares of the start-up at the end of the whole process.

On the other hand, under the legality principle in the Colombian legislation a prohibition can only be considered as such if it is stipulated unequivocally in the law. Consequently, offering assignment agreements of the pre-emptive rights of a start-up is not clearly forbidden by Colombian regulation and is not a security according to the law; therefore Nemo is not breaching the law.

2. Nemo's business model can be considered fraudulent due to the evasion of all the regulation of public offerings, such as not having the authorization of the SFC and therefore not being registered with RNVE. As a consequence, all the transactions that are performed through the platform may be declared ineffective<sup>56</sup>, which means that every transaction would lack effects, so is necessary to take back all acts performed as a result of the public offering in relation to each one of the investors who signed the contracts.

Under these circumstances, the business transaction offered through Nemo's platform is not a public offer considering the following reasons:

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<sup>56</sup> Article 10 Law 32 of 1979.

1. The purpose of the offer is not to subscribe a share acquisition contract nor purchase or sale shares. The main purpose of the offer is to offer an assignment agreement of the pre-emptive rights of the incumbent shareholders (founders).
2. The object of the offer does not correspond to documents or titles that have been issued in mass, in fact the object of the offer would be the right to sign the assignment agreement of the pre-emptive rights to acquire shares that have not been issued yet.
3. The platform offers the right to sign the assignment agreement of the pre-emptive rights of the start-up, not the shares of the company. Thus, the investors will not receive debt titles or certificates representing goods, they will just receive the right to sign the assignment agreement.

Consequently, the offer made through Nemo's platform is a private offer. For this reason is not necessary to have authorization of the SFC according to Article 5.2.1.1.1. of Decree 2555 of 2010, nor being register with RNVE.

### **3.5.2. Nemo does not raise money from the public regularly and massively**

First, as was explain previously in Section 1.6.3., investors will pay the right given by the assignment agreement through bank transfer to the account controlled by the entrepreneur, therefore the financial resources are never entering into Nemo's bank accounts or are never transferred through the portal.

Second, Nemo does not perform activities under agency agreements or intermediation to manage the raised money. Nemo perform its activities under a service provision contract signed with the entrepreneurs.

Third, Nemo does not manage the amounts invested and the condition that requires the collector not to give any consideration to the investors for the amounts received is not applicable, because the investors will receive the right to sign the assignment agreement of the pre-emptive rights and will become shareholders of the company after completing successfully the whole legal and financial process.

Regarding this matter, the SFC has stated<sup>57</sup> that when a the consideration in a transaction is the provision of a service or a good, regular and massive fundraising does not take place according to Article 1 of Decree 1981 of 1988.

*"In this sense, evaluated the above conditions against the case that is specifically under study, this office finds that taking into account the hypothesis of your inquiry is based on the fact that there is a prepayment of goods or services, such a situation would be a consideration (although future) for the money received by the natural or legal person in question, so that such activity would not be subject to the supervision of the Superintendence. However, in case the aforementioned consideration is not provided that is, when the monthly contribution do not materialize at the end of the term with the provision of a good or service to the contributor, but the money received is returned to the contributor, a loan agreement would be formed, whether in return of payment or free of charge, in which case the transaction would be found within the situation referred to in paragraph 2 of paragraph 1 recorded on the sheet 2 of this concept, thus constituting what Decree 1981 of 1988 calls 'liabilities to the public' (translation made by the Author) ["En este orden de ideas, evaluadas las anteriores condiciones frente al caso que es concretamente objeto de estudio, este despacho encuentra que como quiera que la hipótesis de su consulta se fundamenta en el hecho de que se están prepagando bienes o servicios, tal situación haría que se presente una contraprestación (aunque futura) por los dineros que en su oportunidad recibiera la persona natural o jurídica que nos ocupa, de suerte tal que dicha actividad no se encontraría sujeta a la vigilancia de esta Superintendencia. "Sin embargo, en el caso de no brindarse la contraprestación antes aludida, esto es, cuando el aporte mensual no se concrete al final del plazo en el suministro de un bien o servicio al aportante, sino que se restituya el dinero recibido, se configuraría el contrato de mutuo, ya sea este oneroso o gratuito -según se reconozcan o no intereses sobre la suma captada-, caso en el cual la operación consultada se ubicaría dentro de la situación prevista en el inciso 2º del numeral 1 consignado en la hoja 2 del presente concepto, constituyendo así lo que el Decreto 1981 de 1988 denomina 'pasivo para con el público] "*

In conclusion, Nemo does not perform activities of massive and regular fundraising because of these key aspects: 1) the money paid by the investors is transferred into the entrepreneur's bank account, thus Nemo does not receive nor have any control of that money; 2) Nemo does not perform activities under agency agreements or intermediation to manage the raised money; 3) the investors who support the projects published on Nemo's platform will receive, if the whole transaction is successful, the

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<sup>57</sup> Superintendencia Financiera de Colombia. "Captación Masiva y Habitual –Configuración y Normativa –Medidas Cautelares" (2007). Concepto 2006068741-001 < <https://www.superfinanciera.gov.co/SFCant/Normativa/Conceptos2007/2006068741.pdf> > accessed 12 May 2016.

shares in a company through an assignment agreement, therefore they will receive a future consideration; 4) There is no entrepreneur's liability according to the law.

