



**RIGA  
GRADUATE  
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LAW**

# **Real estate crowdfunding: potential in Latvia**

## **MASTER'S THESIS**

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**DECLARATION OF HONOUR:**

I declare that this thesis is my own work, and that all references to, or quotations from, the work of others are fully and correctly cited.

(Signed) .....

RIGA, 2017

## **SUMMARY**

The title of the thesis is “Real estate crowdfunding: potential in Latvia”. The length of thesis is 66 pages, including five figures, two graphs and eight tables drawn up by the author. The thesis consists of 4 chapters as well as subchapters. The purpose of this thesis is to investigate the effects of Latvian regulator approach on real estate crowdfunding services. The case study of three real estate crowdfunding platforms from the Baltics serves as an evaluation of the sector development in Latvia and Estonia.

In the first chapter of the thesis there will be the history and development of crowdfunding described, explaining the different forms and models how crowdfunding is managed. This will be followed by an overview of the crowdfunding’s volume and future trends, as well as legislation status in the world.

The second chapter will begin with a practical description about the real estate crowdfunding model, indicating participating parties and their actions. Further, the risks related to real estate crowdfunding will be highlighted to gain insight of possible interest of protection in the legislation.

The third chapter will analyse the three real estate crowdfunding platforms currently active in the Baltics, describing their formation and crowdfunding business model. A thorough research will be done on the funded loans during the year 2017.

The fourth chapter will be dedicated to analysing the legal and regulative approach on real estate crowdfunding in Latvia and Estonia, comparing national (current and proposed) regulations in this field and addressing potential issues on blocking further real estate crowdfunding’s expansion.

Finally, the author will present his conclusions on real estate crowdfunding potential in Latvia by addressing issues in the regulator and legislator approach.

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## **LIST OF ABBREVIATIONS**

AFSAL	Alternative Financial Services Association of Latvia
CRPC	Consumer Rights Protection Centre of Latvia
EC	European Commission
ECSF	European Crowdfunding Stakeholders Forum
EEA	European Economic Area
EESC	European Economic and Social Committee
EU	European Union
FCMC	Financial and Capital Market Commission of Latvia
FinTech	Alternative finance technology
FSA	Financial Supervision Authority of Estonia
JOBS	Jumpstart Our Business Startups Act
LTV	Loan to value ratio
P2P	Peer-to-peer lending
SME	Small to medium size enterprise
SPV	Special purpose vehicle

## INTRODUCTION

Currently the economic environment is changing rapidly. The millennium's development phase was followed by global financial crisis, which has changed the rules of game for all financial players and made others' think outside the box. After the economic crisis people started losing trust in traditional financial institutions like banks, where all the processes are still very bureaucratic. Overregulated bank lending system could not satisfy the credit demand of small to medium size enterprises, thus triggering the need for a new, innovative financing model to fill the gap. At the same time, the communication afforded by Internet and information technologies opened up new opportunities. Taking advantage of such situation, the development of alternative financial sources like crowdfunding became notable.

Crowdfunding refers to open calls to the public for the purpose of raising funds for a certain project. It is a way of gathering finance for projects launched by people or organizations as well as for business activity. The funds are normally collected from a wide group of individuals in the form of small contributions toward the desired level of financing, and often use is made of Internet-based service platforms.

The relatively higher returns compared to other investment types have emerged crowdfunding all over the world, becoming more and more popular each year. The crowdfunding's increasing popularity has been noticed by governments, who feel the need to legislate in this new and attractive area. However, the approaches differ. Some try to protect investors by putting too many restrictions on crowdfunding operation, but others are still holding on to see what happens next, letting the sector self-regulate.

Recently the potential was revealed of crowdfunding real estate projects, as it offers secured loans with a reasonably high return. The advantage of real estate crowdfunding today is the ability to transact online and the unparalleled access to deals by using the Internet as the new distribution platform. Given the advantages in modern technology, investors can now browse investments online, securely sign legal documents online and transfer funds. Rather than doing due diligence on hundreds of real estate projects to find one to invest in, investors can browse lists of pre-vetted investments through crowdfunding platforms.

This concept reached the Baltics few years ago and two platforms were established in Estonia to offer investment opportunities in mortgage backed loans. All parties can benefit – the real estate developer gets funding, investors get reasonable returns, but the society benefit from additional employment, paid taxes and enhanced real estate sector. Evaluating the success in Estonia, a year ago a similar platform was developed in Latvia for local purposes. **However, due to Latvia's regulatory issues it has not developed as successfully as the ones in Estonia.**

The thesis has two major purposes:

- 1) to investigate the operation of three real estate crowdfunding platforms in the Baltics;
- 2) to demonstrate Latvian and Estonian regulator approach and the resulting crowdfunding volume.

The first chapter will gain reader's insight on crowdfunding's concept, paying attention to its development, forms, current volume and legal status. The second chapter will explain how real

estate crowdfunding model works from each actor's perspective; it will also pay attention to risks related to such investments. The third chapter is dedicated to case analysis of three real estate crowdfunding platforms operating in the Baltics, explaining their foundation, crowdfunding business model and loan portfolio. The fourth chapter will evaluate Latvian and Estonian regulator approach on crowdfunding. Finally, author's conclusions regarding real estate crowdfunding in the Baltics will be presented.

# 1. CROWDFUNDING AS A NEW SOURCE OF FINANCE

The first chapter “Crowdfunding as a new source of finance” consists of four subchapters. The first subchapter describes the development of crowdfunding in the world, starting with the history of how and when crowdfunding has started and why it has developed, ending with interesting facts about its development. In the second subchapter, the forms of crowdfunding will be examined by mainly looking deeper into two forms of crowdfunding – with return and without return. Following, in the third subchapter, the global crowdfunding volume will be analysed and the subchapter’s title is “Size and growth of crowdfunding finance”. To continue the theoretical chapter and understand both financial and legislative factors there will be Crowdfunding’s legislation overview in the fourth subchapter viewed. Altogether, the first chapter will improve readers’ understanding on the concept and give relevant background to understand the next chapters and analysis in the end of the thesis.

## 1.1. Crowdfunding’s development in the world

The basics of crowdfunding goes back to early 18th century when wealthy Irishman Jonathan Swift lent a sum of £ 500 to poor craftsmen. He chose around 50 skilled craftsmen and his loan was not bigger than £ 10 for each. Few years later the same system was followed by Dublin Musical Society and many other persons distributed their wealth to the poor. This allowed industrious individual workers and tradesmen to develop their businesses. The social benefits of such micro-crediting were soon recognized, so few decades later such public lending was made legal by an Act propagated in 1778 by the Irish parliament.<sup>1</sup>

A similar approach was taken in 1884 when Americans built the Statue of Liberty designed by French sculptor Frederic Auguste Bartholdi. The sculpture of statue was prepared in France and paid by its government, served as a diplomatic gift to the United States. The Americans only had to build a granite plinth as a pedestal for the statue which cost \$250 000 - around \$ 6,8 million<sup>2</sup> at today's prices.

However, New York Governor Grover Cleveland rejected to allow city funds to be used for it, but Congress could not agree on a funding either. The situation seemed as a dead end, when local publisher Joseph Pulitzer decided to launch a fundraising campaign in his newspaper The New York World. In the end, the campaign raised money from more than 160 000 people, including young children, businessmen, street cleaners and politicians, more than 75% of donations amounting to less than a dollar. After five months the campaign celebrated success, raising in total \$100 000 to complete the pedestal. “It used a single collection point - the newspaper - to raise money from a very large pool of donors each pledging as little as pocket change.”<sup>3</sup> If

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<sup>1</sup> Aidan Hollis and Arthur Sweetman, “Microfinance and Famine: The Irish Loan Funds during the Great Famine,” *World Development* 32 (2004): p. 1511, accessed October 24, 2017, [doi.org/10.1016/j.worlddev.2004.04.002](https://doi.org/10.1016/j.worlddev.2004.04.002).

<sup>2</sup> Federal Reserve Bank of Minneapolis. Consumer Price Index (Estimate) 1800-. (Calculation: \$ 250 000 x (734,2 / 27) = \$ 6 798 148) Available on: <https://www.minneapolisfed.org/community/teaching-aids/cpi-calculator-information/consumer-price-index-1800>. Accessed October 24, 2017.

<sup>3</sup> BBC. The Statue of Liberty and America's crowdfunding pioneer, available on: <http://www.bbc.com/news/magazine-21932675>. Accessed October 24, 2017.

launched today, the campaign would be a classic crowdfunding project like the thousands we can observe online at this moment. So what is the real reason it took three centuries until the concept of crowdfunding got so popular as it is for today?

A more recent development of crowdfunding practices can be observed during the last decade. Back in 2006 the term “crowdfunding” was first invented by a social entrepreneur Michael Sullivan, founder of “foundavlog” – a web-based video platform with the ability to send micro amount of money (starting from one cent) to other users.<sup>4</sup> His wording was inspired by Jeff Howe, who just few months earlier invented a term called “crowdsourcing” – a modified concept of the word “outsourcing”.<sup>5</sup> “Such a switch in words denotes a new management philosophy: ask an easily reachable “crowd” to raise funds, to bring up new ideas, or to appraise opinions.”<sup>6</sup>

Although the terms were new, fundamentally resource collection from the crowd has been known for centuries - but it has never been practiced on the Internet. “The novelty of what we could call “crowdpractices” lies in the opportunities afforded by the Internet, and thus in a new momentum for a proven pattern.”<sup>7</sup> The Internet is a powerful tool to connect millions of people, each with their own interests – be it social, entrepreneurial or any other. Information technology which is highly developed nowadays, helps us to communicate with each other in a more effective, easier, faster, and last but not least, cheaper way.

## 1.2. Forms of crowdfunding

To understand the different approaches and aims of crowdfunding, this chapter will include description of diverse forms which crowdfunding include and also explanation on how this financing technique can be managed. In general, crowdfunding can be categorized by two criteria: fundraising mode and whether it aims for return or not.<sup>8</sup> There are two fundraising modes commonly known – “all-or-nothing” or “keep-it-all”.<sup>9</sup> The first “all-or-nothing” refers to crowdfunding campaigns which have a set goal of amount needed to be raised within a specified timeframe. If the amount is not achieved, the campaign is cancelled and investment does not occur. The other mode, as described in the wording “keep-it-all”, is not dependent on the funding amount raised – the fund seeker gets the amount raised even if the goal is not achieved.

When analyzing diverse articles on forms of crowdfunding, different opinions on this mode comes up, however there were two which stood out. One strong opinion is openly discussed in

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<sup>4</sup> Crowdfunding.de. „I felt that a new term was needed“ – Crowdfunding-Wortschöpfer Michael Sullivan im Interview, available on: <https://www.crowdfunding.de/crowdfunding-wortschoepfer-michael-sullivan-im-interview/>. Accessed October 23, 2017.

<sup>5</sup> Wired. The Rise of Crowdsourcing, available on: <https://www.wired.com/2006/06/crowds/>. Accessed October 24, 2017.

<sup>6</sup> Jérôme Méric, Isabelle Maque and Julienne Brabet, *International Perspectives on Crowdfunding: Positive, Normative and Critical Theory* (Bingley: Emerald Group Publishing Limited, 2016), p. xv. Available on: eBook Academic Collection (EBSCOhost) database. Accessed October 23, 2017.

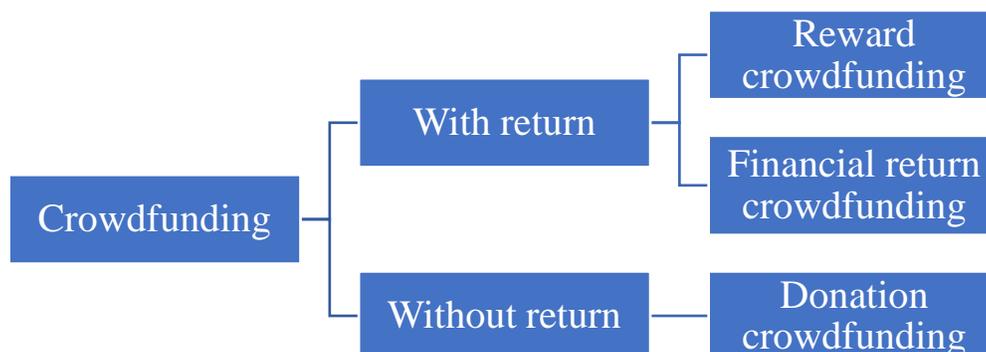
<sup>7</sup> *Ibid.* p. xvi.

<sup>8</sup> Roberto Bottiglia, Flavio Pichler, *Crowdfunding for SMEs: A European Perspective* (London: Palgrave Macmillan, 2016), p. 11.

<sup>9</sup> Douglas J. Cumming, Gaël Leboeuf and Armin Schwiendbacher, *Crowdfunding Models: Keep-It-All vs. All-Or-Nothing* (2015), available on <https://ssrn.com/abstract=2447567>. Accessed October 25, 2017.

different articles and books by scholars Pichler and Tezza from Italy, but the opposite opinion have come from research made by “Institute of Economics Research” paper made by Bednarz, Markiewicz and Ploska – scholars from Poland - described below. From the return point of view, Pichler and Tezza have categorized crowdfunding in following forms:

- Donation crowdfunding: donors are funding a project or idea without the expectation of any financial return, but they can have immaterial or intangible rewards;
- Social lending: a web-based form of donation crowdfunding for social projects in developing countries, no interest or principal is paid back;
- Reward crowdfunding: compared to donation crowdfunding, people can get gift in return for their investment, but it cannot be financial.
- Pre-purchase: commonly known as Kickstarter campaigns, where people are investing money in a form of advance payment for a product to be manufactured;
- Peer-to-peer (P2P) lending: this is the current alternative for bank loans, where individuals finance a project with the expectation of periodic interest and principal at the end of period;
- Equity crowdfunding: investors are offered shares of a company (usually startups), the return can be in the form of dividend payments and/or capital gains;
- Profit and revenue sharing: similar to P2P lending form, but long term.<sup>10</sup>



Differences of the crowdfunding models are displayed graphically in Figure 1.1.

Figure 1.1. Crowdfunding models. Source: Pichler and Tezza.<sup>11</sup>

Contrary to the figure above, Bednarz, Markiewicz and Ploska are defining crowdfunding as an investment that always has either a financial or non-financial return.<sup>12</sup> This is also supported by many other scholars, e.g. Vassallo pointing out, that the participating individuals in any form of crowdfunding are generating themselves a social reputation and trust in the crowd economy.<sup>13</sup>

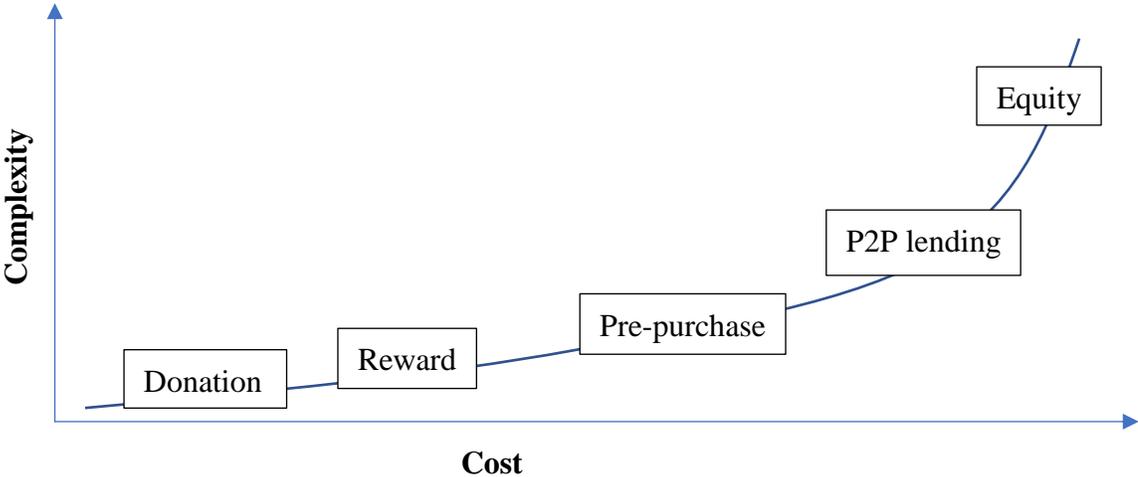
<sup>10</sup> *Supra* note 8. p. 12.

<sup>11</sup> *Ibid*, p. 13.

<sup>12</sup> Joanna Bednarz, Magdalena Markiewicz and Agnieszka Ploska. *The determinants of crowdfunding development – empirical analysis in the countries of Central and Eastern Europe*. No. 70/2017 (2017), available on: [http://www.badania-gospodarcze.pl/images/Working\\_Papers/2017\\_No\\_70.pdf](http://www.badania-gospodarcze.pl/images/Working_Papers/2017_No_70.pdf). Accessed October 24, 2017.

<sup>13</sup> Walter Vassallo, *Crowdfunding for Sustainable Entrepreneurship and Innovation* (Hershey: Business Science Reference, 2017), p. 5. Available on Google Books database. Accessed October 28, 2017.

