# EQUITY CROWDFUNDING IN NEW ZEALAND: THE ROLE OF INCOME TAX INCENTIVES

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## ABSTRACT

Equity crowdfunding facilitates companies' access to capital, particularly for start-ups. In New Zealand, light-handed regulation and a syndication model have contributed to the growth of equity crowdfunding. This article analyses the effects of income tax legislation on crowdfunding in New Zealand and considers how — and whether — amendments to income tax legislation could further promote this form of private investment. This paper argues that dissonance exists between financial markets policy on crowdfunding and tax policy on research and development. In the context of dire predictions for Covid-19-related job losses, the potential for crowdfunding to promote start-ups, and to create jobs, deserves tax policymakers' attention.

**Keywords:** equity crowdfunding, R&D, return on investment, tax incentives

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## I INTRODUCTION

'Crowdfunding' is a means 'of funding a project or venture by raising money from a large number of people, each of whom contributes a relatively small amount, typically via the internet'.[1] Crowdfunding arose from the confluence of internet-based technology, including the rise of social media, and the need for small businesses to raise capital in the wake of the Global Financial Crisis ('GFC'). Bradford identifies five models for crowdfunding: the donation model; the reward model; the pre-purchase model; the lending model; and the equity model.[2] Relevantly, this article is concerned with raising equity capital through crowdfunding.

Securities laws commonly allow wealthy investors, who are presumed to be capable of assessing the risks of a venture, to buy shares in a company without the usual stringent consumer protections applying. Exemptions typically require a minimum investment amount or certification that the investor is wealthy or experienced.[3]

In the United States, in the wake of the GFC, start-ups experienced a pressing need for new sources of capital, since banks were generally unwilling to lend — even to well-established companies.[4] Furthermore, the market shunned initial public offerings.[5] Crowdfunding proponents argued that, if new ventures had better access to capital funding, they would be able to create jobs. Indeed, research showed that in the United States, new firms (as a class) added an average of three million jobs in their first year, while older companies lost one million jobs annually.[6] Lawmakers, therefore, envisaged crowdfunding as a means of revitalising the American economy, principally through job creation. However, if capital for start-ups was to be crowdfunded, securities laws needed to be relaxed. The *Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act of 2012* ('*CROWDFUND Act*'), which forms part of title III of the omnibus *Jumpstart Our Business Startups Act of 2012*, Pub L No 112-106 ('*JOBS Act*') attracted rare bipartisan support and was enacted on 5 April 2012. The *CROWDFUND Act* opened up the market for crowdfunding intermediaries as registered funding portals to facilitate equity

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1 The *Oxford English Dictionary* (online ed).

2 C Steven Bradford, 'Crowdfunding and the Federal Securities Laws' (2012) *Columbia Business Law Review* 1, 14–15.

3 See, eg, the concept of an 'accredited investor' in the United States (*Securities Act* 15 USC § 77a; s 2(a)(15) of the *Securities Act of 1993*); a 'sophisticated investor' in Australia (*Corporations Act 2001* (Cth) s 708); and 'high net wealth investors' and 'sophisticated investors' in the United Kingdom's (Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (UK) arts 50, 50A).

4 'Many Scrappy Returns', *The Economist* (United Kingdom, 19 November 2011) 36.

5 See John C Coffee, 'Statement of Professor John C Coffee, Jr, Adolf A Berle Professor of Law Columbia University Law School at Hearings Before the Senate Committee on Banking, Housing and Urban Affairs, 'Spurring Job Growth Through Capital Formation While Protecting Investors', United States Senate (Washington DC, 1 December 2011) 1–3.

6 See Tim Kane, 'The Importance of Startups in Job Creation and Job Destruction' (Foundation Research Series, Kauffman, July 2010) 2.

offers by start-ups.[7] A non-accredited investor could invest up to the lesser of 10 per cent of their annual income or USD10,000 in start-up equity. Companies seeking crowdfunding investment had to register with the Securities and Exchange Commission and restrict this method of financing to USD1 million per year or USD2 million, if they issued audited financial statements.[8]

In the United Kingdom, a private company must not offer shares to the public[9] and an offer of shares by a public company must normally be accompanied by a detailed prospectus,[10] which is expensive to prepare. However, successive governments have promoted angel investment by wealthy investors,[11] particularly through generous tax concessions.[12] Equity crowdfunding is permitted if: the total amount sought from investors is less than EUR5 million (in a 12-month period); the offer is made to qualified investors only or fewer than other 150 persons; or the minimum investment is EUR100,000 per person.[13]

Job creation was not a stated policy purpose for permitting equity crowdfunding in New Zealand; rather the goal was to extend the narrow scope of exemptions under the extant *Securities Act 1978* (NZ), in order to provide small firms with better access to capital.[14] However, in a post Covid-19 context, when as many as 120,000 job losses are predicted for New Zealand,[15] the role of crowdfunding in promoting start-ups and potentially creating jobs deserves more policy attention.