### **3.5.3. Nemo's activities do not constitute financial intermediation**

The SFC has defined the financial intermediation as an exclusive activity of the entities supervised by this organization. This activity is understood as professional fundraising from the public by conducting passive operations or receiving funds in order to place them, also in a plural manner, through the execution of active operations or lending money (loans), activities that because of their nature require prior administrative authorization<sup>58</sup>.

Moreover, it is been said by the same entity<sup>59</sup>, that the financial intermediation is an industry that requires strict regulation, so that is not possible to create undertakings freely to perform it, especially for being a service of public interest that requires administrative authorization given by the State. For this reason this activity can only be performed by the entities under inspection, surveillance and control of the SFC following the parameters set by Articles 90 and 92 of Law 45 of 1990.

Considering the definition of this activity, one of the characteristics of the financial intermediation is the link between raising funds from the public and placing them to third parties<sup>60</sup>, therefore we conclude that Nemo's business model does not include the performance of activities that constitute either massive or regular fundraising or financial intermediation because Nemo does not raise money or place money to its participants.

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<sup>58</sup> Intermediación Financiera (n 53)

<sup>59</sup> Superintendencia Financiera de Colombia “*Intermediación Financiera*” (2000) Concepto No. 2000048692-1 < <https://www.superfinanciera.gov.co/jsp/loader.jsf?lServicio=Publicaciones&lTipo=publicaciones&lFuncion=loadContenidoPublicacion&id=18542&dPrint=1> > accessed 12 May 2016.

<sup>60</sup> Superintendencia Financiera de Colombia “*Captación Masiva y Habitual*” (2002). Concepto 200202222-1 < <https://www.superfinanciera.gov.co/jsp/loader.jsf?lServicio=Publicaciones&lTipo=publicaciones&lFuncion=loadContenidoPublicacion&id=18706&dPrint=1> > accessed 12 May 2016.

## **CHAPTER 4: Equity Crowdfunding around the World and legal framework for Colombia**

Equity crowdfunding is increasingly growing among entrepreneurs as an alternative way to raise money in order to fill the existing funding gap when they resort to traditional financing systems. Consequently the venture capital cycle has included a new type of founders that can be reached through Internet platforms in order to raise the resources needed. Investors, then become crucial in this structure and as was said before, crowdfunding is a new way to democratize the investment markets, allowing any person, either accredited or not, to be part of the system and to obtain profits.

In order to prevent the information asymmetry and the uncertainty involved in this type of transactions, some countries have developed a regulatory framework containing the necessary rules for this mechanism to function properly, providing transparency, trust and protection to investors and at the same time promoting entrepreneurship.

What follows is a description of the main requirements that equity platforms shall comply according to the legislation in some countries. First we are going to mention the United States case with the Jumpstart Our Business Startups Act which has been the role model for many other countries; second we will study Italy, which was the first European example regarding the regulation and third we will assess the Spanish case, which is the latest regulation approved in Europe which could be useful for the Colombian future regulation and we will conclude with a comparative table regarding the main provision of each country and some suggestions for the future regulation in Colombia.

### **4.1. United States: JOBS ACT**

Title III of the Jumpstart Our Business Startups Act (hereinafter “JOBS Act”) was approved by the Securities and Exchange Commission (hereinafter “SEC”) on the 30 of October 2015, with the aim of providing to the non-accredited investors with the opportunity to invest in start-up companies, which are in a initial stage and are looking for capital in order to make their businesses grow.

The Title III of JOBS Act establishes a certain number of requirements as follow<sup>61</sup>:

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<sup>61</sup> Securities Exchange Commission, “SEC Adopts Rules to Permit Crowdfunding Proposes Amendments to Existing Rules to Facilitate Intrastate and Regional Securities Offerings” (2015) < <https://www.sec.gov/news/pressrelease/2015-249.html> > accessed 5 May 2016.