Depending on the crowdfunding model, the complexity to run a given campaign can have different levels. From the platform point of view, the more complex campaign, the more expensive it is to run it. The complexity of the platform differs from phases involved in it, the project usually includes project evaluation, marketing, attracting investors and last but not least defining the legal relations between parties by preparing agreements. Therefore it is important to predetermine what kind of crowdfunding model should be used for each project. A graphical overview of the different crowdfunding model complexity and expense level is presented below



in Graph 1.1.

Graph 1.1. Crowdfunding models’ complexity and cost comparison. Source: Adapted from Méric *et al.*<sup>14</sup>

The least complex and cheapest form of crowdfunding is donation model, where typically no background analysis is needed to evaluate the project, and backers and fund seekers interests do not need to be secured with an agreement, because no financial return is expected. The reward and pre-purchase models involve already a post-investment relationship between the parties, thus calling for an extra effort in relationship management, agreement drafting and even financial monitoring and controlling. The third model, namely P2P lending, expands the complexity with financial analysis as well as advanced legal patterns, but equity crowdfunding is believed to be the most complex model due to all previously mentioned matters added with the structuring of company ownership rights.

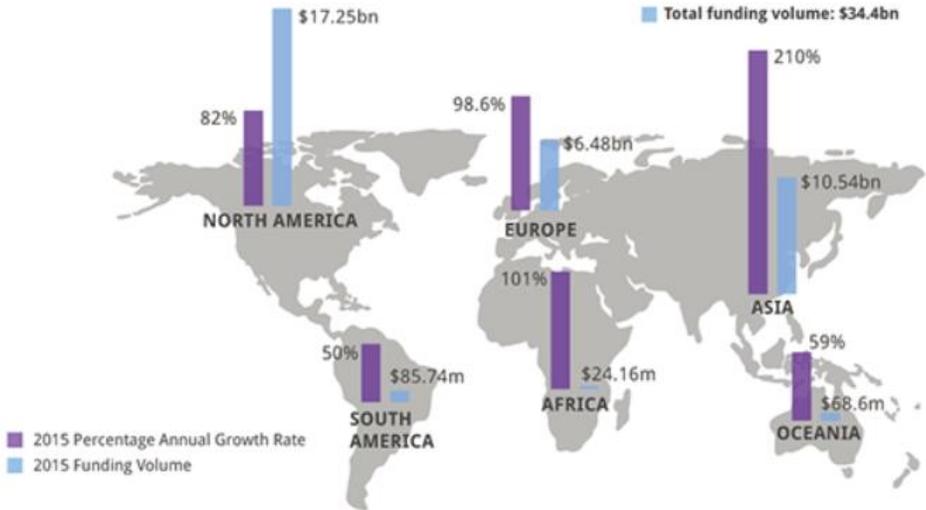
**1.3. The size and growth of crowdfunding finance**

To assess the current volume and future trends of crowdfunding, the following chapter will analyse the available information about global crowdfunding amounts. The crowdfunding development is analysed by two main drivers: the Internet and the recent economic crisis. Followed by a recession and its (d)effects on financing small and medium – sized enterprises

<sup>14</sup> *Supra* note 6. p. xxii.

(SMEs), it has triggered the need for a new, innovative financing model to fill the gap – and this is where crowdfunding phenomenon comes in. The time-consuming bank lending system cannot keep up with the emerging start-up company funding, which demands a prompt investment action, even not mentioning the fact that banks avoid such risky ventures. It is surprising, yet understandable that during recession time crowdfunding has emerged, while the overall financing by banking sector ceased.

The importance of engaging into innovative financial solutions is highlighted by global management consulting and professional services company “Accenture” report which states that alternative finance technology (FinTech) ventures has grown from nearly two billion dollars in 2010 to \$22,3 billion in 2015.<sup>15</sup> Other sources report that the total crowdfunding industry fundraising volume in 2015 was \$34,4 billion, of which \$25 billion are generated from P2P lending, \$5,5 billion from reward and donation crowdfunding, but \$2,5 billion from equity crowdfunding.<sup>16</sup> Crowdfunding’s volume division by the markets has been visualized in Figure 1.2., showing US as the leader with \$17,25 billion, followed by Asia and Europe. South America, Africa and Oceania are accounting only for 5% of global crowdfunding volume, thus addressing a great future potential. All markets are signaling a significant growth of crowdfunding industry,



led by Asia with 210% annual growth.

Figure 1.2. Volume and growth of crowdfunding in 2015. Source: Crowdexpt.<sup>17</sup>

However, a precise evaluation of crowdfunding’s volume is hindered by the unclear taxonomy of its terminology and forms. According to CrowdfundingHub research in the EU, the data interpretation does not follow a fixed pattern across the member states.<sup>18</sup> Same as with the

<sup>15</sup> Accenture. Fintech’s Golden Age, available on: [https://www.accenture.com/t20160724T221504Z\\_w\\_us-en/acnmedia/PDF-26/Accenture-FinTech-New-York-Competition-to-Collaboration.pdf](https://www.accenture.com/t20160724T221504Z_w_us-en/acnmedia/PDF-26/Accenture-FinTech-New-York-Competition-to-Collaboration.pdf). Accessed October 26, 2017.

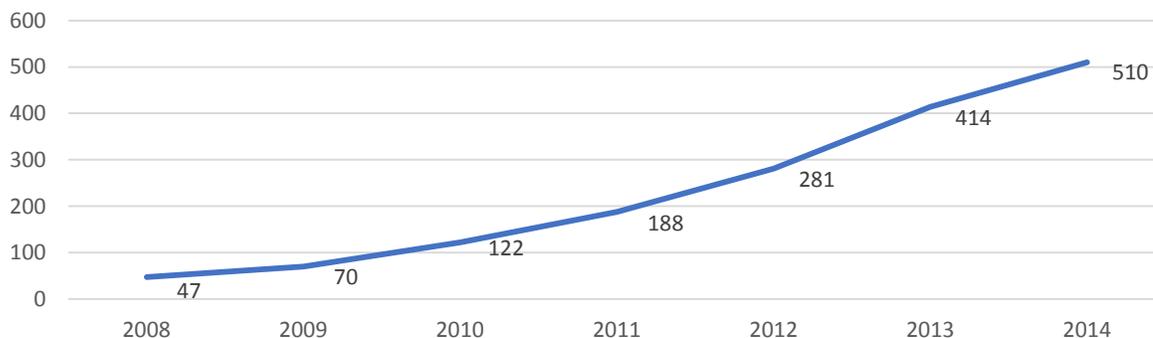
<sup>16</sup> Crowdexpt. Massolution Crowdfunding Industry 2015 Report, available on: <http://crowdexpt.com/crowdfunding-industry-statistics/>. Accessed October 31, 2017.

<sup>17</sup> *Ibid.*

<sup>18</sup> CrowdfundingHub. Current State of Crowdfunding in Europe. An Overview of the Crowdfunding Industry in more than 25 Countries: Trends, Volumes & Regulations, available on:

legislation, also terminology and data collection is not harmonized, thus pointing out issues for precise comparison. In context with the main topic of this thesis, real estate crowdfunding in many cases is still recognized as a developing form of crowdfunding and therefore omitted from the general statistics. Yet, to capture the trend of crowdfunding's breakthrough performance it is worth analysing some key numbers.

As presented for the European Crowdfunding Stakeholders Forum (ECSF), in the period of 2008-2014 the amount of live crowdfunding platforms has increased by more than 10 times in six years, amounting to a total of 510 platforms in the EU. The graph below shows the dynamics of crowdfunding platform amount.



Graph 1.2. Number of live crowdfunding platforms in the EU, 2008-2014. Source: Crowdsurfer.<sup>19</sup>

UK is a dominant leader with 143 live platforms, followed by 77 in France, 65 in Germany, 58 in the Netherlands, 42 in Italy, 33 in Spain and 16 in Poland. The number of live platforms in other EU member states in 2014 was below 10. From the operating 510 platforms, 30% were reward, 23% equity, 21% loan and 18% donation-based crowdfunding platforms.<sup>20</sup>

#### 1.4. Legislative overview of crowdfunding

Despite the fact that crowdfunding has become popular already a decade ago, only recently lawyers around the world have started to analyse it. Enjoying the rise of the internet and thus being a pioneer of the new millennium's alternative financing system, crowdfunding experienced a slightly delayed notice by specialists and public authorities. In practice, it took some time for crowdfunding to get popular across the world and raise public interest about it.<sup>21</sup>

It can be argued that the development of crowdfunding has been affected by the responsiveness of the legal authorities' actions. Lack of precise legal framework has been as a hand brake for crowdfunding to emerge already before 2010. On the other hand, the financial distress resulting

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[https://www.sbs.ox.ac.uk/sites/default/files/Entrepreneurship\\_Centre/Docs/OxEPR2/current-state-crowdfunding-europe-2016.pdf](https://www.sbs.ox.ac.uk/sites/default/files/Entrepreneurship_Centre/Docs/OxEPR2/current-state-crowdfunding-europe-2016.pdf). Accessed October 29, 2017.

<sup>19</sup> Crowdsurfer. Crowdfunding: Mapping EU markets and events study, available on: <http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetailDoc&id=27040&no=3>. Accessed October 30, 2017.

<sup>20</sup> *Ibid.*

<sup>21</sup> *Supra* note 6. p. 82.

from the crisis made society very cautious on wanting to review new forms of investment systems right after the collapse.

However, the cuts in standard funding sources like banks, stock markets, government funding etc. made entrepreneurs seek for other forms of funding. Probably crowdfunding was the golden path for both parties – investors and fund seekers, because such financing way allowed direct interaction between the parties, having both social and financial benefits. The fact that banks are theoretically excluded, made this system emotionally acceptable for a wide range of population. Considering the economic growth potential of this phenomenon, states began to prepare legislation. In fact, common law states were the first to adopt legislation on this matter.

### **United States**

The JOBS (Jumpstart Our Business Startups) Act was adopted in the United States on April 5, 2012.<sup>22</sup> Not surprising, due to the fact that the web-based concept and terminology was born there. The new Act amended both the 1933 Act and the 1934 Act by reducing disclosure requirements for emerging growth companies as well as by expanding criteria to qualify for exemption from registering securities under the 1933 Act.<sup>23</sup> The importance of this exemption is to avoid providing investment prospectus, which usually forms high cost and would not pay off due to the smaller financial amount of crowdfunding offerings. Congress was aiming to increase US job creation and economic development for startup companies.<sup>24</sup> The JOBS Act Title III is defining crowdfunding in following words:

Crowdfunding is a relatively new and evolving method of using the Internet to raise capital to support a wide range of ideas and ventures. An entity or individual raising funds through crowdfunding typically seeks small individual contributions from a large number of people. Individuals interested in the crowdfunding campaign – members of the “crowd” – may share information about the project, cause, idea or business with each other and use the information to decide whether to fund the campaign based on the collective “wisdom of the crowd.”

JOBS Act sets out following requirements for Crowdfunding Regulation:

- a) A company is permitted to raise a maximum aggregate amount of \$1,070,000 in a 12-month period;
- b) Investors are limited in amount of their investments into crowdfunding campaigns depending on their annual income or investor net worth;
- c) Each offer must be conducted only through one registered intermediary;
- d) Eligibility to operate under this Regulation
- e) Issuers must electronically file its offering statement on Form C<sup>25</sup> exposing a mass of information about the company including financial indices, as well as noting the intermediary;

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<sup>22</sup> US. Securities and Exchange Commission (SEC). Jumpstart Our Business Startups (JOBS) Act. (5 April 2017). Available on: <https://www.sec.gov/spotlight/jobs-act.shtml>. Accessed October 25, 2017.

<sup>23</sup> Richard A. Mann, Barry S. Roberts, *Essentials of Business Law and the Legal Environment*, (Boston: Cengage Learning, 2016), p. 795. Available on: Google Books database. Accessed October 25, 2017.

<sup>24</sup> San Francisco Daily Journal. The Truth Behind the Small Business Jobs Act, available on: [http://www.law.uci.edu/news/in-the-news/2010/djournal\\_lawreview\\_112310.pdf](http://www.law.uci.edu/news/in-the-news/2010/djournal_lawreview_112310.pdf). Accessed October 25, 2017.

<sup>25</sup> See <https://www.sec.gov/about/forms/formc.pdf>

- f) After successfully raising funds through an offering, issuers have to file their annual reports each fiscal year to the Commission, as well as post it to their website;
- g) Limitations on advertisement and promotion of the offering by the issuer, where mostly all advertising, promoting and communication has to be carried out through communication channels provided by the intermediary;
- h) Restrictions on resale of securities in a crowdfunding platform.

## European Union

Similar to US legislation, EU provides for a Prospectus Directive 2003<sup>26</sup> which stipulates that a prospectus must be published when an offer of securities is made to the public within a member state. However, Directive offers a number of exemptions from the prospectus requirements, one of the most important being a threshold of the amount of public offering to be subject to this Directive.<sup>27</sup> In context with crowdfunding, with the latest amendment of Prospectus Directive 2010/73/EU<sup>28</sup> this threshold is set €5 million over 12 month period.<sup>29</sup> Though, member states are allowed to pass national laws for offerings below the Directive threshold.<sup>30</sup> Currently there is no union-wide legislation to regulate crowdfunding, but the EC has defined this financing with the following words:

Crowdfunding is an emerging alternative form of financing that connects those who can give, lend or invest money directly with those who need financing for a specific project. It usually refers to public online calls to contribute finance to specific projects.<sup>31</sup>

Due to the fact that EU still doesn't have a union-wide approach, at the moment, the JOBS Act is the most widely adopted legislation concerning crowdfunding in the world. However, several EU countries like Italy, France, UK and Germany have already passed legislation in national level, though each having a different scope and approach.<sup>32</sup> Diversity over the national laws are reaching from too much protected investor rights, thus blocking the expansion of this financing instrument, to balanced investor interest protection with supported development of crowdfunding.

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<sup>26</sup> Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (Text with EEA relevance), *OJ L* 345, 31.12.2003, p. 64-89. Available on: <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:32003L0071>. Accessed October 27, 2017.

<sup>27</sup> Dennis Brüntje, Oliver Gajda, *Crowdfunding in Europe: State of the Art in Theory and Practice*, (New York: Springer Berlin Heidelberg, 2015), p. 137.

<sup>28</sup> Directive 2010/73/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market (Text with EEA relevance), *OJ L* 327, 11.12.2010, p. 11-12. Available on: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32010L0073>. Accessed October 27, 2017.

<sup>29</sup> Art. 1(2)(h) Prospectus Directive.

<sup>30</sup> *Supra* note 6. p. 138

<sup>31</sup> European Commission. What is Crowdfunding? Available on: [https://ec.europa.eu/info/business-economy-euro/growth-and-investment/financing-investment/crowdfunding\\_en#what-is-crowdfunding](https://ec.europa.eu/info/business-economy-euro/growth-and-investment/financing-investment/crowdfunding_en#what-is-crowdfunding). Accessed November 10, 2017.

<sup>32</sup> *Supra* note 6. p. 97.

Recently European Commission (EC) has drawn its attention to the case and crowdfunding question is under action. In 2014 EC has defined the legal status of crowdfunding in different states in its communication to The Parliament.<sup>33</sup>

Several Member States have sought to address concerns around crowdfunding with financial return through guidelines (e.g. in Germany, the Netherlands, Belgium). Others (Italy, the UK, France and Spain) are considering, or have already taken, regulatory action to facilitate this new form of financing, while also aiming to adequately protect investors. The danger is that too burdensome and premature regulatory action could stymie the development of crowdfunding, while too lax policies could lead to losses to investors, harming consumer confidence and trust in crowdfunding.

On February 2015, EC had prepared a Green Paper on developing a Capital Markets Union.<sup>34</sup> It states that “European and national company law has not kept pace with technological development, for example by insufficiently integrating the benefits of digitalization.”<sup>35</sup> As the EC’s goal is more jobs and growth, it is a challenge to unlock investment in Europe’s companies. Few months later EC communicated its Action Plan on Building a Capital Markets Union, where it stated that it will “promote innovative forms of business financing such as crowd-funding, private placement, and loan-originating funds whilst safeguarding investor protection and financial stability”.<sup>36</sup> It is believed that a long-term investment growth can be ensured, if all 28 EU member states form a single market for capital.

Although the web-based technology would suggest a great potential for cross-border movement of capital, according to EC’s research there is a limited activity in this context. The research results indicate that “the diverse national approaches in these areas may encourage crowdfunding activity locally, but may not be necessarily compatible with each other in a cross-border context.”<sup>37</sup>

During 2016 EC has carried on research in this field by submitting a report on Crowdfunding in the EU Capital Markets Union. The purpose for this report was to compare national legislation, identify best practice and present the results of the observed evolution of crowdfunding sector. It showed that crowdfunding can give significant help to achieve CMU Action Plan objective to mobilize capital across Europe and channel it to companies, especially SMEs.<sup>38</sup> CMU Action Plan is referring to US regulatory framework as being substantially more investment-friendly for

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<sup>33</sup> European Commission. Communication from the Commission to The European Parliament, The Council, The European Economic and Social Committee and The Committee of The Regions. Unleashing the potential of Crowdfunding in the European Union. COM(2014) 172 final (27 March 2014). Available on: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52014DC0172>. Accessed October 26, 2017.