1. The issue of the shares must be done through a broker or through a platform that is registered with SEC on new Form Funding Portal, and become a member of a national securities association (currently, FINRA).
2. The money raising is limited up to 1 million dollars within a period of 12 months.
3. The numbers of securities bought by an investor over a period of 12 months is limited up to: I) USD \$2,000 or 5% of their annual income or net worth; II) 10% of their annual income or net worth up to USD\$100,000 for those investors whose income is higher than the amount thereof.
4. Prohibits an intermediary's (broker or platform) directors, officers or partners (or any person occupying a similar status or performing a similar function) from having any financial interest in an issuer using its services.
5. Requires that an intermediary have a reasonable basis for believing that an issuer seeking to offer and sell securities in reliance on Section 4(a)(6) through the intermediary's platform complies with the requirements in Securities Act Section 4A(b) and the related requirements in Regulation Crowdfunding, to prevent fraud.
6. Make information that a company is required to disclose available to the public on its platform throughout the offering period and for a minimum of 21 days before any security may be sold in the offering.
7. Provide communication channels to permit discussions about offerings on the platform.
8. Provide disclosure to investors about the compensation the intermediary receives.
9. Accept an investment commitment from an investor only after that investor has opened an account.
10. Have a reasonable basis for believing an investor complies with the investment limitations.
11. Provide investors notices once they have made investment commitments and confirmations at or before completion of a transaction;
12. Comply with maintenance and transmission of funds requirements; and
13. Comply with completion, cancellation and reconfirmation of offerings requirements.
14. The rules also would prohibit intermediaries from engaging in certain activities, such as: i) Providing access to their platforms to companies that they have a reasonable basis to believe that they have the potential for fraud or other investor protection concerns; ii) Having a financial interest in a company that is offering or selling securities on its platform unless the intermediary receives the financial interest as compensation for the services and receives the same equity as the public did; iii) Compensating any person for providing the intermediary with personally identifiable information of any investor or potential investor.

This title of the JOBS ACT has been considered for many as the opening door for non-accredited investors to be part of the market by giving them protection and by providing them with certainty. However it has also a lot of critics due to the limits regarding the investments and the burdens imposed to the portals such as the background check, revising if there are any investors with potential to commit fraud, the written policies regarding almost every aspect of the platform, the prohibition for platforms to accept equity compensation unless certain requirements are met, the disclosure of intermediaries' compensation and the implementation of educational tools, among others. The obligations assigned to the platforms create a lot of liability for them<sup>62</sup>.

In addition, Section 201I of the JOBS Act adds a new paragraph (b) to Section 4 of the Securities Act. Section 4(b) of the Securities Act created an exemption for platforms that offer, sale or solicit securities in accordance with Rule 506 of Regulation D will not require the registration as broker or dealer unless, the platform receives compensation for the sale or purchase of the securities, holds the customer funds or securities in connection with the purchase or sale of such security or is associated with the statutory disqualification as defined in section 3(a)(39) thereof. This exemption has been said not to be very functional for platforms because of the non-compensation requirement, taking into account that the exemption is not very clear, so any compensation as a carried-interest would make the exemption non applicable<sup>63</sup>.

#### **4.2. Italy: Crescita Bis Decree (D.L 221/2012)**

Italy is the first European country that regulated the equity crowdfunding as a mechanism to raise money from the public. In 2012 the Crescita Bis Decree was passed and its main objective was to promote the economy's development and the digital culture and it considered research and technological innovation as key factors economic enrichment, cultural and civil progress of the country<sup>64</sup>.

Then, in June of 2013 the regulation No. 18592 was approved and adopted by the *Commissione Nazionale per le Società e la Borsa* (CONSOB for its name in Italian). This regulation set the legal

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<sup>62</sup> David Pricco, "Sec's New Jobs Act Title Iii Crowdfunding Rules: Overview And First Thoughts" (2015) crowdexpert.com, < [http://crowdexpert.com/articles/new\\_jobs\\_act\\_titleiii\\_rules\\_overview\\_first\\_thoughts/](http://crowdexpert.com/articles/new_jobs_act_titleiii_rules_overview_first_thoughts/) > accessed 22 May 2016, Ryan M Feit, "Final Title III Crowdfunding Rules: Five Major Developments" (2015) crowdfundinsider.com < <http://www.crowdfundinsider.com/2015/11/76664-final-title-iii-crowdfunding-rules-five-major-developments/> > accessed 22 May 2016, Seedinvest.com, "Equity Crowdfunding Rules: The Good, The Bad & The Ugly, < <https://www.seedinvest.com/blog/jobs-act/equity-crowdfunding-rules-good-bad-ugly-part-ii> > accessed 22 May 2016.

<sup>63</sup> Mark Roderik, "Why the Jobs Act Broker-Dealer Exception Doesn't Matter (Much)" (2015) [CrowdfundAttny.com](https://crowdfundattny.com), < <https://crowdfundattny.com/2015/03/02/why-the-jobs-act-broker-dealer-exception-doesnt-matter-much/> > accessed 12 May 2016.

<sup>64</sup> Art. 1 L.221/2012

framework for platforms to operate, for start-ups to be part of the entrepreneurial ecosystem and the issuance of equity through the use of platforms.

The following aspects are considered essential in order to analyze the requirements of platforms according to the Italian regulation:

1. The start-up must be qualified as a “*start-up innovative*” which requires meeting these conditions:
  - a. The company shall be incorporated as a limited liability company (S.P.A., S.A.P.A., srl), therefore partnerships are excluded from this concept. The Italian legislation considers this type of corporate structure the most adequate due to its autonomy.
  - b. The company shall be incorporated in Italy and must operate there.
  - c. The *start-up innovative* must have as its principal corporate purpose, the development, production and marketing of innovative products or services with high technological value.
  - d. The *start-up innovative*, to be such, must be established and perform business activity by no more than 48 months.
  - e. The *start-up innovative* cannot be formed through extraordinary transactions, such as mergers, spin-off and sales of companies or business units.
  - f. The owners of the *start-up innovative* can be natural persons or undertakings.
  - g. The latest balance sheet approved of the *start-up innovative* within six months of the financial year, may not exceed 5 million Euros.
  - h. The *start-up innovative* cannot distribute dividends. The idea of the legislator is that the profits should be used to capitalize the company or to make investments in R & D, thus promoting the growth of start-ups.
  - i. “Meet at least one of the following alternate requirements:
    - *The costs allocated to research and development must be equal to or higher than 20 per cent of the higher value between (i) the company’s production costs and (ii) the company’s production value;*
    - *At least one-third of its work force shall be represented by individuals having a PHD or carrying out a PHD or having a degree and having completed a research programme of three years at public or private research entities in Italy or abroad; or*
    - *The start up shall be the owner or assignee, or have applied for the registration with the relevant authorities, of an industrial property right (eg, a patent) related*

*to its core business*”<sup>65</sup>.

2. The platform shall be registered with CONSOB.
3. Any investor, either retail or professional, is free to invest without any limit.
4. Two thresholds have been set: I) for individuals 500 Euros per investment and 1.000 Euros annually and II) for undertakings 5.000 Euros per transaction and 10.000 Euros annually.
5. In each transaction 5% of the investors must be accredited or professional.
6. If the transaction does not exceed 5 million Euros is not necessary to have an issue prospectus.
7. *“If the managers of the platform are banks or investment funds, they must comply with MiFID regulations and will only have to report their intention to manage the platform”*<sup>66</sup>.
8. If any other type of firm manages the platform, is required to have CONSOB’s authorization and the issue should be handled by a professional broker.

The main two weaknesses that this regulation presents are<sup>67</sup>:

- 1) That is only applicable to the start-ups that are effectively compliant with the definition of start-up innovative, which could lead to a reduction of the market, because it means that only start-up that have a technological purpose are considered as such, therefore the purpose of increasing and promoting Italian’s economy’s growth through funding small companies is reduced.
- 2) 5% of the investors in each transaction shall be an accredited or professional investor, which also can interrupt the conclusion of the deal.

#### **4.3. Spain: Law 5 of 2015**

On the 27 of April of 2015 the Law 5 of 2015 was approved with the objective of making more flexible the financing process for SME and make a progress in the development of alternative methods of financing establishing the proper regulation<sup>68</sup>.

The Participative Financing Platforms (*Plataformas de Financiación Paticipativa*, hereinafter PFP for its name in Spanish) are defined according to Article 46 of Law as the authorized companies whose activities involve contacting, in a professional manner and through web sites or other electronic means

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<sup>65</sup> Antonia Verna, Luca Gambini “The New Regulation on ‘Innovative’ Start Ups In Italy” (2013) portolano.it, June 1 of 2013. < <http://www.portolano.it/2013/06/the-new-regulation-on-innovative-start-ups-in-italy-2/> > accessed 12 May 2016.

<sup>66</sup> Crowdfunding in 360 (n 37) P. 17

<sup>67</sup> Antonia Verna, “Brief Overview on the New Italian Crowdfunding Regulation” < [http://www.portolano.it/pcc\\_newsletters\\_corp/brief-overview-on-the-new-italian-crowdfunding-regulation/](http://www.portolano.it/pcc_newsletters_corp/brief-overview-on-the-new-italian-crowdfunding-regulation/) > accessed 12 May 2016.

<sup>68</sup> Preamble, Law 5/2015.

to a plurality of individuals or legal entities offering funding in exchange for a monetary profit, called investors and individual or legal undertakings applying for funding on its own behalf to finance a participative project, called promoters.