<sup>34</sup> European Commission. Green Paper. Building a Capital Markets Union (18 February 2015). Available on: [http://ec.europa.eu/finance/consultations/2015/capital-markets-union/docs/green-paper\\_en.pdf](http://ec.europa.eu/finance/consultations/2015/capital-markets-union/docs/green-paper_en.pdf). Accessed October 26, 2017.

<sup>35</sup> *Ibid.* p. 25.

<sup>36</sup> European Commission. Communication from the Commission to The European Parliament, The Council, The European Economic and Social Committee and The Committee of The Regions. Action Plan on Building a Capital Markets Union. COM(2015) 468 final (30 September 2015). Available on: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52015DC0468>. Accessed October 26, 2017.

<sup>37</sup> *Ibid.* p. 15.

<sup>38</sup> European Commission. Report on Crowdfunding in the EU Capital Markets Union (3 May 2016). Available on: [https://ec.europa.eu/info/system/files/crowdfunding-report-03052016\\_en.pdf](https://ec.europa.eu/info/system/files/crowdfunding-report-03052016_en.pdf). Accessed October 26, 2017.

SMEs, which, if transposed to EU law, would have unlocked more than €90 billion for companies between 2009 and 2014.<sup>39</sup>

As stated by scholars Juredieu and Mayoux analyzing crowdfunding's legal status, "[t]he responsiveness of the public authorities which is not the same everywhere reveals the necessity of legislating in this attractive area, but it also raises issues. Defining the notion of crowdfunding will help to better understand why it definitely needs a legal framework."<sup>40</sup> This statement perfectly describes the current status of crowdfunding regulation in the EU. Some member states have already passed legislation, but some have prepared proposals/drafts to be ratified in near future, however they do not share the same scope. A missing EU-wide legal framework and definition for crowdfunding is preventing a harmonization of applicable law in cross-border context. As set out in the opinion of European Economic and Social Committee (EESC), only crowdfunding with financial return shall be regulated by EU law and covering at least:

- arrangements;
- services to be provided;
- caps on amounts;
- information obligations (including potential conflicts of interest);
- exemptions from the scope of application;
- prohibitions (especially prohibition of the acquisition and publication of related projects);
- need for a level playing field;
- financial requirements; and
- compulsory public registration (disclosure and transparency).<sup>41</sup>

The absence of harmonization can lead to a situation, where crowdfunding platforms are migrating to a member state with more flexible legislation. Such migration has already been practiced by one Latvian real estate crowdfunding platform. They have registered their company in Estonia and now operate under Estonian law.<sup>42</sup> It is not recognized as a credit institution there and therefore it is possible to avoid minimum capital requirements and costly licensing process compared to the situation in Latvia and still operate the platform from Estonia.

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<sup>39</sup> *Supra* note 33. p. 5.

<sup>40</sup> *Supra* note 6. p. 82.

<sup>41</sup> European Economic and Social Committee. Opinion of the European Economic and Social Committee on the communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions — Unleashing the potential of Crowdfunding in the European Union COM(2014) 172 final (16 December 2014), *OJ C* 451, 16.12.2014, p. 69-75. Available on: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52014AE4004>. Accessed November 7, 2017.

<sup>42</sup> Māris Krautmanis. Inovatīvo investīciju igaunizācija (Translation: Innovative investment estonisation), available on: <http://nra.lv/latvija/maris-krautmanis-3/218991-inovativo-investiciju-igaunizacija.htm>. Accessed November 7, 2017.

## 2. REAL ESTATE CROWDFUNDING

Over the last few years crowdfunding has remarkably raised interest by investors and fund seekers, as well as legislators, who try to define a legal framework to balance and safeguard the interests and rights of all parties. “From a public policy point of view, it is now widely agreed that crowdfunding should be promoted as it offers an alternative and potentially powerful means for channeling funds toward small innovative firms.”<sup>43</sup> However, return seeking crowdfunding as a source of finance should not be limited only to start-up businesses. This model can also be successfully used to fund traditional businesses, e.g. real estate development. Real estate crowdfunding campaigns can be either secured or non-secured, however to ensure successful fundraising in most cases they are secured.

Although real estate financing has been established as a separate sector already back in 1960s in the form of Real Estate Investment Trusts, crowdfunding model offers a different scope of finance both from the investor and fund seeker perspective.

As defined by Valanciene and Jegeleviciute, in any kind of crowdfunding process there are three parties involved in a close cooperation: investors, intermediaries and entrepreneurs.<sup>44</sup> The investors are a large number of individuals who are able to perform small investments for projects they find interesting. Intermediaries are crowdfunding platforms, which are displaying businesses seeking for funding, thus enabling a large number of investors to connect with the entrepreneurs by committing an investment. Entrepreneurs often use crowdfunding because they have failed to raise capital in other ways, mainly being refused by bank lending to support their project due to high risk levels or not reaching their threshold for an investment amount (usually few million euros and up).<sup>45</sup> This highlights the gap in finance for lower scale real estate projects, thus creating a big potential for crowdfunding in this sector.

Research shows that real estate crowdfunding has grown by 156 % in 2014, amounting to one billion dollars worldwide. Two main markets for real estate crowdfunding development are highlighted: North America has been the market leader with 56% share, followed by Europe with 42%. As forecasted by Massolution, real estate crowdfunding would continue to increase annually by 150%, making it one of the fastest-growing industry segments of crowd capitalism.<sup>46</sup>

On one hand, the increasing real estate crowdfunding volume proves its popularity among investors, signaling it to be a legitimate and trusted alternative for choosing banks both in lending and borrowing. On the other, traditional bank lending has become less and less available since the

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<sup>43</sup> *Supra* note 6. p. 3.

<sup>44</sup> Loreta Valanciene and Sima Jegeleviciute, *Valuation of Crowdfunding: Benefits and Drawbacks*. . Economics and Management 18 (2013) p. 41. Available on: <http://dx.doi.org/10.5755/j01.em.18.1.3713>. Accessed November 11, 2017.

<sup>45</sup> Fabian I. Marchand, *Crowdfunding Real Estate: Institutions and Markets. An Institutional Comparison on the Growth-patterns and Behaviour of Crowdfunding Real Estate Markets in the Netherlands and United States* (Master's Thesis). Delft University of Technology (2016) p. 18., available on: <https://repository.tudelft.nl/islandora/object/uuid:785a36c8-2a5b-4d5f-84a2-b60093491551>. Accessed October 29, 2017.

<sup>46</sup> *Supra* note 16.

last financial crisis. After implementation of such regulations as Basel III, the banks are forced to review their credit portfolio and manage it with less risky assets. This mostly results in cutting finance to SMEs and tilting towards financing large corporations. Also applying for a bank loan is a complex process which takes time, but the result often is unpredictable and expensive. Often companies with good projects get rejected by banks due to the small scale of business. Besides that, from the investor's point of view crowdfunding platforms are much more attractive as they offer higher returns than bank deposits. According to Bank of Latvia and Ministry of Finance reports from 2015, bank deposits are yielding around 0-1 %, whereas crowdfunding platforms offer investments with returns starting from 12 %.<sup>47</sup>

The evolving crowdfunding industry is changing the way small and medium companies used to fund their activities by bypassing financial intermediaries and creating direct connection between investors and fund seekers. It can take only minutes for a high quality projects to raise funds through a crowdfunding campaign, however usually these are few days. Still, it cannot be compared to a much more extended loan review process performed by banks.

At its core, crowdfunding means pooling money together from a group of investors to make an investment. In this sense, crowdfunding has existed in real estate for centuries. Neighbors have bought property together, husbands and wives and their sisters and brothers have collectively bought property and even multiple institutions have come together to collectively purchase property. The major difference between collective real estate investing of the past and crowdfunding for real estate today is the ability to transact online and the unparalleled access to deal flow by using the internet as the new distribution platform. Given the advances in modern technology, investors can now browse investments online, securely sign legal documents online, transfer funds and have access to investor dashboards to watch how investments are performing. Rather than doing due diligence on hundreds of real estate transactions to find one to invest in, investors can browse lists of pre-curated investments through crowdfunding companies.

## **2.1. Actors in the real estate crowdfunding process**

Real estate crowdfunding campaign can be described in six steps, both from the investor and fund seeker point of view. Obviously, there cannot be investors without investment seeking projects, so the borrower's role will be described first, followed by the intermediary platform's description and finally analysing investor's role.

### **Borrower**

First of all, a new borrower has to register an account on the platform. This will require borrower's identity information like person's first and last name, company name, registration number, address, phone number; it may even ask to upload copies of passport and company registration certificates to comply with "know your customer" checks. In this step the borrower

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<sup>47</sup> Anna Dravniece. Ministry of Finance experts' opinions. Kādēļ regulēt kolektīvās finansēšanas platformas? (Translation: Why to regulate crowdfunding platforms?). Available on: [http://www.fm.gov.lv/lv/aktualitates/jaunumi/fm\\_eksperu\\_viedokli/51773-kadel-regulet-kolektivas-finansesanas-platformas](http://www.fm.gov.lv/lv/aktualitates/jaunumi/fm_eksperu_viedokli/51773-kadel-regulet-kolektivas-finansesanas-platformas). Accessed November 11, 2017.

may have to agree with platforms user terms and privacy rules. After a successful registration the borrower has set up a user account with password.

Further on, the borrower has to create a project for a new campaign on the platform. In this step, the borrower is asked to specify details of the real estate project like location, intended use of property, forecasted sales prices, size of the property and if it is a renovation or new building project. Further the borrower has to specify detail on loan type, loan amount, period, method of repayment (annuity/repayment at the end/full bullet schedule), security type and market value.

After submitting the project of campaign, the platform is cross checking the information, performing due diligence on the borrower to evaluate its credit risk. Usually a competent and independent third party valuation is used to examine the security as well as the project. The platform management may also evaluate the exit strategy, as this is an important point to ensure all investors are paid back the principal and interest at the end of the campaign. If the platform management finds the project suitable for fundraising, it gets approved. Usually this is followed by a request to sign a loan agreement between the platform and the borrower.

In this step the project is ready to be published on the crowdfunding platform and can start fundraising. Once the project is live, the investors have chance to view all the details of it and make decision about investment through the platform. As stated before, this syndication period can last from one day to few weeks. Normally real estate crowdfunding platforms are working according all-or-nothing model, where a specified amount of funds has to be raised, otherwise the campaign is cancelled and the funds are transferred back to all investors. This is based on the assumption that project owners are only able to succeed with their project and deliver the promised returns if they have the complete financing required for doing so. However, if the raised amount has not reached the target within the specified time frame, but is close to it, the campaign can be extended for few days to allow more investors to participate, which can result in a fully funded campaign.

As soon as the fundraising target has been reached, the platform will ask the borrower to grant security rights for pledge and satisfy all other necessary conditions in order to release the funds to the borrower, who would be able to drawdown the loan. Now the funds raised are at the borrower's disposal and the business plan can be realized. Usually the platforms are following the development of project to monitor, prudentially supervise and control that the loan is used effectively.

Finally, in the end of loan period the borrower has to make a repayment of the principal and interest in full amount in order to exit the deal. The repayment schedule can be either on a monthly basis or a full repayment at the end of loan period. If the project has not been finalized e.g. property not sold, the borrower may ask to extend the loan period to finalize the project and be able to repay the loan later. Additional interest for the extended period would be calculated to appreciate investors' patience. The pay back is processed by the platform, where the borrower transfers the payment to its account, but the platform distributes the principals with accrued interest to the investors. After settlement, the pledge gets released and the funding cycle has been finalized.

## **Platform**

The user registration process is automated thanks to the developed information technology solutions available. In most cases the new user personal data will be electronically stored on the platforms databases. If the platform requires email or phone number verification, it will automatically send unique verification codes and the user will have to type them back to complete registration.

Each submitted project is carefully vetted and a due diligence is carried out to assess each particular project's riskiness and profitability. At the same time platform can ask an independent valuation service to be performed on the project and the security. If the project is accepted, the platform will prepare a loan agreement for the borrower.

When the borrower signs the agreement, the platform will publish the campaign to start crowdfunding. The syndication period can last for several days, during which the platform may promote it through email or social media like Facebook etc. The invested amounts are reserved for the particular project but not yet transferred to the borrower. Mostly the platforms are running campaigns according the all-or-nothing-principle which means that project initiators are only paid out the collected amount if they reach their pre-defined funding goal. If the investment target is not reached within the specified time period, the platform can decide to extend it for few days to let more investors participate and reach the goal. As soon as the target fund amount is reached, the platform will contact the borrower to grant the security for fund release. If the target investment is not reached, investor money is automatically transferred back to each user's virtual account.

As soon as the platform receives all relevant documents confirming the security registration, the platform will release funds to the borrower and send loan agreements to the investors. At this step the investment stage is completed.

In the post-investment stage the platform will contact with the borrower on regular basis to monitor how well the project is developing. When the loan period matures, the platform will ask the borrower to repay the principal and interest to distribute proceeds further to the investors. However, if the borrower experiences problems with repayment in due time, the platform will inform all investors about the status of project, action plan and suggest an extended loan period. In case of borrower's insolvency, the platform in cooperation with a law firm will action insolvency proceedings where the pledged security will be sold to recover the debt.

Contrary to traditional financial intermediaries, crowdfunding platforms do not borrow, pool, or lend money on their own account. Instead, they focus on matching project owners and backers, providing information about the projects and advice (for instance, on how to reduce investment risks).<sup>48</sup>

## **Investor**

From the investor point of view, the first action is same as for the borrower – the investor has to register an account providing all data needed for identification. The investor can be either a

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<sup>48</sup> Angelos Delivorias. Crowdfunding in Europe. Introduction and state of play (2017). Available on: [http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/595882/EPRS\\_BRI\(2017\)595882\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/595882/EPRS_BRI(2017)595882_EN.pdf). Accessed November 13, 2017.

natural or a legal person. An investor can only be a person which is at least 18 years old. The “know your customer” checks apply also here, asking investors to upload their passport copies. For a successful registration it is necessary to agree with platforms user terms and privacy rules.

After registration the investors now are able to add funds to their virtual account operated by the platform. This is usually done by making a bank transfer to the crowdfunding platforms company bank account with a reference to the user account. After payment processing, the amount is available for investment on the platform.

At this moment investors are able to choose project they find interesting to invest in. The lenders can see a detailed information about the business project – location, purpose, developer contacts, loan amount and terms, interest rate, loan to value (LTV) ratio, offered security etc. Each campaign is showing how many days are left until the syndication process will end as well as the amount raised at the moment. This helps to evaluate how actively other investors have invested in this loan. If the funded amount is substantially below the target, this may signal that a lot of investors have given a negative evaluation of the business project. A fast increase in the funded amount will vice versa indicate to the rest of investors that it is a perspective business.

When a particular project is chosen to invest in, the lender has to choose an amount and it is done simply by a click. At this moment the investment is frozen until the campaign raises the target amount of funding needed. When that happens, the platform will finalize the deal with the borrower and afterwards will provide the lender with a loan agreement. If the campaign was unsuccessful and the project did not raise the target of amount needed, the investment will be returned to the investors’ virtual account and will be instantly available for other projects.

Finally, after the platform has notified about successfully finished campaign, the lender can continue browsing other projects to invest in or wait for the end of loan period to expect the principal plus interest repayment by the borrower. The repayment will be done to the platform, which will distribute the proceeds to investors’ virtual accounts. Now the investor has the choice either to keep the money on the platforms virtual account for further investments or withdraw it back to own bank account.

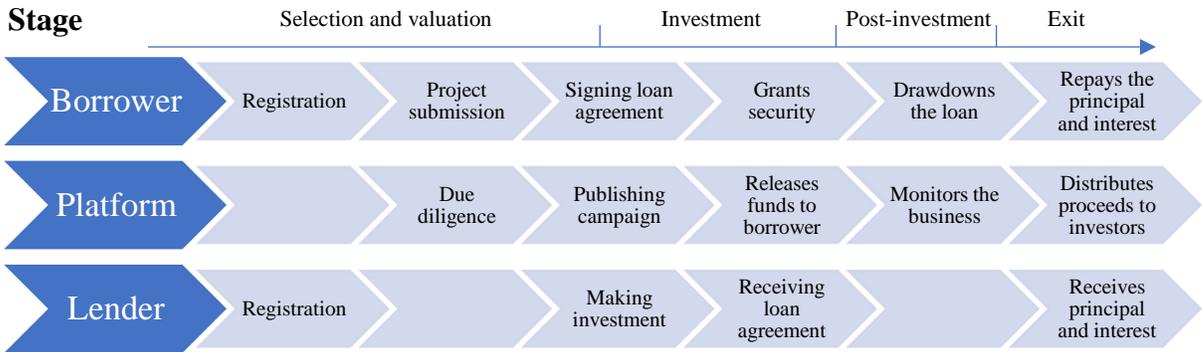


Figure 2.1. Real estate crowdfunding stages. Source: Own illustration.

The actions of each party in a real estate crowdfunding campaign have been graphically displayed in Figure 2.1. The crowdfunding cycle has been divided in four stages: selection and valuation, investment, post-investment and exit.

## **2.2. Risks related to real estate crowdfunding**

As it is with any kind of investment, also real estate crowdfunding has a variety of risks, which should be evaluated before engaging in such activities. In order to understand what kind of protective measures should be adapted in real estate crowdfunding legislation, this chapter will focus on risks involved in these investments.