The requirements to function as a PFP established by Law are the following:

1. The platform cannot perform transactions involving donations, the sale of goods or services nor loans without interests, it need to have its registered office and its effective administration and management, in national territory or in another Member state of the European Union, it has to be constitution of a Limited Liability Company or S.L.
2. Is required to have, during its operation, at least 60.000 Euros as capital entirely paid in cash, a professional insurance with a coverage of 300.000 euros.
3. They need to be authorized and registered with National Stock Market Commission (*Comisión Nacional del Mercado de Valores*, hereinafter C.N.M.V. for its name in Spanish).
4. The maximum amount of fundraising for project through each of the platforms may not exceed 2.000.000 Euros, being possible to carry out successive rounds of financing that do not exceed that amount on a yearly basis. When the projects are directed exclusively to accredited investors, the maximum amount can reach 5.000.000 Euros.
5. PFP will make sure that non-accredited investors will invest more than 3.000 Euros in one project or more than 10.000 Euros in one year on the same platform.
6. PFP are allowed to perform the following activities: a) Receipt, selection and publication of participatory projects funding; b) Development, establishment and operation of communication channels facilitating the funds raising between investors and promoters.
7. PFP may provide ancillary services such as: a) The advice to promoters in connection with the publication of the project including the provision of services and advice in the areas of IT, marketing, advertising and design; b) Analysis of the projects determining the risk involved in each project for the investors and the determination of any other variables that could be useful for the investors to make the informed decision of investment. The publication, classification and grouping of such information in objective terms, without making personalized recommendations shall not constitute financial advice; c) Enabling remote communication channels for users, investors and promoters to contact directly with each other before, during or after activities that lead to project financing; d) the provision of contract templates that could be signed by the parties; e) the transmission to the investors of the information provided by the promoter on the evolution of the project, as well as the most relevant corporate events; f) the judicial and extrajudicial claims of credit rights, acting in representation of investors or on their own behalf if investors assigned him their credit rights.

8. The platforms are not allowed to perform activities exclusively reserved to financial entities such as providing loans to the investors or promoters; Assure the fundraising to the investors; Make individual recommendation to investors; Provide mechanisms that allow automatic investment to the non-accredited investors unaccredited to automate their investment decisions, whether or not based on criteria prefixed by the investor.
9. Have a good administrative and accounting procedures or adequate internal control.
10. To have adequate means to ensure the security, confidentiality, reliability and the service provided by electronic means.
11. Having an internal code of conduct that includes, in particular, potential conflicts of interest and the terms of participation of administrators, directors, employees and agents in applications for funding are implemented through the platform.
12. Provide mechanisms so that in case of cessation of activity are followed paying all or part of the services that pledged for projects participatory funding had obtained funding

This regulation is following the JOBS Act as a model and is remarkable that is limiting its scope to equity crowdfunding and lending-based crowdfunding, leaving aside the donations or the purchase of good or services. Is important to mention as well that besides having as an objective the promotion of entrepreneurial funding, it has also as main concern the protection of the non-accredited investors, therefore it establishes some measures to assure the transparency and trust in this new marketplace like requiring platforms to have a minimal capital and insurance to guarantee its liquidity, however this measures can also difficult the creation and function of these platforms due the burdens imposed.

In order to summarize what was exposed we created this comparative graphic taking into account the most important requirements set by each country to the equity platforms:

Requirements	United States of America	Italy	Spain
<b>Corporate structure</b>	Intermediary that acts as broker or dealer (provided the exemption) or a funding platform	The company shall be incorporated as a limited liability companies (S.P.A., S.A.P.A., srl	Limited Liability Company or S.L.
<b>Register</b>	With SEC on new Form Funding Portal, and shall become a member of a national securities	With CONSOB ( <i>Commissione Nazionale per le Società de la Borsa</i> )	With C.N.M.V ( <i>Comisión Nacional del Mercado de Valores</i> )

	association (currently, FINRA)		
<b>Money raising Limit</b>	Up to \$1.000.000 dollars	The public offer does not exceed 5.000.000 euros	2.000.000 euros or 5.000.000 if the offer is directed to accredited investors
<b>Investor's investing limit</b>	USD \$2,000 or 5% of their annual income or net worth; II) 10% of their annual income or net worth up to USD \$100.000 for those investors whose income is higher than the amount thereof	For individuals 500 to 1.000 euros per project or annually respectively; For legal undertakings 5.000 to 10.000 euros per project or annually respectively	3.000 euros in one project or more than 10.000 euros in one year on the same platform

#### 4.4. Colombia's challenges regarding Crowdfunding regulation

The challenges creating viable and functioning regulation for crowdfunding in Colombia are noteworthy. The major challenge is to generate trust in this new financing method. To achieve this is required to modify the existing regulation and create a new one in order to allow the start-ups and MIPYMES to be funded using the crowdfunding platforms. Therefore, we would like to suggest some changes to the current regulation in order to open the possibility for crowdfunding, especially for equity crowdfunding:

First, is necessary to change the Article 4 of Law 1258 of 2008, allowing the S.A.S. (*Sociedades por Acciones Simplificadas*) to register their shares with RNVE or any other entity, so they can be issued and traded through equity crowdfunding platforms. Although the prohibition of registering shares and trade them on the stock market was created because of the size of the companies that are constituted under this legal form and the idea of facilitating formalization of small businesses making simpler the compliance with corporate standards and law, this prohibition prevents S.A.S. to grow and acquire funding through the listing of its shares on the stock exchange.

As a consequence of this change investors would be able to fund projects and receive equity of the supported company directly from the issuer. However it is important to consider that this entails the

creation of a secondary market for this type of shares<sup>69</sup>, which requires an specific regulation, giving the investors in crowdfunding platforms the possibility to negotiate them in the market, otherwise the investor would have to exit the investment through a share purchase agreement or an assignment contract.

Second, it is necessary to amend the Decree 1981 of 1988 for the equity crowdfunding platforms not to be considered as regular and massive fundraisers, allowing them to raise money from the public in order to support entrepreneurship. Since raising money from the public, according to Colombia's Constitution is an activity of public interest, there must be a regime that protects investors, that is why today we find all the restrictions regarding the stock and financial market. However, in order to make the regulation and the system more open and according to reality it is important to create an exception that permits crowdfunding portals to raise money from the public establishing certain limits and prohibitions such as amounts raised per project, the proscription of granting loans to the investors or entrepreneurs (which are activities reserved to financial entities) and not to manage directly the money raised.

The participation of a trust fund or an escrow agent in this process could be considered as well, as mechanism to protect the investors, because these entities are professional managers previously authorized by the government to function as such, therefore its participation means an investment fund could create trust in the crowdfunding operations and would prevent the platforms to be considered as regular and massive fundraisers or financial intermediaries. Another advantage of using the trust fund is that they could help the platform to prevent money laundry with all the procedures they already had established by these financial entities.

Third, Article 6.1.1.1. of Decree 2555 of 2010 should be modified in order to create an exception that allows equity platforms to offer the start-up or MIPYMES' shares to more than 99 undetermined people and not to fall within the concept of public offering of securities, considering that this funding method is developed through Internet and it has enormous scope, which matches the idea of matching democratization the investments, allowing any person to be part of the projects published.

Finally, as described in the previous sections United States, Italy and Spain have set a precedent for the crowdfunding regulation; hence some of the issues set forth in these legislations can be used as a guideline to establish the regulation in Colombia.

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<sup>69</sup> Ivan Rodríguez, "La necesidad de Regular el Crowdfunding en Colombia" (2014) Diario La República July 7, < [http://www.larepublica.co/la-necesidad-de-regular-el-crowdfunding-en-colombia\\_142026](http://www.larepublica.co/la-necesidad-de-regular-el-crowdfunding-en-colombia_142026) > accessed 15 January 2016.



We can start with the limitation of the amount that can be raised for each project during a period of 12 months, setting up a threshold for the platforms. We believe this measure is beneficial to investors because it allows to control some of the risks presented during the investment in start-ups and MIPYMES.

With this idea of protecting the investors most of regulators established also a limited amount of investment according to the investors' income, especially for non-accredited investors. However we consider that this measure is not necessary since equity crowdfunding as any other investments involves risks that evidently shall be informed to the investors and they should have them clear before making the investment decision, thus what should be establish in the future regulation is the platforms' obligation to disclose all the material and essential information of the projects to the investors. Therefore, in our opinion setting up a maximum ceiling for investors is a measure that does not protect them but it does create a limit on their chances of obtaining yields in large quantities.

The disclosure of information to investors is a very delicate issue that shall be addressed in the most explicit way in order to prevent misrepresentations. We consider Spanish regulation very precise regarding this matter and therefore platforms should disclose information such as the operation of the platform, the risks involved in each transaction like the loss or the lack of liquidity of the investment, the possibility of not receiving dividends, the applicable fees, procedures to solve claims and requests. Having the disclosure rule established would enhance the investors' trust regarding the investment decision and would allow them to choose in an informed way.

In order to protect investors, which is main concern when dealing with equity crowdfunding, platforms could be required to register with Financial Superintendence of Colombia or other entity, so to as have control of the activities performed and to promote investors' trust in this new mechanism. This registration is contemplated in every regulation and Colombia should not be the exception, taking into account that is a constitutional mandate to protect investors, therefore the surveillance and control of these platforms is a way to provide that protection and prevent fraud.

Another important issue to consider is the responsibility of the platforms. Are they performing obligations to achieve results (*obligaciones de resultado*) or are they acting according to their best efforts (*obligaciones de medio*)? In our opinion the platforms are performing obligations according to their best efforts, therefore following the Colombian regulation regarding liability the burden of proof would be on the plaintiff, meaning he would have to demonstrate the negligence of the platform that

caused him damages. However, in order to protect the investors, the start-ups and MIPYMES should be accountable to their sponsors for the information provided through the platform.

To conclude this chapter we would like to mention that the main problem when creating this regulation is that the government cannot fall in excesses, setting up procedures, which ultimately would prevent the creation and operation of these platforms due to the inability of meeting the requirements requested, and forgetting the convenience and effectiveness of the mechanism. Therefore, it is important that the government takes into account the views and opinions of the participants that would be benefited with the implementation of this new method, so the equity crowdfunding can be a reality in Colombia.