The diversity of crowdfunding and the unestablished nature of the business mean that the activity also involves a wide variety of risks and challenges for the investor. Therefore, an investor participating in crowdfunding should clarify his commitment. Providing finance to new start-up companies takes by nature the form of venture capital and private equity investment - however, there is no regulated secondary market, and the investment may lose all of its value.

### **General investment risks**

#### *Market risk*

##### Market risks

Market risk is the chance that the value of an investment may change due to the unfavourable market events, such as the macro-economic reasons, political or social instability, due to the behaviour of investors etc. Such events may lead to changes in real estate prices and volatility. Diversifying the investment portfolio into various asset classes, industries and regions of the economy, can reduce the market risk.<sup>49</sup> Market risk arises from the fluctuating prices of investments as they are traded in the global markets. Market risk changes cyclically, from calm times to periods with wild price swings. Risk grades were conceived to help investors measure their continually changing exposure to market risk.<sup>50</sup>

#### *Liquidity risk*

Liquidity is generally defined as the ability of a firm to meet its debt obligations without incurring unacceptably large losses.<sup>51</sup> In context with real estate crowdfunding, liquidity risk refers to the adverse situation at the time of the liquidation of investment. There might be not enough buyers of real estate at the exiting time or at the price level expected by the seller. Liquidity risk may lead to the extended exit period.<sup>52</sup> The realization of liquidity risk may lead to

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<sup>49</sup> Crowdestate. Investment risks. Available on: <https://crowdestate.eu>. Accessed November 20, 2017.

<sup>50</sup> Nasdaq. RiskMetric – Market risk. Available on: <http://www.nasdaq.com/investing/risk/market-risk.aspx>. Accessed November 20, 2017.

<sup>51</sup> Jose A. Lopez. What is liquidity risk? Federal Reserve Bank of San Francisco Economic Letter. Available on: <http://www.frbsf.org/economic-research/publications/economic-letter/2008/october/liquidity-risk/>. Accessed November 20, 2017.

<sup>52</sup> *Supra* note 49.

significantly longer exit time unless investor is willing to sell its investment at considerably lower price.

#### *Currency risk*

When investing in another country or in foreign currency, there is a risk that investor may suffer losses due to unfavourable changes in currency exchange rates. However, currency risk can easily be hedged using various risk management methods and instruments.<sup>53</sup>

#### *Inflation risk*

Inflation risk is a situation where the inflation rate reduces the actual rate of return or real value of the investment.<sup>54</sup> Therefore the actual return rate or risk premium is the calculation excluding the value decrease after inflation rate has been applied.

#### *Legal risk*

Legal or regulatory risk is related to the fact that the legislative acts regulating the asset, investment activities or taxation of earned income may change during the investment period. For example, the government may change the tax laws that govern the taxation of capital appreciation or income earned by the investor.<sup>55</sup>

#### *Political risk*

Political risk or country risk is the chance of investment value changing due to the political changes or instability in the country. Radical changes in economic or legal environment (such as nationalisation), internal political affairs or social crisis situations (such as civil war) are all examples of political risk.<sup>56</sup>

#### *Concentration risk*

Concentration risk can occur in a situation where investor's investment portfolio is focused on just one asset class (for example, shares) or economic region.<sup>57</sup> In relation to real estate crowdfunding, the concentration risk would be high if an investor invested all his or hers funds into one campaign. In case of default, the investor would lose all savings. The concentration risk can be substantially reduced by reasonable portfolio diversification.

### **Specific risks related to real estate investments**

#### *Vacancy risk*

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<sup>53</sup> *Ibid.*

<sup>54</sup> *Ibid.*

<sup>55</sup> *Ibid.*

<sup>56</sup> *Ibid.*

<sup>57</sup> *Ibid.*

Vacancy refers to the situation where the real estate property has no tenant. The realisation of vacancy risk leads to the loss of rental income and the decrease of investment returns. Vacancy risk can be managed by keeping the lease terms on the market level, professional property maintenance, using proper and legally binding lease agreements etc.<sup>58</sup>

#### *Tenant risk*

Bad tenants refusing to pay rent or leave the property can significantly reduce the value of the real estate investment. Disputes with tenants may take long time and incur significant expenses. The lack of rental income might lead to temporary losses in times where ownership expenses exceed current income.<sup>59</sup>

#### *Technical risks*

Technical risk describes a situation where investment is made into real estate with technical defects that can cause a decrease in rental income or adversely affect the property's sales price. Technical risks may lead to the need for unexpected repair and renovation costs. However, technical risks can be managed and reduced performing real estate due diligence and the subsequent maintenance process.<sup>60</sup>

#### *Location risk*

Location risk refers to the situation where the property's location might become less favourable over time, which might lead to the reduction in rental income or potential sale price, thus having an adverse effect on investment's overall profitability.<sup>61</sup> For example, if a large factory is built near residential villa, it will likely decrease the value of it because potential buyers would evaluate the comfort level of such property.

#### *Oversupply risk*

Occasional oversupply effect might arise in certain regions or market segments, resulting in increased competition, thus having difficulties in achieving planned rental prices.<sup>62</sup>

#### *Operational risk*

Operational risk is related to a situation where crowdfunding platform is not able to continue its business and the company would be liquidated. Liquidation reasons may be financial (lack of liquidity, bankruptcy), legal (changes in the legal environment), management (inability to run the business as planned), operational (loss of key personnel) etc.

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<sup>58</sup> *Ibid.*

<sup>59</sup> *Ibid.*

<sup>60</sup> *Ibid.*

<sup>61</sup> *Ibid.*

<sup>62</sup> *Ibid.*

### 3. ANALYSIS OF BALTIC REAL ESTATE CROWDFUNDING PLATFORMS

In order to understand the real estate crowdfunding sector in Baltics, this chapter will analyse three live platforms operating in this field and discover what kind of crowdfunding business models they are running. Each platform will be analysed separately, indicating its origin country, development, real estate crowdfunding market share, crowdfunding model and the legal relationships arising from the funding model. As described in previous chapters, crowdfunding has several models divided into financial and non-financial return groups. Financial return crowdfunding serves as an alternative for traditional financial intermediaries, and it can have different approaches to fund real estate projects.

#### 3.1. Case analysis of Bulkestate.com

Bulkestate platform is known as the first Latvian owned player in the real estate crowdfunding sector. Initially it was operated by SIA “LP Private Property”, which was registered as a private limited company in Latvian Commercial register on 20.04.2015.<sup>63</sup> At the registration time there were three shareholders: Karlīna Skalberga (55,6 %), Igors Puntuss (27,91 %) and Mārtiņš Zutis (16,49 %) with a registered paid in capital of € 9500.<sup>64</sup> According to the owners, an investment of € 70 000 was made to develop the platform. The first crowdfunding campaign was started on December 2016 to fund a real estate development project in Riga for € 60 000. The campaign was closed on the New Year’s Eve, when with a participation of 151 investors the project reached its investment target. The loan period was set for 6 months, however it was paid back already in the end of April 2017 in full including the interest 15% per annum. The minimal investment is set as low as € 50, making it possible for a wide range of public to participate. As stated by Vita Liberte, “BDO Latvia” partner and Bulkstestate investment committee member, crowdfunding for real estate makes it possible for a wide range of people to invest in this market, and there are not only institutional players among them. This means that it is possible for investors, who are ready to invest only € 300, to participate in projects with annual returns of 10 – 15 % and earn from it 30 to 45.<sup>65</sup> The company which owns Bulkstestate crowdfunding portal is also a member of Alternative Financial Services Association of Latvia (AFSAL).<sup>66</sup>

Bulkestate platform is serving as an intermediary between the borrower and lender offering a new alternative to bank loans. The purpose of these loans are reserved for real estate development projects as well as development of other kind of businesses. Investors from different countries are introduced to each project’s idea, which needs funding. A collateral is used as a security for the loan to be repaid according to the agreement. As soon as the borrower has settled the loan, the

<sup>63</sup> Lursoft. Companies Register – LP Private Property, SIA. Available on: <https://company.lursoft.lv/en/lp-private-property-fund/40103891306>. Accessed November 14, 2017.

<sup>64</sup> *Ibid.*

<sup>65</sup> Labs of Latvia. Latvijā izveidota pirmā puļa finansējuma platforma nekustamā īpašuma jomā (Translation: Latvia has launched first crowdfunding platform dealing in real estate sector). Available on: <http://www.labsoflatvia.com/lv/zinas/latvija-izveidota-pirma-pula-finansejuma-platforma-nekustama-ipasuma-joma>. Accessed November 14, 2017.

<sup>66</sup> Alternative Financial Services Association of Latvia. Available on: <http://lafna.lv/en/about-us>. Accessed November 15, 2017.



collateral is released. The fundraising process is performed online, thus it enables to save time and costs what would otherwise be used when borrowing through traditional financial intermediaries like banks. At the same time such fundraising model ensures higher security for capital and transactions, reducing risks to all related parties. According to Bulkestate, financing through crowdfunding offers more flexible rules for real estate developers and other entrepreneurs than banks. It is possible to agree on individual loan repayment terms, where the loan is repaid in parts or all at once in the end of loan period. The interest rates are adjusted so that they are interesting for both - entrepreneurs and investors. Bulkestate is not asking the potential borrower for perfect income statements and credit history, rather they are focusing on the borrower's project and the planned loan repayment structure. The fundraising through Bulkestate platform serves not only as an alternative source of finance, but also provides the possibility to advertise and promote a particular real estate project or other business and reach target audience which would not be possible when lending through banks.<sup>67</sup>

Figure 3.1. "Bulkestate" stakeholders' relationships. Source: Own illustration.

Bulkestate's operation in practice is illustrated in Figure 3.1 above. First of all, Bulkestate signs loan agreement with the borrower, where it acts as the loan originator. To secure the loan, borrower is asked to grant a security by pledging a collateral in favor to Bulkestate. At the same time, investors have the chance to invest in Bulkestate's loans, where they are offered to sign an assignment agreement for the rights of credit claim arising from Bulkestate's and borrower's loan agreement. Moreover, the assignment agreement's Article 10.5 stipulates that Bulkestate has no obligation to make a claim, or any other payment to the investor before Bulkestate has not received such payments from the borrower under the loan agreement.<sup>68</sup>

Although being a Latvian platform, Bulkestate has registered as Estonian limited liability company "Bulkestate" OÜ for the purpose of legally running their business. According to different sources, Latvian Financial and Capital Market Commission (FCMC) recognized Bulkestate as a credit institution under Latvian Credit institution Law<sup>69</sup>, which is based on EU Regulation 575/2013<sup>70</sup> stipulating, that "credit institution means an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account." Credit institutions in Latvia are subject to licensing by FCMC. In order to receive a credit institution operating license (permit), the minimum initial capital of a bank shall be equal to five million euros.<sup>71</sup> However, obtaining such initial capital for a start up like Bulkestate can be challenging. Contrary to Latvian FCMC approach, Estonian Financial Supervision Authority

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<sup>67</sup> Bulkestate Latvija. Facebook, November 23, 2017. Available on: <https://www.facebook.com/BulkestateLatvija/>.

<sup>68</sup> Bulkestate. Terms & Conditions. Bulkestate general terms for the use of web-site and the purchase of claims rights. Available on: <https://www.bulkestate.com/en/terms-conditions/>. Accessed November 15, 2017.

<sup>69</sup> Saeima. Kredītiestāžu likums (Translation: Credit Institution Law). Available on: <https://likumi.lv/doc.php?id=37426>. Accessed November 14, 2017.

<sup>70</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 Text with EEA relevance, *OJ L 176*, 27.6.2013, p. 18.

<sup>71</sup> Financial and Capital Market Commission of Latvia. Licensing of banks. Available on: <http://www.fctk.lv/en/licensing/credit-institutions.html>. Accessed November 15, 2017.

(FSA) does not recognize crowdfunding platforms like Bulkestate as credit institutions, thus excluding them from licensing requirements.<sup>72</sup>

As it is postulated on Bulkestate website, all investment projects on it are carefully selected before made available to investors. Every Bulkestate deal goes through a rigorous, consistent and multi-tiered evaluation process by Investment committee, which consists of two professional members experienced in business advisory and real estate development. The investment security is ensured also by offering only secured debts with as low as possible Loan to Value (LTV) ratios, which is letting Bulkestate to forecast a 0% default rate on their crowdfunded loans.<sup>73</sup> With regards to investors' funds, they are kept safe in an escrow account that is separated from Bulkestate operational bank account. If fundraising/crowdfunding project isn't successful and investment goal isn't reached, developers do not suffer any losses, but the investments are returned back to each investor's account. Although all loans are secured with a mortgage, Bulkestate admits that every investment project involves risks, which at times may have significant adverse effect on the performance of respective real estate project and may result in loss of a part of entire investment.<sup>74</sup>

Almost a year after Bulkestate launch, this platform has successfully crowdfunded seven loans. According to the platforms website, campaigns #1 and #2 have already been repaid, but the rest of five are outstanding. Most of the borrowers have used the loan to refinance an existing one. There is no information available if the existing loans are dealing with real estate business or other meaning that the property has only been used as a collateral for the loan, which is not used for development. Two loans have been used to purchase a property and prepare it for sale. Campaign #2 was used to buy an apartment, renovate it and sell afterwards with a profit. The other one, Midia Grand Resort campaign #7 was used to buy an apartment package in a holiday resort in Bulgaria. Bulkestate are now preparing a new campaign for collective purchase of these apartments. As stated on the platform, to participate in the collective purchase, interested persons have to choose one of the offered properties and make a reservation payment amounting to 10% of its value. If the campaign will reach the target reservations, all potential buyers will be contacted to sign property purchase agreements. In this way the platform is working as a gathering point of a mass of buyers, making the sales and marketing process cheaper, thus enabling sellers to offer a lower sales price for the property. If the target amount of reservations is not reached, the offer is closed and reservation sums are transferred back to the interested persons. The description of campaign #6 did not contain any clear information for the loan purpose. The details on all Bulkestate's crowdfunded loans can be viewed in Table 3.1.

#	Campaign	Investment type	Investment	Loan period, months	Interest per annum	LTV	Investments	Average investment
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<sup>72</sup> Financial Supervision Authority of Estonia. Press releases. FSA put forth a proposal to regulate crowdfunding. Available on: <http://www.fi.ee/index.php?id=20146&year=2016>. Accessed November 15, 2017.

<sup>73</sup> Explore P2P. Meet the startup – interview with Igors Puntuss, CEO of Bulkestate. Available on: <http://explorep2p.com/meet-bulkestate/>. Accessed November 15, 2017.

<sup>74</sup> Bulkestate. About. Available on: <https://www.bulkestate.com/en/about/>. Accessed November 15, 2017.

#	Campaign	Investment type	Investment	Loan period, months	Interest per annum	LTV	Investments	Average investment
1	Ernestīnes iela 37 <sup>75</sup>	Development of other projects	€ 60 000	6	15 %	50 %	151	€ 397
2	Dzirnavu iela 132 <sup>76</sup>	Development	€ 48 000	9	15 %	70,5 %	61	€ 787
3	Vidzemes pr. 10 <sup>77</sup>	Refinancing of current loan	€ 20 000	12	15 %	60 %	25	€ 800
4	Kr. Valdemāra iela 76 <sup>78</sup>	Refinancing of current loan	€ 70 000	12	14 %	61 %	135	€ 519
5	Dzīvojamā māja <sup>79</sup>	Refinancing of current loan	€ 140 000	12	13,40 %	16,3 %	126	€ 1 111
6	Meldru iela 11 <sup>80</sup>	Not mentioned	€ 30 000	12	15 %	68 %	59	€ 508
7	Midia Grand Resort <sup>81</sup>	Flip	€ 200 000	8	13,80 %	35 %	168	€ 1 190
8	Gravas iela 19 <sup>82</sup>	Financing other business	€ 10 000	12	14,00 %	34 %	34	€ 294

Table 3.1. Bulkestate crowdfunded loan statistics. Source: Bulkestestate.com

As already stated, Bulkestestate is paying attention to ensure low LTV ratio on their loans. LTV ratio represents the percentage of the loan compared to the offered collateral's (usually real estate property) estimated market value. The higher the LTV ratio, the riskier the loan is for an investor, because in case of depreciating market value of the collateral, the loan can exceed the collateral's value, thus not securing it in full amount anymore.

So far Bulkestate has successfully crowdfunded loans amounting to € 578 000, with an average loan of approximately € 72 250. Most of the loans are signed for a repayment after a year, but the shortest loan is only 6 months, averaging to 10 months per loan. In most cases the interest rate is 14 or 15 %, however two loans with a lower LTV ratio are also having a reduced interest of 13,4 and 13,8 %. All loans are secured by a first rank pledge on a real estate. None of the loans are exceeding a 70,5 % LTV ratio, signaling that even if the borrower would default, sale of the given collateral could recover the investments including interest. The average number of investments per campaign is 94, but the average investment amount is € 700 per campaign.

<sup>75</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/14-ernestines-iela-37/>.

<sup>76</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/16-dzirnavu-iela-132/>.

<sup>77</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/21-vidzemes-pr-10/>.

<sup>78</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/20-kr-valdemara-iela-76/>.

<sup>79</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/23-dzivojama-maja/>.

<sup>80</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/24-meldru-iela-11/>.

<sup>81</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/25-midia-grand-resort/>.