## CONCLUSION

The purpose of this thesis is giving the readers an overview of Colombians legal framework in order to analyze if the equity crowdfunding platforms are viable within the country's reality. Entrepreneurship plays an important role in countries' economies all around the world. However, in developing countries like Colombia, poverty, unemployment and low education levels are drivers that motivate citizens to create different mechanisms to acquire capital. Therefore, in this context citizens are called to be creative and to innovative in order to survive in a non-patronizing state with high levels of inequality and corruption to improve the economy's indicators.

During the creative process, entrepreneurs face several obstacles preventing the start or expansion of their ideas. Access to traditional financing methods, is undoubtedly the most important barrier that entrepreneurs have to deal with when doing business, either because entrepreneurs are not compliant with the requirements requested by the financial institutions or because the credits offered are not adjusted to their business plans. Therefore, having an alternative funding method like crowdfunding becomes crucial to the entrepreneurial ecosystem and its cycle, facilitating and fostering the creation of innovative business models that enable the competition in different markets.

Despite the success that crowdfunding has had around the world, Colombia is still behind on this subject, since there is no regulation that can protect the parties involved in each transaction. This problem becomes more evident when equity crowdfunding appears into the playground, because the existing regulation *per se* prevents the creation and function of these type of portals. Therefore, our case study, Nemo, is the perfect example of how an equity platform can operate in the country, bearing always in mind that there is a possibility that Nemo may be declared illegal for performing public offerings of securities without the previous authorization of the SFC.

As we explained in chapter 3, we consider Nemo's legal structure an adequate form to operate while the regulation changes. Under the existing regulation, this structure attempts to overcome the main legal obstacles for equity platforms to be established in Colombia. The key aspects of Nemo's legal structure can be summarized as follows:

1) No public offering of securities: According to Colombian law, equity crowdfunding is considered in every case a public offering of securities; therefore every platform shall be registered with RNVE and authorized by the SFC. However, Nemo is not involved in public offering of securities since the object of the transaction made within the portal is the offering of the shareholder's (entrepreneurs) pre-

emptive rights of the shares that would be issued if the funding goals are met. Thus, the investors will subrogate in the shareholders position of the new shares through an assignment agreement. Consequently, the transaction's object is not to subscribe, to sell or to acquire shares but the main object is to offer an assignment agreement of the pre-emptive rights to subscribe shares that eventually will be issued in case the funding goals are met.

2) No massive and regular fundraising from the public: Article 1 of the Decree 1981 of 1988 establishes the concept of massive and regular fundraising from the public, which is an activity that can only be performed by financial entities that are previously authorized, otherwise this activity is penalized with prison and fines according to Article 316 of the Penal Code. Therefore, in Colombia equity crowdfunding platforms may fall within this conduct's definition if all the conditions set thereof are met. Nevertheless, Nemo is not performing this activity because a) the money paid by the investors is transferred into the entrepreneur's bank account, thus Nemo does not receive directly nor has any control of that money; b) Nemo does not perform activities under agency agreements or intermediation to manage the money raised; c) the investors who support the projects published on Nemo's platform will receive, if the whole transaction successfully meets the goals set, the shares in a company through an assignment agreement, therefore they will receive a future consideration; d) The entrepreneur has no liability.

Regarding the massive and regular fundraising, is important to mention that illegality would be circumvented when a mechanism such as a trust fund or an escrow agent is used as an instrument to raise the money, because the money would not enter into the coffers of the platform but would be deposited in the fund or account created specifically for the project. Therefore, the money will only be disbursed to the start-up if the requirements of the escrow agreement are met. This scheme has a lot of benefits because it gives more confidence to the operations made in the platforms and is also useful to prevent fraud. As a remarkable example of a trust fund used in Colombia to raise money we can find the construction the skyscraper BD Bacata, which has been qualified as the biggest campaign of "real state crowdfunding" in the world collecting 190 million dollars<sup>70</sup>. Thus, having an ancillary mechanism to raise money like a trust fund from the public would bring more trust to the operations and it would prevent the platforms from doing this activity, which is forbidden unless is duly authorized.

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<sup>70</sup> Nelson Doria, "El Crowdfunding es la forma de Financiación e Inversión del Futuro" (2016) Revista Dinero. < <http://www.portafolio.co/negocios/empresas/crowdfunding-forma-financiacion-e-inversion-futuro-495849> > 22 May 2016.

3) No financial intermediaries: Equity crowdfunding platforms are considered financial intermediaries according to the Colombian Law, which means that can only be performed by the entities duly authorized. This activity involves professional fundraising from the public through passive operations (receiving deposits) in order to place the resources in active operations (lending money), which requires prior authorization by the government for being an activity of public interest. Nemo does not perform any of those activities within its business model, so it cannot be qualified as a financial intermediary. However Nemo, as any other crowdfunding platform is an “*electronic intermediary of accessibility, visibility and credibility*”. The crowdfunding platforms main function is to bring together two groups of people providing accessibility to the participants in order to achieve their objectives (i.e., resource for entrepreneurs and return for investors). In addition the platforms provide visibility, and become a good way to promote entrepreneurs’ businesses and marketing them with a role of credibility that is generated due to the asymmetry of information. Therefore, platforms create procedures to enhance investors’ trust.<sup>71</sup>.

As was pointed out before, there is a legal stability risk involved in Nemo’s establishment under Colombian regulation. Although Nemo’s legal structure would allow it to operate, the structure set up can be dismantled by a forced and strict interpretation of the law that considers that the negotiation of the pre-emptive rights through an assignment agreement is a security or a certificate of venture capital by its effect, because of the subrogation involved that will give him shares at the end of the process. Therefore, if any competent authority determines that Nemo is performing activities that constitute public offering of securities (either because of the mechanism used or because it exceeds the threshold allowed by Article 6.1.1.1.1. of Decree 2555 of 2010), Nemo’s founders would be committing an offence by not having the previous required authorization and all the transactions made throughout the platform would be ineffective.

Overall, everything that has been explained strengthens the idea that not having any regulation regarding crowdfunding in Colombia clearly affects the entrepreneurial cycle preventing start-ups and MIPYMES from obtaining the resources needed from different and dynamic mechanisms than the traditional ones. The lack of financial resources interrupts the emergence of new companies with high growth potential and competitiveness, which certainly has an impact in Colombia’s indicators concerning innovation and technology.

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<sup>71</sup> El Crowdfunding como Mecanismo Alternativo para la Financiación de Proyectos (n 29) P 132

The interruption of the entrepreneurial cycle is the reason why in section 4.4. we suggested some changes in the regulation and the introduction of some topics in order to make possible the equity crowdfunding to operate in Colombia. The main changes suggested to make the platforms legal are:

- Changing Article 4 of Law 1258 of 2008, allowing the S.A.S. to register their shares with RNVE or any other entity, so can be issued and traded through equity crowdfunding platforms. However, the consequence of this change involves the creation of a secondary market for these shares<sup>72</sup> in order facilitate the exit of the investment.
- Amendment of the Decree 1981 of 1988 for the equity crowdfunding platforms not to be considered as regular and massive fundraisers, allowing them to raise money from the public in order to support entrepreneurship. Establishing certain limits and prohibitions such as amounts raised per project, the proscription of granting loans to the investors or entrepreneurs (which are activities reserved to financial entities) and not to directly manage the money raised.
- The participation of a trust fund or an escrow agent in this process could also be considered as mechanism to protect the investors, because these entities are professional managers previously authorized by the government.
- Article 6.1.1.1.1. of Decree 2555 of 2010 should be modified in order to create an exception that allows equity platforms to offer the start-up or MIPYMES' shares to more than 99 undetermined people and not to fall within the concept of public offering of securities.
- Taking into consideration the regulation of equity crowdfunding in other countries, we conclude that having some of the parameters set forth in these regulations can be useful for the implementation of a new regime: a) a limitation of the amount that can be raised for each project during a period of 12 months, setting up a threshold for the platforms; b) the disclosure of the projects' information in order to prevent misrepresentations, such as the operation of the platform, the risks involved in each transaction (like the loss or the lack of liquidity of the investment), the possibility of not receiving dividends, the applicable fees, procedures to solve claims and requests; c) registration with a control entity that in the Colombian case could be the SFC; d) accountability of the entrepreneurs to the investors and the liability of the platforms, which should be performed according to their best efforts.

Returning to the question posed at the beginning of this thesis, it is now possible to state that equity crowdfunding definitely is required in Colombia in order to motivate entrepreneurs' growth providing

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<sup>72</sup> Ivan Rodriguez, "Ley española de Crowdfunding, Esperanza Colombiana" (2014) Diario la República. < [http://www.larepublica.co/ley-esp%C3%B1ola-de-crowdfunding-esperanza-colombiana\\_195196](http://www.larepublica.co/ley-esp%C3%B1ola-de-crowdfunding-esperanza-colombiana_195196) > accessed 12 May 2016.

them with an alternative funding method to overcome the major difficulty they have to face, the lack of resources. However, for equity crowdfunding to be viable, it is necessary that the government intervenes in the creation and promotion of a complete legal framework that generates trust in the system, and also matches the simplicity and efficiency concept with which crowdfunding was created

Unless the Colombian government adopts the challenge of creating a regulation that allows the operation of these mechanisms, entrepreneurship and innovation will continue to stagnate, meaning the country and its companies would not be able to compete in more sophisticated markets, which consequently affects the economy's growth.

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