<sup>82</sup> *Ibid.* See <https://www.bulkestestate.com/lv/investicijas/26-gravas-iela-19/>.

However, the analysis of Bulkestate campaigns shows a small commitment to actual real estate development. Although Bulkestate is positioning itself as a platform for real estate crowdfunding, which “provides easy, secure and transparent way for everyone to invest in real estate and buy apartments”<sup>83</sup>, most of the borrowers have indicated, that the purpose for their crowdfunding loan request was either refinancing of outstanding loans or financing of other business. In both cases, there are no indications that the loans or businesses are dealing with real estate development. Another campaign didn’t mention any information about the purpose of the loan. This points out that basically the only connection with real estate in context with these crowdfunding campaigns is in the form of collateral. The lack of information for what kind of projects or businesses the loan will be used is lowering the transparency level for such investments. In general only campaign #2 was about real estate development, where the loan was intended to be used for purchase and renovation of property, followed by a sale (i.e. fix & flip). Campaign #7 has a similar nature, however this investment does not include any development activities; it is rather focusing on acquiring an apartment package in bulk for a lower price and afterwards selling them individually with a profit.

### **3.2. Case analysis of Crowdestate.eu**

Crowdestate is an Estonian owned crowdfunding platform dealing with real estate, it has been operating since January 2014 and can be nominated as one of the pioneers in this sector in the Baltics. It is operated by Estonian private limited company OÜ “Crowdestate”, which is managed by Loit Linnupõld and Märt Meerits. The paid in share capital of this company is € 53 000.<sup>84</sup>

Crowdestate is positioning itself as a leading Nordic real estate crowdfunding platform, providing more than 15 000 retail investors with a direct and transparent way to crowd-invest with professional real estate developers. This platform offers its investors an opportunity to build a diversified real estate investment portfolio by investing into carefully picked and thoroughly pre-vetted real estate investment projects. Crowdestate has set the minimum amount of € 100 that can be invested in a project. And this is the highest minimum amount among all three most popular real estate crowdfunding platforms operating in the Baltics. The platform is providing a follow-up reporting to all investors on a regular base. Crowdestate provides professional real estate developers with an access to full capital stack (senior loans, mezzanine financing, preferred or common equity) required in real estate business.<sup>85</sup> At the moment, Crowdestate has raised more than € 23 million for 49 real estate projects since it launched in 2014.<sup>86</sup> Its investors have successfully exited from 15 investments with a net annual return from 12,25 % to 48,01 % depending on the project and capital types. Crowdestate entered Latvian market with its first project in August 2016 by raising € 750 000 in just few days to finance an apartment building

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<sup>83</sup> *Ibid.* See <https://www.bulkestate.com/en/about/>.

<sup>84</sup> Centre of Registers and Information Systems of Estonia. E-Business Register. Available on: <https://ariregister.rik.ee/index?lang=eng>. Accessed November 15, 2017.

<sup>85</sup> European Fintech Awards 2017. Crowdestate OU. Available on: <https://europe2017.fintech.nl/companies/crowdestate-ou>. Accessed November 15, 2017.

<sup>86</sup> Crowdestate. All opportunities. Available on: <https://crowdestate.eu/opportunities>. Accessed November 17, 2017.

development.<sup>87</sup> Currently Crowdestate offices are established in Tallinn, Estonia, and Riga, Latvia, but the company is looking to expand to other EU countries in the nearest future.

As commented by Crowdestate CEO Loit Linnupõld on Reddit discussion website, the key reasons people should consider real estate crowdfunding platforms as a way to have real estate exposure are:

- high transparency level of investment offerings (all relevant information disclosed publicly);
- investment decisions are fully controlled (investors pick their individual investment properties);
- no barriers to entry (you can start investing from as low as 100 euros per investment);
- no investor-side fees;
- thorough pre-vetting (in Crowdestate's case, less than 5% of original investment ideas are ending being published on the platform);
- regular progress reporting.<sup>88</sup>

He also states that investors should consider following risk groups in mind when investing on real estate crowdfunding platforms: market risks; platform-related risks; legal and agreement-based risks.<sup>89</sup> These concerns of platform's CEO are also introduced in its operation: the platform is offering a thorough due diligence report for each campaign, consisting of detailed information about the project; loan purpose; borrower's experience in this field; SWOT analysis; a Crowdestate internal risk rating. The due diligence report is complemented with financial information including past financial data, forecasted financial models (base, negative and positive scenarios), repayment schedule and other figures. Platform is also presenting relevant documentation on the project like valuation reports.

As mentioned before, Crowdestate platform is operating since 2014 and there have been 50 projects so far, but due to the limited length of this paper only 18 campaigns from the recent calendar year will be analysed. During the year 2017, Crowdestate has completed 18 campaigns and crowdfunded more than € 9 million. Crowdestate can be viewed as the most advanced real estate crowdfunding platform in the Baltics, as it is offering investors different type of capital type investments. The campaigns analysed show following capital types: equity investment, mezzanine loans, secured loans (mortgage backed and commercial pledge) and unsecured loans. Altogether 14 loans have been issued to projects located in Estonia, three loans are related to real estate development projects in Latvia and one loan has been crowdfunded for a real estate project in Finland.

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<sup>87</sup> Investoriem.lv. Ar pirmo NĪ projektu Latvijā startē igauņu pūļa finansēšanas platforma Crowdestate (Translation: Crowdestate crowdfunding platform is launching its first real estate development project in Latvia). Available on: [www.investoriem.lv/2016/08/ar-pirmo-ni-projektu-latvija-starte.html](http://www.investoriem.lv/2016/08/ar-pirmo-ni-projektu-latvija-starte.html). Accessed November 15, 2017.

<sup>88</sup> Reddit. Discussion: Opinions on CrowdEstate and similar "crowdinvesting" platforms for real estate? Available on: [https://www.reddit.com/r/investing/comments/60tmrz/opinions\\_on\\_crowdestate\\_and\\_similar/](https://www.reddit.com/r/investing/comments/60tmrz/opinions_on_crowdestate_and_similar/). Accessed November 15, 2017.

<sup>89</sup> *Ibid.*

Firstly, the group of equity crowdfunding campaigns will be analysed. This group builds up the largest share of total investment amount in this platform during this year, which exceeds 36 % of total investment value. In fact, all 3 Latvian related projects have been fundraised in this model. The average funding per campaign has been € 658 700 with an average expected rate of return of 19,80 %. The number of investors participating in such campaigns varies from 452 to 989, depending on the funding goal (the higher goal, the more investors participate). On average, each campaign is funded by 640 investors, each committing a € 1013 investment. The average project period on equity real estate crowdfunding campaigns is 33 months. The data of each campaign has been gathered in Table 3.2. below.

#	Campaign	Investment type	Investment	Project period, months	Expected return	Number of investors	Average investment
1	Saules aleja 2A <sup>90</sup>	Development	€ 950 000	30	20,46 %	732	€ 1 298
2	Balozu 7 <sup>91</sup>	Development	€ 400 000	27	21,20 %	452	€ 885
3	Agenskalna 24 <sup>92</sup>	Development	€ 500 000	30	20,81 %	456	€ 1 096
4	Verkkosaar enranta <sup>93</sup>	Development	€ 1 003 500	42	19,80 %	989	€ 1 015
5	Kadaka pst 167 <sup>94</sup>	Development	€ 440 000	38	16,75 %	571	€ 771

Table 3.2. Crowdestate equity crowdfunding campaigns in 2017. Source: Crowdestate.

All five equity crowdfunding campaigns are related to real estate business, mainly offering additional capital for the development. All campaigns are supported with a detailed project description, SWOT analysis and Crowdestate risk rating. In order to execute each of the equity investment campaigns, Crowdestate is setting up special purpose vehicle (SPV) for each project. The raised investment will be treated as equity, letting the SPV own a share of the project. Each project's full net profit will be distributed between the investors in the form of variable interest.

In the time period analysed, Crowdestate has completed one crowdfunding campaign to raise funds for a mezzanine capital, which typically involves a mix of debt and equity financing, allowing investors to achieve gains through capital appreciation and interests on debt-repayment.<sup>95</sup> Due to the fact that equity is one of the most expensive source of capital and by its nature, it dilutes existing shareholders, mezzanine capital is an attractive alternative way to get the capital needed and it can be helpful in financing the start-up, expansion of

<sup>90</sup> *Supra* note 86. See <https://crowdestate.eu/opportunity/Saules-Aleja>.

<sup>91</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Balozu>.

<sup>92</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Agenskalna-24>.

<sup>93</sup> *Ibid.* See <https://crowdestate.eu/opportunity/floating-villas>.

<sup>94</sup> *Ibid.* See <https://crowdestate.eu/opportunity/kadaka-pst-167>.

<sup>95</sup> Laura Giurca Vasilescu, "Financing Gap for SMEs and the Mezzanine Capital," *Economic Research - Ekonomska Istraživanja* 23 (3) (2010): p. 58, accessed November 20, 2017, doi: <http://dx.doi.org/10.1080/1331677X.2010.11517423>

SMEs, innovation and business transfers.<sup>96</sup> Additionally, mezzanine finance improves the balance sheet structure, because it is treated like equity. From the borrower’s point of view, it offers greater entrepreneurial freedom and does not require consultations with the mezzanine investor, letting the borrower retain control over the company and avoid surrendering of ownership rights. However, mezzanine capital is subordinated and unsecured, thus drawing disadvantage for such capital investors.<sup>97</sup>

The information about mezzanine capital crowdfunding campaign is listed below in Table 3.3., showing the funding goal, expected investment period, annual interest, the number of participating investors and average investment made. Compared to equity crowdfunding campaigns, mezzanine capital campaign has a lower expected interest rate per annum, but the investor activity with regards to participation number and average investment is similar to equity crowdfunding campaigns. This is also supported with the theory that mezzanine capital is not as expensive as equity capital, thus resulting in a similar, yet cheaper interest loan for the borrower, but better protection of investor capital compared with private equity investment.<sup>98</sup> In this case, investments will be secured by a registered pledge on 100 % shares of the borrower set in favor of “Crowdestate Collateral Agent” OÜ.

#	Campaign	Investment type	Investment	Investment period, months	Interest per annum	Number of investors	Average investment
6	Peterburi tee 19/21 <sup>99</sup>	M&A	€ 400 000	24	16,00 %	390	1 026

Table 3.3. Crowdestate mezzanine capital crowdfunding campaigns in 2017. Source: Crowdestate.

The biggest group of equity crowdfunding investment campaigns is followed by two equally big groups of secured debts crowdfunding campaigns – mortgage secured loans and commercial pledge secured loans. Both groups together are forming 25 % of the total crowdfunded investment volume in 2017 through Crowdestate platform. However, from the investor’s point of view, commercial pledge does not have the same security level as real estate collateral. According to article from European Bank for Reconstruction and Development leading expert, mortgage backed financing has also been one of the most popular forms of financing for banks. The primary credit risk is supported by solid security that is immovable and normally maintains its value. Moreover, “[t]he incentive to avoid default is high, especially with residential property because a borrower will make every effort to avoid losing his home.”<sup>100</sup> Due to this point these two groups will be analysed separately, starting with the mortgage secured debt group.

The average funding per campaign on real estate secured debts has been € 289 050 with an average expected rate of return of 11,90 %, which is significantly lower than other capital type

<sup>96</sup> *Ibid.* p. 61.

<sup>97</sup> *Ibid.* p. 62.

<sup>98</sup> *Ibid.*

<sup>99</sup> *Supra* note 86. See <https://crowdestate.eu/opportunity/Lumina-kvartal>.

<sup>100</sup> Frederique Dahan, “Securitising mortgages in transition economies: the challenge of providing an efficient legal framework,” *Law and Financial Markets Review* 2 (2) (2008): p. 124, accessed November 20, 2017, doi: <http://dx.doi.org/10.1080/17521440.2008.11427950>.

campaigns due to the offered collateral. The number of investors participating in such campaigns varies from 107 to 532, depending on the funding goal (the higher goal, the more investors participate). On average, the investment in such campaigns is € 838, being lower compared to equity crowdfunding campaigns. The average project period on real estate backed crowdfunding campaigns is 26 months, which is also shorter compared to equity crowdfunding. The average LTV ratio is 64 %, which is higher compared to Bulkestate offerings. All Crowdestate’s investors’ claims, including loan principals and accrued interests, are secured by a first rank mortgage. The mortgage and collateral agent is “Crowdestate Collateral Agent” OÜ. The data of each Crowdestate real estate backed crowdfunding campaigns has been gathered in Table 3.4. below.

#	Campaign	Investment type	Investment	Loan period, months	Interest per annum	LTV	Number of investors	Average investment
7	L. Koidula 32 (II) <sup>101</sup>	Development of other projects	€ 415 000	12	11,00%	75 %	479	866
8	ROSENA DK OÜ <sup>102</sup>	Other	€ 31 200	60	12,00%	60 %	107	292
9	Koru põik 3 <sup>103</sup>	Development	€ 160 000	18	12,50%	77 %	138	1 159
10	Rataskaevu 5 (II) <sup>104</sup>	Development	€ 550 000	12	12,00%	43 %	532	1 034

Table 3.4. Crowdestate real estate backed crowdfunding campaigns in 2017. Source: Crowdestate.

The second group, consisting of commercial pledge secured debts, has a higher average interest rate than the previously analysed group. This is supported by the fact, that company shares are not as liquid as real estate collateral. Another disadvantage of commercial pledge is the fact that the share value can substantially drop, when the company is facing default. From the investor’s point of view, it is important to check the borrower’s balance sheet for any higher ranking debts, because this investment would be subordinated in favour of e.g. bank loan. A thorough financial analysis of the borrower must be carried out to assess the riskiness of such investment. In all cases the collateral of pledged assets are set in favour of “Crowdestate Collateral Agent” OÜ.

In total, during the year 2017 Crowdestate has offered three campaigns ranging from € 200 000 to € 500 000 dealing with pledged asset secured loans. The average fundraising amount per campaign has been € 383 000 with an average interest rate of 15,20 %. The offered loan period varies from 18 to 24 months. Average investment across all three campaigns is € 900 which is higher than on mortgage backed campaigns, but lower than on equity crowdfunding campaigns. All three campaigns have no relation to real estate business, neither in the form of collateral, nor

<sup>101</sup> *Supra* note 86. See <https://crowdestate.eu/opportunity/koidula-32-2>.

<sup>102</sup> *Ibid.* <https://crowdestate.eu/opportunity/Rosena>.

<sup>103</sup> *Ibid.* <https://crowdestate.eu/opportunity/Veskimoldre-rowhouses>.

<sup>104</sup> *Ibid.* <https://crowdestate.eu/opportunity/rataskaevu-5-2>.

loan purpose. The borrowers of these loans are companies from other sectors of business looking for extra capital to finance their projects. The data of each corresponding campaign is shown in Table 3.5.

#	Campaign	Investment type	Investment	Loan period, months	Interest per annum	Number of investors	Average investment
11	Click & Grow II <sup>105</sup>	Other	€ 500 000	18	16,10 %	414	1 208
12	Decoreter OÜ <sup>106</sup>	Other	€ 200 000	24	14,50 %	309	647
13	CT Kapital OÜ <sup>107</sup>	M&A	€ 450 000	24	15,00 %	532	846

Table 3.5. Crowdestate pledged asset crowdfunding campaigns in 2017. Source: Crowdestate.

As noted, Crowdestate has a diverse range of offered crowdfunding investment capital types. It is also offering unsecured loans, meaning that the loan is not backed by any means of collateral, thus having an increased risk of defaulting. Nevertheless, these loans are actually forming the second biggest part of Crowdestate platform's issued loans portfolio, accounting for 34 % of total investment volume. The loans in this group in terms of their volume are ranging from € 150 000 to € 1 500 000, which is also the biggest loan issued so far in 2017. The average unsecured loan crowdfunded is € 606 000 with an average interest rate of 15 %. The investment period varies from 7 to 30 months, with the average loan period being 20 months. All Crowdestate's funded unsecured loans are listed in Table 3.6.

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	Number of investors	Average investment
14	Mustakivi tee 25 <sup>108</sup>	Development	1 500 000	30	15,00 %	1036	1 448
15	Tööstuse 47d (I) <sup>109</sup>	Development	750 000	24	14,50 %	781	960

<sup>105</sup> *Ibid.* See <https://crowdestate.eu/opportunity/click-grow-II>.

<sup>106</sup> *Ibid.* See <https://crowdestate.eu/opportunity/decoreter-alpaka>.

<sup>107</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Cellin>.

<sup>108</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Project-Vega>.

<sup>109</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Toostuse-47D>.

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	Number of investors	Average investment
16	Tööstuse 47d (II) <sup>110</sup>	Development	328 400	23	14,50 %	449	731
17	Vabaduse 16 <sup>111</sup>	Development	150 000	14	16,00 %	178	843
18	Global Nord Timber OÜ <sup>112</sup>	Other	300 000	7	15,00 %	366	820

Table 3.6. Crowdestate unsecured loan crowdfunding campaigns in 2017. Source: Crowdestate.

### 3.3. Case analysis of Estateguru.co

Estateguru is the last of the three most popular real estate crowdfunding platforms analysed in this thesis. It is one of the leading Nordic online P2P lending platform facilitating short- and mid-term property loans. The platform has been established by property and FinTech professionals. EstateGuru’s team consists of experts in their field with over 15 years of experience in the real estate industry and 10 years in risk assessment.

The platform is owned by Estonian limited liability company “EstateGuru” OÜ and it is established in year 2013. Estateguru has three board members: Marek Pärtel (serving also as CEO), Marko Arro and Kaspar Kaljuvee.<sup>113</sup> According to Centre of Registers and Information Systems of Estonia, the registered share capital of this company is € 2 500, which is also the lowest among all three companies owning the real estate crowdfunding platforms.

The platform began to work in the end of year 2014. During its first operation year it had funded loans amounting more than € 4 million, but in the end of year 2016 the total amount of money lent through this platform exceeded € 16 million, indicating a 369 % growth per year. In the end of November 2017, this platform has funded loans for more than € 35 million, more than doubling its previous year result. To date, EstateGuru has more than 8 900 investors from 45 countries, who have participated in funding 226 crowdfunding campaigns on this platform, of which 87 have already been repaid.<sup>114</sup> “Even though the minimum investment is €50, biggest portfolios in the platform exceed €500,000.”<sup>115</sup> The funding speed on the EstateGuru platform is remarkable with the current record being € 31 000 in just 31 minutes.<sup>116</sup> Currently the platform’s

<sup>110</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Volta-Lofts-2>.

<sup>111</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Vabaduse-16>.

<sup>112</sup> *Ibid.* See <https://crowdestate.eu/opportunity/Global-Nord-Timber>.

<sup>113</sup> *Supra* note 84.

<sup>114</sup> Estateguru. Statistics and Trends. Available on: <https://estateguru.co/home/statistics>. Accessed November 24, 2017.

<sup>115</sup> Labs of Latvia. Estonian Estateguru is launching its first investment opportunity in Latvia. Available on: <http://www.labsflatvia.com/news/estonian-estateguru-is-launching-its-first-investment-opportunity-in-latvia>. Accessed November 24, 2017.

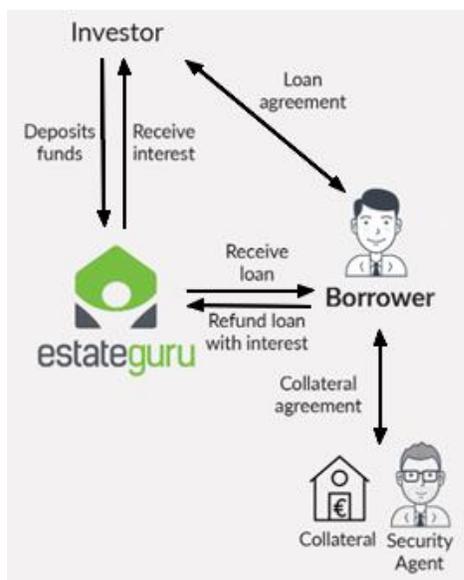
<sup>116</sup> *Ibid.*

0% default rate is among the most attractive statistics in the market.<sup>117</sup> Although it recently announced its first defaulted loan which would be followed by an auction sale of the collateral, the borrower took actions to refinance it and pay the overdue loan to avoid losing the collateral.<sup>118</sup>

The loans ranging from € 20 000 to more than one million facilitated through the EstateGuru platform are secured against property with a maximum LTV of 75%. As stated on platform’s website, “[t]he mission of EstateGuru is to provide hassle free and flexible financing to property developers and entrepreneurs and property backed investment opportunities to its international investor base. In the near future EstateGuru is launching its platform in new European markets to offer its investors even more investment opportunities.”<sup>119</sup>

The first Latvian project crowdfunding campaign performed by Estateguru took place on August 30, 2016 – right after Crowdestate entered Latvian market. The borrower needed a bridge loan for predevelopment to prepare the new capital structure and complete the design of the project secured by residential property at Zentenes 19a in Riga. The target loan amount of € 290 000 was successfully raised by 330 investors, yielding a 12,50 % interest rate per annum. Loan period was set for 18 months, but according Estateguru it has already been repaid.<sup>120</sup>

The relationship model between the stakeholders participating in Estateguru crowdfunding



campaigns is displayed in Figure 3.2 below.

<sup>117</sup> FinLantern. Findating - Estateguru. Available on: <https://finlantern.com/findating/estateguru/>. Accessed November 24, 2017.

<sup>118</sup> Estateguru blog. Estateguru sells the collateral of its first defaulted loan. Available on: <https://blog.estateguru.co/estateguru-sells-the-collateral-of-its-first-defaulted-loan/>. Accessed November 24, 2017.

<sup>119</sup> *Ibid.*

<sup>120</sup> Estateguru. Investments. Zentenes development loan - 1.stage (Riga, Latvia). Available on: <https://estateguru.co/investment/single/LV0820>. Accessed November 24, 2017.

Figure 3.2. “Estateguru” stakeholders’ relationships. Source: FinLantern.<sup>121</sup>

After a crowdfunding campaign has been published, the investors have the chance to invest their funds into the project through the platform. As soon as the amount needed is raised, the borrower has to go to the notary office and enter into an agreement with the Estateguru’s Security Agent to create a mortgage. The mortgage will then be registered at the Land Register with the Security Agent as mortgagee on behalf of the investors. The Security Agent is a separate limited liability company EstateGuru Tagatisagent OÜ whose primary purpose is to hold securities for the benefit of investors making investments via EstateGuru. The entity is controlled by a Baltic leading law office Jesse & Kalas.<sup>122</sup> All investment contracts are signed between the borrower and the investor, leaving EstateGuru out. All client funds are separated from EstateGuru’s operational funds

As stated in previous paragraphs, Estateguru has performed 226 campaigns, being a leader in this figure compared to other two real estate crowdfunding platforms operating in the Baltics. Due to the limited length of this paper, only 120 campaigns from the recent calendar year will be analysed. The collected data table can be viewed in Appendix 1 in the end of this paper. Average loan size through the platform is € 142 541, with the LTV (loan to value) ratio being 56.9 % and average rate of return of 10,82 %. The average loan term is 15 months.

	Campaigns	Loans issued	Average loan	Average interest p.a.	Average loan period, months	Average number of investors	Average investment
<b>Estonian projects</b>	<b>93</b>	<b>14 311 402</b>	<b>153 886</b>	<b>10,84 %</b>	<b>15</b>	<b>322</b>	<b>423</b>
Development	64	10 893 200	170 206	10,94 %	13	340	448
Other business development	18	1 636 735	90 930	10,46 %	21	253	325
Purchase	4	334 500	83 625	10,75 %	21	234	350
Refinancing	7	1 446 967	206 710	10,93 %	15	379	487
<b>Lithuanian projects</b>	<b>12</b>	<b>1 214 912</b>	<b>101 243</b>	<b>10,58 %</b>	<b>13</b>	<b>324</b>	<b>281</b>
Development	12	1 214 912	101 243	10,58 %	13	324	281
<b>Latvian projects</b>	<b>15</b>	<b>1 578 633</b>	<b>105 242</b>	<b>10,90 %</b>	<b>15</b>	<b>300</b>	<b>325</b>
Development	9	852 600	94 733	10,78 %	12	312	281
Other business development	3	375 000	125 000	11,00 %	18	277	410
Purchase	2	319 033	159 517	11,50 %	19	352	454

<sup>121</sup> FinLantern. Marek Pärtel. FinTech in the Innovation Hub of Estonia. Available on: <https://finlantern.com/findating/wp-content/uploads/2017/06/Estate-guru-June-2017.pdf>. Accessed November 24, 2017.

<sup>122</sup> Estateguru. EstateGuru General Frequently Asked Questions. Available on: <https://estateguru.co/faq/faq>. Accessed November 24, 2017.

Refinancing	1	32 000	32 000	10,50 %	18	152	211
<b>Grand Total</b>	<b>120</b>	<b>17 104 947</b>	<b>142 541</b>	<b>10,82 %</b>	<b>15</b>	<b>319</b>	<b>397</b>

Table 3.7. Estateguru crowdfunding campaigns in 2017. Source: Own calculations (see Appendix 1).

To improve the interpretation of collected data, separate calculations displayed in Table 3.7 have been performed for each country, divided by the respective investment type. As indicated in the table above, Estonian projects account for more than 75 % of the campaigns. In terms of investment value Estonian projects raised 83 % due to higher average loan per campaign compared to others. Latvian and Lithuanian projects are accounting for similar parts, however Latvia is a little bit ahead. Crowdfunding through Estateguru has been mostly used for real estate development projects in all countries, however around 17 % of the projects are only related to real estate with regards to the collateral used to secure the loan. The average number of investors is similar for all three countries, but Estonian projects have a much higher average individual investment. The average loan period is 15 months, the shortest - 12 months - are loans for real estate development, but longest are for real estate purchase loans as well as for other business development loans.

In terms of market share, Estateguru is the biggest platform accounting for 64 % of the total real estate crowdfunded loans' value in Baltics. It is followed by the other Estonian platform Crowdestate, which has 33,7 % market share, but the Latvian Bulkestate takes the remaining part of 2,1 %. Bulkestate's 2018 plan of reaching € 3 million threshold on funded loans could help to establish a more considerable market share, however the two competitors will also be expanding at a significant pace. If Bulkestate will be able to continue offering loans with 14-15 % annual interest, it has a good chance to attract more and more investors who are not appreciated with lower rates offered by Estateguru. From all crowdfunded loans, more than 81 % have been transferred to Estonian projects, 14 % to Latvian, but 5 % have been invested in Lithuanian projects.

## 4. EVALUATION OF PROPOSED LEGISLATION CONCERNING CROWDFUNDING

The final chapter of this thesis will analyse proposed legislation regarding crowdfunding. The first subchapter will be dedicated to crowdfunding status in Latvia, analyzing the lately passed bill of co-financing services, but the second will focus on Estonia, where the legislator has not yet defined any legal status for crowdfunding, but the public-private sector organization is performing self-regulatory activities.

### 4.1. Latvian approach

In March 2017 Ministry of Finance of Latvia has passed the Financial sector development plan for 2017 – 2019, consisting of capital market policy targets and action plan for further development of financial sector in Latvia.<sup>123</sup> The aim of this action plan is to develop stable, secure and internationally competitive financial sector with the availability of innovative financial services, which promotes sustainable economic growth for Latvia as well as strengthens Latvia's position as a regional financial services center. The development of technologies is recognized as a challenge which may relocate the traditional financial services providers with new players offering innovative solutions in this sector. Such trend is breaking the borders, enabling consumers to use services of non-resident financial services providers, thus putting resident providers at competition pressure not only from local competitors, but also from abroad.<sup>124</sup>

In such changing environment, the financial sector needs to successfully adapt to the situation and competition challenges, in order to continue its development towards sustainable, long term economics as well as pursue the leading position in Baltic region.<sup>125</sup> The inability to adapt can lead Latvian financial sector to lose competitiveness and eventually also its leading position, resulting not only in reduced support to economics in short term, but also decreasing the potential long term growth.<sup>126</sup>

The plan is defining 4 specific financial sector areas as priorities: banks'; capital markets'; alternative financial service providers' and insurance sectors. Three factors are considered as vital for the success of this plan: digitalization and innovations; financial sector compliance with anti-money laundering and counter-terrorism financing provisions; and international competitiveness.

In line with the development of financial technologies, a rapid increase in the offerings of alternative financial services can be observed. Services offered by FinTech companies are having effects of increased speed, cost optimization and analytic data management. Ministry of Finance are defining these companies as platforms which provide payment or financial services. However, formally they do not fall under the scope of financial sector, but still increase the competition in capital markets by increasing the transparency in price formation, as well as

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<sup>123</sup> Cabinet of Ministers order Nr. 126 "Par Finanšu sektora attīstības plānu 2017.-2019. gadam" (Translation: Financial sector development plan for 2017 – 2019). Published on "*Latvijas Vēstnesis*", 23.03.2017., Nr. 61 (5888), p. 4. Available on: <https://www.vestnesis.lv/op/2017/61>. Accessed November 25, 2017.

<sup>124</sup> *Ibid.* p. 7.

<sup>125</sup> *Ibid.*

<sup>126</sup> *Ibid.*

pushing prices down.<sup>127</sup> The cornerstones for successful development of such services are named modern technologies and legal framework which is balanced to the innovation's risk level. In context to relationship between FinTech companies and regulatory bodies, the formation of regulatory sandbox approach has been acknowledged as a good practice from UK<sup>128</sup> to promote FinTech development. Therefore, the action plan includes an aim to adapt legal framework for regulatory sandboxes until the end of year 2017, where Ministry of Finance should act as the responsible organization. According to AFSAL, in August it has passed suggestions to Ministry of Finance and FCMC to form the legal framework, pointing out the importance of it for FinTech companies. In AFSAL opinion<sup>129</sup>, FinTech companies should have the ability to submit for temporary license in order to avoid high costs in startup phase such as those related to licensing and the basic capital requirements. The regulatory sandbox should only apply to FinTech companies offering innovative service, which ensures added value to its customers, or promotes competition in the market. At the same time, such companies have to prove that the new service offered is not sufficiently regulated by the law in force or the current provisions concerning licensing are inadequately expensive for the startup phase. However, at the moment further activities neither by Ministry of Finance, nor FCMC have not been carried out in this field.

The development of alternative financial services is in line with the interests of consumers and investors in Latvia, but it has to ensure a good reputation for Latvia, because with an absent or insufficient legislative framework it can reduce transaction safety and increase threats on money laundering and terrorism financing, as well as increase the two traditional financial risks: credit-risk and liquidity-risk.<sup>130</sup>

The importance of supporting alternative financial services sector is explained with the fact that it is growing with considerable speed, accounting for 14,35 % of total resident credit volume.<sup>131</sup> This figure also consists of crowdfunding platform loans, which are substituting for the decrease in bank crediting.<sup>132</sup> As with regards to the European Commission interest in crowdfunding, Latvian legislator has confirmed the aim of adapting legislative act for regulating crowdfunding platform services. The target of planned activities in alternative finance sector is to increase capital accessibility for SMEs by 5,25 % of Latvia's GDP in a 3 year period.<sup>133</sup> However, the rapid growth of investments carried out through Latvian P2P platforms is obvious even before adapting the law. In the first three fiscal quarters of this year, 329 million euro has been invested through Latvian P2P lending platforms, according to data from AFSAL. Compared to the same

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<sup>127</sup> *Ibid.* p. 8.

<sup>128</sup> Financial Conduct Authority of the UK. Regulatory Sandbox. Available on: <https://www.fca.org.uk/firms/regulatory-sandbox>. Accessed November 26, 2017.

<sup>129</sup> Alternative Financial Services Association of Latvia. LAFPA rosina FM un FKTK uzsākt darbu pie regulatīvās smilšu kastes izveides. (Translation: AFSAL suggests Ministry of Finance and FCMC to start working on formation of regulatory sandbox). Available on: <http://www.lafpa.lv/lv/lafpa-rosina-fm-un-fktk-uzsakt-darbu-pie-regulativas-smilsu-kastes-izveides/>. Accessed November 26, 2017.

<sup>130</sup> *Supra* note 123. p. 9.

<sup>131</sup> *Ibid.* p. 24

<sup>132</sup> *Ibid.*

<sup>133</sup> *Ibid.* p. 26.

period of last year, when 141 million euro was invested through Latvian platforms, the volume of investments increased nearly threefold.<sup>134</sup>

As set out in the Financial sector development plan for 2017 – 2019, a legal framework has to be adapted for regulation of crowdfunding services providers. On September 9, 2017 Ministry of Finance announced the co-funding services bill<sup>135</sup> in the meeting of state secretaries. The bill lays down rules and requirements for the provision of peer-to-peer (P2P) lending services. Although the draft legal framework has just begun its procedure to official approval from the government, the scope of it can be viewed already now. Gints Āboltniņš, the director of AFSAL, has already supported it with a following opinion:

“By significantly increasing performance indicators each quarter, Latvian peer-to-peer lending platforms have made a name for Latvia as an industry leader in Europe’s financial technology services market. However, the co-financing platform draft law currently announced in the State Secretaries’ meeting will be critical to future growth and development. Businesses in the industry welcome the Finance Ministry’s project, which is intended to cover all market participants, creating a regulatory framework for the deployment and administration of credit claims on co-financing platforms.”<sup>136</sup>

According Āboltniņš, the law clearly defines the requirements for different types of platforms within a single regulatory act, which could become the best practices example in Europe, where many countries have not even begun to work on regulatory framework in this field.<sup>137</sup> To summarize, the bill mainly governs the following areas:

- how a service provider can be registered and start operating;
- general requirements for the service provider’s operations;
- requirements for the service provider’s shareholders and officials;
- capital requirements and distribution of profits;
- contractual relationships between service providers and administration of payments;
- protection of investors’ interests;
- preventing conflicts of interest;
- FCMC supervisory functions;
- information to be provided to the FCMC and advertising restrictions;
- transition rules designed to help existing service providers switch to the new legal framework.

With the Bill still facing the parliamentary process of legislation, changes are likely to be made to its current version. However, the areas governed and regulated by it can be analysed already now.

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<sup>134</sup> Alternative Financial Services Association of Latvia. 329 million euro funded through Latvia’s peer-to-peer lending platforms in nine months of this year. Available on: <http://www.lafpa.lv/en/329-million-euro-funded-through-latvias-peer-to-peer-lending-platforms-in-nine-months-of-this-year/>. Accessed November 26, 2017.

<sup>135</sup> Latvijas Republikas Ministru kabineta tiesību aktu projekti. Likumprojekts "Kopfinansējuma pakalpojumu likums" (Translation: “Co-funding services bill”). Available on: <http://tap.mk.gov.lv/mk/tap/?pid=40435945>. Accessed November 26, 2017.

<sup>136</sup> *Supra* note 134.

<sup>137</sup> *Ibid.*

To begin with, the current version of bill covers only P2P lending platforms and does not apply to equity crowdfunding.<sup>138</sup> According to European Commission, equity crowdfunding as a source of raising finance is very important for start-up companies.<sup>139</sup> Therefore industry representatives are not supporting such division, where the regulator has planned to reserve the use of equity crowdfunding exclusively for public limited companies.<sup>140</sup> As commented by law firm's Kronbergs Čukste Derling partner Zane Veidemane-Bērziņa, such defect of law would mean startup companies, who decide to use equity crowdfunding, will have to register as public limited companies with a basic share capital of at least € 35 000. Nevertheless, it would probably also require FCMC accept for public offerings as well as prepare a prospectus, if the capital raise exceeds € 100 000.<sup>141</sup> According Veidemane-Bērziņa, if the regulator will not make any changes in current version, equity crowdfunding in Latvia most probably will not exist. To add, a lesson should be learned from Italian regulator regime on equity crowdfunding, which has been criticized by many scholars, describing it as “ill-crafted and to a large extent bound to generate significant operational dysfunctions.”<sup>142</sup>

In essence, the scope of co-financing service offered by platform operators has been described in Article 1 of the bill in following definitions:

- a) service, where an investor lends money to a borrower which is a natural person;
- b) service, where an investor lends money to a borrower to develop its submitted project;
- c) investment service, where an investor receives debt or equity security emitted by the borrower as a legal person;
- d) credit claim offerings through a platform as well as service and administration of them.

Furthermore, the bill lays down rules for the legal status of co-financing service providers, procedures for licensing and supervising them stipulating that a co-funding service provider may start operation in Latvia once it has been entered on the register of co-funding service providers maintained by FCMC. Thus, FCMC will be responsible for registering co-funding service providers and supervising their operations, on the contrary to non-bank credit service providers who are registered and supervised by Consumer Rights Protection Centre (CRPC). Such delegation has been appreciated by the industry.<sup>143</sup>

In order for the co-financing service provider to be eligible for registration by FCMC, the bill imposes a € 50 000 basic share capital requirement as described in Article 11(1). However, opinions on the suggested share capital level differ. Some claim, that € 50 000 can serve as a barrier for “wannabes” wanting to offer investment services without sufficient own capital, but at the same time the suggested amount is relatively small sum to protect customer interests in case

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<sup>138</sup> Jānis Gavars. Pirmais ieskats Kopfinansējuma pakalpojumu likumā (Translation: First glance at Co-Funding Services Bill). PricewaterhouseCoopers. Available on: [https://www.mindlink.lv/lv/aktuali/kopfinansejuma\\_likums/](https://www.mindlink.lv/lv/aktuali/kopfinansejuma_likums/). Accessed November 25, 2017.

<sup>139</sup> *Supra* note 41.

<sup>140</sup> Anda Asere, Žanete Hāka, Progresīvs, bet ar dažiem trūkumiem (Translation: Progressive, but with some defects). *Dienas Bizness*, November 14, 2017. p. 10.

<sup>141</sup> *Ibid.*

<sup>142</sup> Antonio Nigro, Casimiro & Santoro, Vittorio, “The Quest for Innovative Entrepreneurship and the Italian Regime for Equity Crowdfunding”. *European Company Law* 11, no. 5 (2014), p. 230.

<sup>143</sup> *Supra* note 140.

of platform's financial problems.<sup>144</sup> In addition, the regulator supports it with the fact that other financial market participants have relatively higher minimum capital requirements. To put it differently, € 50 000 would be a huge sum for a startup FinTech, therefore the presence of regulatory sandbox approach becomes crucial in order not to lose innovations due to the share capital threshold. However, what happens if other EU member states will set the minimum capital requirement lower? To point out, such competition among rules has been already experienced in relation to limited liability company minimum capital requirements, triggering the race to the bottom. Needless to say, it is now possible to register the so called € 1 company in every EU member state. So does the minimum capital requirement really protects investors, even though it has proven to be inefficient in case of insolvency and creditor protection?<sup>145</sup>

The bill also outlines payments intended to finance the FCMC operations. Article 31(1) prescribes a registration duty of € 4 000, but Article 31(2) stipulates the calculation of annual duty consisting of base € 7 000 plus up to 1,4% of the co-funding service provider's gross annual revenue related to service providing, however the sum of both shall not exceed € 100 000. Assuming that successful FinTech companies can generate substantial revenues, in theory the suggested annual duty does not seem to put pressure on them, but in practice they can again lead companies to choose the least expensive regime for operation. To bear in mind, FinTech as a developing sector requires continuous investments into the business model, IT solutions and overall efficiency, therefore regulator should be careful not to hinder it. For this reason, Eduards Lapkovskis, CEO of a Latvian P2P platform VIA Invest, has already rated the duty as rather high<sup>146</sup>. On the other hand, in any company's interests would be to avoid such duties in order to maximize their earnings, so industry's opinion raises doubt on its objectivity level.

With regards to the scope of peer-to-peer relationship, it is important to note that the bill changes the usual way P2P lending platforms operate, with claim rights being offered for investors to purchase (by entering into an assignment agreement) relating to loans already made to borrowers. According to the proposed rules in the bill, P2P lending services will be provided without assignment of claims. Instead, an investor will enter into a special agreement with a co-funding service provider, under which the investor transfers funds to the co-funding service provider in order to have those issued to a funding recipient chosen by the investor, or to finance the funding recipient by acquiring the lender's credit claims and issuing funds to the lender in return for the credit claims acquired by the investor.<sup>147</sup>

At the same time the bill takes into account risks associated to transfer of investor funds to the platform. The bill provides for several provisions on investor safeguarding:

- investor funds need to be separated from the platform operator's operating accounts, ensuring that the money received from investors is stored in a separate account;

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<sup>144</sup> *Ibid.*

<sup>145</sup> Jan-Jaap Kuipers, *EU law and private international law: the interrelationship in contractual obligations* (Leiden; Boston: Martinus Nijhoff Publishers, 2012), p. 261.

<sup>146</sup> *Supra* note 140.

<sup>147</sup> *Supra* note 138.

- necessity to carry out due diligence on the funding receiver in order to assess its solvency as well as ensuring that the borrower co-finances his loan for at least 10 % of the loan amount;
- platform operator has to collect information about the investor's financial stability, experience and education in entering in such agreements and inform about risks in case of investor's incompetency;

Among other things, co-funding service providers are subject to limitation on how much investors' funding they are permitted to raise for a single funding recipient. The total funding cannot exceed the following amount over 12 months:

- € 10 000 where an investor lends money to a borrower which is a natural person;
- € 100 000 where an investor lends money to a borrower to develop its submitted project.

The limitation related to borrowers as natural persons is understandable due to the fact that the regulator does not want to support unlimited borrowing by ordinary people for consuming purposes. However, in the second case where the fund receiver's intention is to develop a project, the limit is totally prohibiting to co-finance projects seeking for a bigger investments like real estate development. With such provision, the regulator clearly bans the opportunity of crowdfunding real estate projects in need of more than € 100 000 over 12 months. However, almost every Crowdestate's or Estateguru's crowdfunded loan is exceeding this limit. Bulkestate as a still developing platform has mostly issued loans qualifying under this limit, but it would be more effective to issue larger loans resulting in higher platform commission fees. It can be concluded that the restriction of investment amount can avoid Bulkestate to register their company under Latvian law.

## 4.2. Estonian approach

Crowdfunding is gathering more and more popularity in Estonia, but is still not directly regulated by any national laws.<sup>148</sup> Regulatory bodies of Estonia, namely the Ministry of Finance and Financial Supervision Authority (FSA), have so far kept their distance on crowdfunding, leaving the sector at a self-regulatory status. In May 2016, FinanceEstonia, a public-private financial sector cluster organization consisting of members like law offices, advisory firms and Estonian crowdfunding companies, has approved and published Estonian Crowdfunding Code of Conduct.<sup>149</sup> Ministry of Finance and FSA took active part of creating the requirements. The Crowdfunding Code of Conduct is a collection of rules and principles to serve as a best practice for crowdfunding service providers. The requirements are made to protect the interests of the investors and to ensure the transparency of the crowdfunding business.

The Code of Conduct can be viewed as a soft law, meaning that it does not have any legally binding force, but it shows the attitude of industry striving for legal certainty. On one hand, this is

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<sup>148</sup> Crowdestate blog. Crowdfunding Code of Conduct created in Estonia. Available on: <https://blog.crowdestate.eu/en/2016/uhisrahastusportaalide-tegevuse-reguleerimiseks-loodi-hea-tava/>. Accessed November 28, 2017.

<sup>149</sup> FinanceEstonia. Best Practice for Crowdfunding. Available on: <http://www.financeestonia.eu/wp-content/uploads/2016/02/Crowdfunding-Best-Practice.pdf>. Accessed November 28, 2017.

a welcome initiative and shows the deep insight of industry of maintaining sustainable relationships between all involved parties. On the other hand, it can take the form of lobbying industry's interests, and if so – it has been very successful.

The platforms complying with the provisions of Code of Conduct are awarded with a trust badge. Platforms are asked to follow the principle of “comply or explain”, meaning that the public shall be notified on its website whether the rules set out in the Code of Conduct are met or not. In case some of the principles are not followed, the provider shall explain it on its website.

To summarize, the Code of Conduct consists of following Articles:

- management of investor funds;
- data protection;
- compliance with Estonian Money Laundering and Terrorist Financing Prevention Act;
- quality of information about the investment;
- risk warning;
- consumer protection and advertising;
- avoiding conflicts of interest and remuneration system;
- sustainability of the activities;
- reporting of crowdfunding performance over past year;
- dispute resolution;
- provisions on joining the Best Practice and compliance with it.

In Article 1 regarding the management of investor funds the Code of Conduct sets out rules on the separation of such funds from the platforms own assets, e.g. in a special bank account. The same applies to money transferred from the borrower for the purpose of making distribution of repayments. The measures of anti-money laundering and implementation of international sanctions point out the need to comply with Estonian regulations on this matter or at least follow the requirements provided in the Best Practice on collecting accurate personal information, bank account numbers and conducting activities to paying attention on unusual situations with money laundering suspicions.

Article 4 is dedicated to information standards related to investment offerings stipulating that the platform shall make available only correct, clear and non-misleading information, thus safeguarding the investors from “too much decorated” campaigns. Pursuant to Article 5, platforms are obliged to make available on their websites information on general risks related to the investments made through the crowdfunding platform.

An interesting provision is laid out in Article 6 regarding consumer protection and advertising stipulating that a “cooling-off” period should be allowed for the potential investors after having made the investment decision, meaning that they should have the possibility to reconsider and also annul their decision. Under Article 7 regarding conflict of interest avoidance and remuneration system the rules ask the platform to publish information about its shareholders, management board and employees or any other persons capable of influencing the activities or economic results of the platform. It also stipulates that platforms need to publish information about the applicable fees for its services, both for investors and borrowers. In case of emergency resulting in termination of platform's operation, Article 8 stipulates that the platform shall have

an agreement with a legal persons of taking over the administration of it. In practice, these legal persons are law offices, which would then continue the administration of repayments and distribution of investors' funds. For making the process easier, there is a provision that the platform must develop a recovery plan for such cases.

Another interesting point is described in Article 9 regarding reporting of financial results of the previous year. It stipulates that such report must be published on platform's website no later than 2 months after the end of each year, and it must contain information about campaigns conducted, putting an accent on forecasted investment returns and the actual results. However, such information will be available only for loans which have been repaid already during that financial year. Moreover, the annual return derived from early repaid loans, which have not yet matured, will be misleading. The Code of Conduct is finalized with provisions on dispute resolution and joining the Best Practice.

Few months later the Code of Conduct was followed by a more official document proposed from the FSA. On 22 September 2016, FSA sent to the Estonian Ministry of Finance a proposal to consider a law regulating the activity of companies offering crowdfunding services.<sup>150</sup> In the FSA's opinion the crowdfunding area needs a bigger legal certainty. The risks need to be managed on a law level in order to protect the savings of persons who have invested into crowdfunding companies as well as to give clarity in the activity environment of companies. Supervisor's position is explained in the following quote by Andre Nõmm, a Member of the FSA Management Board:

Rapidly developing crowdfunding offers new and alternative opportunities next to the regulated banking, fund and investment services market. With financial services, the opportunities and risks go hand in hand. We believe that by addressing the activity requirements and risks more directly through laws helps to create a more transparent, stable and effective financial services market.

As stated in the report, crowdfunding companies are currently not subjects of financial supervision and according to this proposal by the FSA, for the time being, they should not be put under national financial supervision either. In addition, crowdfunding companies do not need an authorisation from the FSA. It believes, that the crowdfunding model should be considered as intermediation of offering investment services. Most of the crowdfunding companies operating in Estonia offer investment opportunities into legal entities and do not provide financing in their own name, but are connecting the peers directly to the borrower. In addition, there are a number of nuances in the crowdfunding operating model, therefore they generally do not fall into scope of the special financial sector laws, e.g. the Credit Institutions Act, the Securities Market Act, the Creditors and Credit Intermediaries Act, the Investment Funds Act. The FSA points out that contrary to market participants who have an authorization to offer financial services, crowdfunding companies are not subjects of national financial supervision, they do not have to apply for an authorization and they are not applicable to guarantees stipulated in the Guarantee Fund Act. However, it cannot be denied that in the future the crowdfunding area may need to be regulated more firmly in case the risks become higher or the EC passes union-wide legislation.

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<sup>150</sup> *Supra* note 72.

Same as Latvian approach, FSA distinguishes between financial and non-financial return crowdfunding, where the last should be governed by Non-profit Associations Act. The initiative does not exclude equity crowdfunding from its scope. It points out that many member states, which have already passed crowdfunding legislation, have distinguished between non-professional and professional investors. In some cases, this division also concerns restrictions on allowable investment amounts. On contrary, FSA initiative currently does not impose such restrictions, but it is not excluded from future discussion.

The primary aim of this initiative is to protect the clients of crowdfunding companies. To summarize, the proposals by the FSA are mostly related to following aspects:

- the disclosure and transparency of information;
- protection of personal data;
- management of conflicts of interests;
- separation of assets;
- prevention of money laundering.

In General Provisions chapter the initiative draft is describing its scope of application and definitions used. It is followed by Chapter II related to the protection of crowdfunding platform users. Paragraph 5 sets out the requirements for separation of assets. Furthermore, it stipulates that the investors' funds received for the purpose of being invested in crowdfunding campaigns cannot be included in the crowdfunding platform's insolvency proceedings. Paragraph 6 lays out the requirements for platforms to perform anti-money laundering actions including personal information collection, confirming the actual beneficiary of the investment and interest and in case of suspicions – duty of informing the relevant departments. Avoidance of conflict of interest is described in Paragraph 7, pointing out that the platform's shareholders and leading employees are not allowed to own or acquire financial interest from a borrower. Moreover, the draft stipulates that they are also not allowed to participate as investors in the crowdfunding campaigns. This provision has already called for sector's critique, emphasizing that having "your own skin in the game" actually adds more trust to the platform, as the owners and employees are believing in their offerings.<sup>151</sup>

Requirements on the information quality about investments are described in Paragraph 8, including notification about risks related to crowdfunding. It also stipulates, that investments in crowdfunding campaigns are neither subject to Securities Market Act, nor Guarantee Fund Act, and the platform has the duty to inform their customer about this fact. Similar to the Best Practice, the FSA initiative also includes provisions on customer data protection, sustainability of platform's activities and duty of reporting of financial results. Contrary to the Best Practice, the draft law requires reporting each quarter.

According Nõmm, the proposed draft law helps to frame the coming discussions on regulating crowdfunding where a balanced result in an open and inclusive way can be reached.<sup>152</sup> He adds, that crowdfunding market in the EU should be opened, because it is a good opportunity to open

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<sup>151</sup> Urmo Andressoo, Äripäev, Ühisrahastuste juhid arvustavad seaduse kava (Translation: Crowdfunding platform CEO's review the law initiative). Available on: <https://www.aripaev.ee/uudised/2016/09/22/uhisrahastuse-juhid-regulatsioonitoorikus-nii-head-kui-halba>. Accessed November 29, 2017.

<sup>152</sup> *Ibid.*

the potential of the single market for Estonian entrepreneurs.<sup>153</sup> Industry representatives claim that the draft law is very similar to the Best Practice set of rules, however they complain about too bureaucratic approach by FSA.<sup>154</sup> It is also concerning the detailed reporting as often as each quarter, which according to Loit Linnupõld, founder of Crowdestate, could cost the platform to hire an employee especially for this purpose. Pärtel Tomberg, founder and CEO of Bondora, commented that tax law should be amended in favour to investment in Estonian crowdfunding campaigns, because this model promotes local investment where the money is not leaving Estonia, unlike investing in foreign markets.<sup>155</sup> Marek Pärtel, CEO of Estateguru, commented that the initiative to regulate crowdfunding in national law is supported, but more attention should be paid to increasing peoples' understanding about crowdfunding's benefit to local economy. "The money deposited in accounts of Swedish banks or which is being invested in foreign securities, does not reach the Estonian economy," he said.<sup>156</sup>

The case analysis of Estonian approach shows less strict regulator intervention, letting the industry to self-regulate. Such regulator attitude has actually attracted Latvian real estate crowdfunding platform to migrate to Estonia and perform its activities as an Estonian legal entity. Estonians seem to have a hybrid regulatory sandbox regime organized by public-private sector cluster organization. The absence of investor claims against Estonian crowdfunding platforms proves that it works well, even not being supervised by FSA. Can it be that the "less is more" approach for crowdfunding regulation can actually help it to develop faster? At least in real estate crowdfunding this has proven true.

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<sup>153</sup> *Ibid.*

<sup>154</sup> *Supra* note 151.

<sup>155</sup> *Ibid.*

<sup>156</sup> *Ibid.*

## CONCLUSIONS

Crowdfunding represents a novel way for real estate developers to raise capital for projects. It also offers the ordinary people to invest small amount of money in directly chosen projects and earn reasonable returns. The thesis statement was that **due to Latvia's regulatory issues Latvian real estate crowdfunding platform has not developed as successfully as the ones in Estonia.**

The case analysis of each platform gave insight about the real estate crowdfunding volume in the Baltics. 75 % of the campaigns are Estonian projects. In terms of investment value Estonian projects raised 83 %, it is supported by the fact that Estonians perform on average a higher investment. Latvian and Lithuanian projects are accounting for similar parts, however Latvia is a little bit ahead.

Case analysis of Bulkestate platform actually shows low relation to real estate development. Purpose for most of the loans is not related to real estate development. In most cases real estate only serves as a collateral for securing the loan. Bulkestate has been able to offer the highest annual returns on fully secured loans compared to Estonian platforms. On average, the LTV ratio is lower than on Estonian platforms as well. If Bulkestate will be able to continue offering loans with 14-15 % annual interest, it has a good chance to attract more and more investors who are not appreciated with lower rates offered by Estonian platforms.

Crowdestate is the most advanced platform, as it offers both debt and equity crowdfunding. It is also offering unsecured loans, and people are still investing in such loans with big activity. Crowdestate has the highest average loan amount per campaign. Many of crowdfunding campaigns are not related to real estate at all.

Crowdfunding through Estateguru has been mostly used for real estate development projects in all countries, however around 17 % of the projects are related to other business. Estonian projects are having much higher average individual investment than projects in Latvia or Lithuania.

In terms of market share, Estateguru is the biggest platform accounting for 64 % of the total real estate crowdfunded loans' value in Baltics. It is followed by the other Estonian platform Crowdestate, which has 33,7 % market share, but the Latvian Bulkestate takes the remaining part of 2,1 %. Bulkestate's 2018 plan of reaching € 3 million threshold on funded loans could help to establish a more considerable market share, however the two competitors will also be expanding at a significant pace.

From all crowdfunded loans, more than 81 % have been transferred to Estonian projects, 14 % to Latvian, but 5 % have been invested in Lithuanian projects. If compared to Estonian activity, Latvia still holds a huge potential for real estate crowdfunding.

The proposed law on co-financing services in current version is not supporting real estate crowdfunding platforms to register in Latvia due to high minimum capital requirements, restrictions on investment limits into a single project. It is also not applying to equity crowdfunding meaning that in the form of current regulatory approach equity crowdfunding in Latvia probably will not exist. Thus, it can be concluded that the current version of co-financing service bill will not fully support the Latvian government's action plan on unlocking capital for SMEs through alternative financial sources like crowdfunding.

The case analysis of Estonian platforms suggest that Estonian regulator approach has been more effective for the development of real estate crowdfunding platforms. Estonians have a hybrid regulatory sandbox regime organized by public-private sector cluster organization. The absence of investor claims against Estonian crowdfunding platforms proves that it works well, even not being supervised by FSA. It can be concluded that the “less is more” approach for crowdfunding regulation can actually help to develop it faster.

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## APPENDICES

Appendix 1: Estageguru 2017 crowdfunding campaigns data table.\* Source: Estageguru.co.

\*Gray filled cells indicate that the borrower is adding 1% bonus annual interest for investors committing a larger investment (usually starting from € 10 000).

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
1	Ravi st development - 3.stage	Development	29 000	12	10,00%	67%	86	337,21	EE
2	Lauka development	Development	67 300	12	11,00%	60%	184	365,76	EE
3	Miiduranna villa development	Development	650 000	18	10,00%	59%	479	1 356,99	EE
4	Pärnu bridge loan	Purchase	77 000	12	10,00%	63%	245	314,29	EE
5	Metsmaaker OÜ refinancing loan	Refinancing	160 000	18	11,00%	46%	335	477,61	EE
6	Refinancing of Raudtee st renovation loan	Development	50 000	12	11,00%	59%	184	271,74	EE
7	Aardla 15 bridge loan 2st phase	Development	95 000	12	12,00%	58%	236	402,54	EE
8	Luha 13 business loan	Other business development	30 000	18	10,00%	59%	122	245,90	EE
9	Edinburgas development loan - 1.stage	Development	192 600	12	10,50%	58%	560	343,93	LV
10	Tsirgu business loan	Other business development	30 000	12	11,00%	57%	118	254,24	EE
11	Pargi bridge loan - 1.stage	Development	480 000	18	11,75%	69%	669	717,49	EE
12	Hansu st business loan	Development	200 000	18	10,50%	44%	277	722,02	EE
13	Kirilase street 6 refinancing loan	Development	350 000	12	11,50%	67%	469	746,27	EE
14	Laineoru development loan 1. phase	Development	300 000	12	11,00%	61,00%	513	584,80	EE

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
15	Pühavaimu development loan I.stage	Development	172 000	18	10,75%	60%	441	390,02	EE
16	Liivaku business loan	Development	40 000	12	8,00%	22%	177	225,99	EE
17	Veju development loan	Development	80 000	18	10,00%	60%	266	300,75	LT
18	Paldiski mnt 38b refinancing loan	Refinancing	91 967	12	10,00%	48%	306	300,55	EE
19	Pivarootsi bridge loan	Refinancing	450 000	12	11,00%	34%	586	767,92	EE
20	Sarra st business loan	Development	175 000	9	11,00%	53%	389	449,87	EE
21	Harju-Risti business loan	Other business development	22 000	24	11,00%	39%	96	229,17	EE
22	Kuljuse st bridge loan	Refinancing	325 000	12	11,50%	72%	493	659,23	EE
23	Säina st bridge loan	Development	135 000	12	11,00%	69%	385	350,65	EE
24	Nova apartment buy-to-let loan	Purchase	111 500	12	11,00%	69%	212	525,94	EE
25	Kose development loan	Refinancing	70 000	18	11,00%	53%	230	304,35	EE
26	Adrenalin Arena bridge loan	Development	460 000	12	11,00%	35%	584	787,67	EE
27	Tööstuse 3c renovation loan	Development	180 000	18	11,50%	50%	346	520,23	EE
28	Suur-Sepa bridge loan- 2. stage	Development	100 000	12	9,50%	49%	256	390,63	EE
29	Ristikü st development loan	Development	100 000	12	11,50%	68%	270	370,37	EE
30	Ardu business loan	Other business development	62 000	24	11,00%	44%	149	416,11	EE

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
31	Vahulille st development loan - 1.stage	Development	110 400	12	10,25%	69%	195	566,15	EE
32	Tamme bridge loan refinancing	Development	395 000	12	12,50%	56%	463	853,13	EE
33	Rapla business loan	Other business development	100 000	24	11,00%	47%	270	370,37	EE
34	A. Haava bridge loan	Development	155 000	12	11,00%	67%	436	355,50	EE
35	Pootsi motgage loan	Other business development	40 000	24	10,75%	65%	192	208,33	EE
36	Pääsusilma st bridge loan	Other business development	21 000	18	10,50%	35%	155	135,48	EE
37	Tehnika st bridge loan	Development	45 000	18	11,00%	62%	212	212,26	EE
38	Vairoga street mortgage loan - 1.stage	Development	43 000	12	10,00%	66%	207	207,73	LV
39	Pärna 33a development loan - 1.stage	Development	233 000	18	11,50%	68%	468	497,86	EE
40	Strelnieku Business Loan - 1. stage	Other business development	250 000	18	11,00%	39%	436	573,39	LV
41	Melleni Business Loan	Other business development	50 000	18	11,00%	56%	137	364,96	LV
42	Veju development loan - 2.stage	Development	29 200	15	10,00%	60%	119	245,38	LT
43	Madara 14 refinancing loan	Refinancing	275 000	18	12,00%	60%	466	590,13	EE
44	Žiburių 16 development loan - 1.stage	Development	76 700	12	10,00%	65%	304	252,30	LT
45	Õismäe bridge loan	Development	30 000	12	10,00%	49%	128	234,38	EE
46	Žiburių 16 development loan - 2.stage	Development	42 250	12	10,00%	65%	194	217,78	LT

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
47	Strelnieku Business Loan - 2. stage	Other business development	75 000	18	11,00%	39%	258	290,70	LV
48	Laineoru development loan 2. phase	Development	350 000	12	11,00%	61%	436	802,75	EE
49	Kaupmehe st 4 bridge loan	Other business development	75 000	12	8,50%	67%	267	280,90	EE
50	Tuukri st bridge loan	Other business development	125 000	12	9,00%	68%	291	429,55	EE
51	A.H. Tammsaare st 93 business loan	Other business development	200 000	24	10,00%	58%	419	477,33	EE
52	Uusküla development refinancing loan	Development	75 000	12	11,75%	51%	247	303,64	EE
53	Hansu st development loan - 1.stage	Development	310 000	13	11,00%	62%	568	545,77	EE
54	Veskimöldre II development - 1.stage refinancing loan	Development	350 000	12	11,00%	56%	602	581,40	EE
55	A.Haava 7 reconstruction loan - 1.stage	Development	200 000	12	11,50%	60%	434	460,83	EE
56	Pamiškės development loan	Development	117 000	12	10,00%	65%	350	334,29	LT
57	Veskimöldre commercial land plots bridge loan - 1.stage	Development	295 000	12	11,00%	43%	383	770,23	EE
58	Katusepapi refinancing loan	Development	240 000	12	10,50%	36%	360	666,67	EE
59	Artillerijas 19/2 Īstermiņa	Development	60 000	12	10,00%	53%	193	310,88	LV

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
	Aizdevums								
60	Jūri refinancing loan	Refinancing	75 000	18	10,00%	65%	240	312,50	EE
61	Kaunas townhouse bridge loan	Development	356 562	18	11,00%	54%	587	607,43	LT
62	Kuninga str bridge loan	Development	120 000	18	11,00%	63%	311	385,85	EE
63	Riia rd. development loan - 1.stage	Development	487 500	18	12,00%	75%	586	831,91	EE
64	Pringi business loan	Other business development	250 000	24	11,50%	55%	508	492,13	EE
65	Elmo Rent 2.0 bridge loan	Other business development	75 000	12	11,00%	71%	273	274,73	EE
66	Aardla 15 bridge loan 3rd phase	Development	60 000	12	12,00%	58%	233	257,51	EE
67	Vardi street refinancing loan	Development	72 000	12	12,00%	50%	221	325,79	EE
68	Audru business loan	Purchase	30 000	36	11,00%	41%	141	212,77	EE
69	A.Haava 7 reconstruction loan - 2.stage	Development	70 000	12	11,50%	60%	238	294,12	EE
70	Kr. Valdemara 34 flip loan	Purchase	140 000	14	12,00%	73%	302	463,58	LV
71	Kr. Valdemara 34 purchase loan	Purchase	179 033	24	11,00%	73%	402	445,36	LV
72	Pringi business loan 2. stage	Other business development	184 004	24	11,50%	55%	474	388,19	EE
73	Drustu 7b Development Loan 1. stage	Refinancing	32 000	18	10,50%	55%	152	210,53	LV
74	Magdaleena 3 bridge loan	Other business development	160 000	12	10,00%	68%	339	471,98	EE

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
75	Šarkuvos development loan - 1.stage	Development	143 000	12	11,00%	58%	469	304,90	LT
76	Veskimöldre II development - 2.stage refinancing loan	Development	194 000	12	11,00%	56%	376	515,96	EE
77	Veskimöldre terraced houses bridge loan I	Development	250 000	12	11,00%	60%	400	625,00	EE
78	Pruuna business loan	Purchase	116 000	24	11,00%	65%	336	345,24	EE
79	Bajoru kvartalas development loan	Development	203 000	12	11,00%	55%	479	423,80	LT
80	Riiasöödi street development loan- 1.stage	Development	74 000	12	11,00%	66%	198	373,74	EE
81	Pakase 47 bridge loan	Development	156 000	12	11,00%	66%	265	588,68	EE
82	Männiku road development loan 1. stage	Development	150 000	12	11,00%	43%	431	348,03	EE
83	Aianduse bridge loan	Development	120 000	12	10,00%	48%	311	385,85	EE
84	Järvakandi mortgage loan	Other business development	27 731	36	10,00%	28%	160	173,32	EE
85	Järveküla bridge loan 1. stage	Development	40 000	12	10,50%	31%	156	256,41	EE
86	Laineoru development loan 3. phase	Development	150 000	12	11,00%	61%	348	431,03	EE
87	Kose development loan 2. stage	Development	20 000	18	11,00%	53%	103	194,17	EE
88	Soontevahe street construction loan	Development	110 000	12	11,00%	63%	397	277,08	EE

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
89	Jüri Sewing Factory business loan	Development	135 000	18	11,00%	62%	337	400,59	EE
90	Tiskre residences development loan I	Development	57 000	12	11,00%	58%	244	233,61	EE
91	Veskimöldre terraced houses bridge loan II	Development	250 000	12	11,00%	60%	406	615,76	EE
92	Pärna 33a development loan - 2.stage	Development	183 000	14	11,50%	68%	398	459,80	EE
93	Komeedi street business loan	Other business development	45 000	36	9,00%	30%	175	257,14	EE
94	Vesivärava st house reconstruction loan	Development	105 000	12	12,00%	72%	211	497,63	EE
95	Tuigo street development loan	Development	130 000	12	11,00%	67%	302	430,46	EE
96	Veskimöldre commercial land plots bridge loan - 2.stage	Development	180 000	12	11,00%	43%	347	518,73	EE
97	Soontevahe street construction loan - 2.stage	Development	22 500	12	11,00%	63%	163	138,04	EE
98	Pringi business loan 3. stage	Other business development	66 000	24	11,50%	55%	156	423,08	EE
99	Pamiškės development loan II	Development	76 000	12	11,00%	69%	304	250,00	LT
100	Artilerijas 19/2 Bridge Loan II	Development	165 000	12	11,00%	59%	369	447,15	LV
101	Suur - Posti st reconstruction loan - 1.stage	Development	125 000	12	11,00%	54%	308	405,84	EE
102	Valmiera Development	Development	20 000	12	11,50%	50%	131	152,67	LV

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
	Loan								
103	Carnikava Bridge Loan	Development	65 000	12	11,00%	31%	287	226,48	LV
104	Žiburių 16 development loan - 3.stage	Development	28 000	12	11,00%	65%	147	190,48	LT
105	Tiskre residences development loan II	Development	345 000	12	10,50%	57%	615	560,98	EE
106	A.Haava 7 reconstruction loan - 3.stage	Development	30 000	12	10,50%	60%	195	153,85	EE
107	Tiskre residences development loan IV	Development	57 000	12	11,00%	58%	232	245,69	EE
108	Tiskre residences development loan III	Development	57 000	12	11,00%	58%	268	212,69	EE
109	Edinburgas development loan (Jurmala, Latvia) - 2. stage	Development	80 000	12	11,00%	58%	287	278,75	LV
110	Pargi bridge loan - 2.stage	Development	144 000	18	11,00%	69%	390	369,23	EE
111	Bizausko development loan	Development	38 000	12	11,00%	50%	201	189,05	LT
112	Metssea road development loan 2. stage	Development	70 000	12	9,00%	66%	324	216,05	EE
113	Metssea road development loan	Development	70 000	12	9,00%	66%	343	204,08	EE
114	Šarkuvos development loan - 2.stage	Development	25 200	12	11,00%	58%	469	53,73	LT
115	Ozolu st bridge loan - 1st stage	Development	160 000	12	11,00%	49%	488	327,87	LV
116	Kaarepere business loan	Other business	124 000	18	11,00%	60%	388	319,59	EE

#	Campaign	Investment type	Goal	Loan period, months	Interest per annum	LTV	Number of investors	Average investment	Country
		development							
117	Riiasöödi street development loan- 2.stage	Development	103 000	12	11,00%	66%	412	250,00	EE
118	Tehnika 35 development loan	Development	318 000	12	11,50%	69%	530	600,00	EE
119	Liepaja development loan	Development	67 000	12	11,00%	44%	290	231,03	LV
120	Soku street 18 development loan - 1.stage	Development	66 500	12	11,00%	65%	285	233,33	EE