Despite starting later than the United Kingdom and the United States, according to Schwartz,[16] New Zealand has become a global leader in equity crowdfunding since the

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7 JJ Colao, 'Breaking Down the JOBS Act: Inside the Bill that Would Transform American Business', *Forbes* (online, 21 March 2012).

8 'Spotlight on Jumpstart Our Business Startups (JOBS) Act', *Securities Exchange Commission* <https://www.sec.gov/spotlight/jobs-act.shtml>.

9 *Companies Act 2006* (UK) s 755.

10 *Financial Services and Markets Act 2000* (UK) s 85.

11 An angel investor is 'a person who provides capital, in the form of debt or equity, from his own funds to a private business owned and operated by someone else, who is neither a friend nor a family member'. See Scott A Shane, *Fool's Gold?: The Truth Behind Angel Investing in America* (Oxford University Press, New York, 2008) 14.

12 See Part IV C of this paper for a discussion of the United Kingdom tax incentives for angel investors.

13 'Policy Statement PS14/4: The FCA's Regulatory Approach to Crowdfunding Over the Internet, and the Promotion of Non-Readily Realisable Securities by Other Media, Feedback to CP13/13 and Final Rules' *Financial Conduct Authority* (Report, March 2014) <https://fca.org.uk/publication/policy/ps14-04.pdf>.

14 Ministry of Economic Development, 'Review of Securities Law Discussion Paper' (Report, June 2010) 47–49 <https://www.mbie.govt.nz/assets/f56be9b821/review-of-secuities-law-dicsussion-document.pdf>.

15 See, eg, Patrick Gower, 'Coronavirus: Up to 120,000 Kiwis Predicted to Lose Jobs – Economist' *Newshub* (Web Page, 7 June 2020) <https://www.newshub.co.nz/home/money/2020/06/coronavirus-up-to-120-000-kiwis-predicted-to-lose-jobs-economist.html>.

16 Andrew A Schwartz, 'Equity Crowdfunding in New Zealand' (2018) *New Zealand Law Review* 243, 252–254.

*Financial Markets Conduct Act 2013* (NZ) first permitted this form of investment in 2014.[17] However, growth in the sector is not consistent. In 2018, the total capital raised through equity crowdfunding platforms increased to NZD16.7 million (from NZD11.97 million in 2017),[18] however in 2019, investment fell to NZD13.7 million.[19]

Through equity crowdfunding, a fundraiser elicits non-debt financing and so entrepreneurial risk is shared between the business founders and outside investors. Investors' risk can be very high, given that a fundraiser is usually a start-up or in a loss-making situation.[20] Undertaking risk generally drives a capitalist economy,[21] in which — to a great extent — profits constitute compensation for investors assuming entrepreneurial risk. Investors' risk includes both income and capital risks. Income risk refers to uncertainty regarding future net revenues, whereas, capital risk arises from the uncertain future value of capital goods which, in turn, results from an uncertain depreciation rate or future replacement cost of the capital.[22]

Incentivising equity crowdfunding through taxation has been considered in the tax literature,[23] however, the impact of tax on the fundamental policy goals underpinning the equity crowdfunding exception to usual securities rules, remains largely unexamined. This article aims to fill this gap and discusses various tax incentives from the perspective of their financial markets policy effects.

Income tax can be expected to deter risk undertaking because it reduces the amount of after-tax income in a shareholder's hands. Empirical evidence, however, does not support this presumption. Stiglitz has found that, if the national tax system shares sufficiently in income risk (through full or partial loss offset) and in expected capital risk (by ex post

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[17] *Financial Markets Conduct Act 2013* (NZ) ('*Financial Markets Conduct Act*'). Some provisions of this Act came into force on 1 April 2014, others on 1 December 2014. For details see Financial Markets Legislation (Phase 1) Commencement Order 2014 (LI 2014/51); Financial Markets Legislation (Phase 2) Commencement Order 2014 (LI 2014/325).

[18] 'Statistical Report on Peer-to-Peer Lending and Crowdfunding in New Zealand', *Financial Markets Authority* (Report, 23 November 2018) <https://public.tableau.com/profile/fmaadmin#!/vizhome/Reg_returns_final_version_0/Story1> ('FMA Statistical Report').

[19] 'Peer-to-Peer and Crowdfunding: Sector Snapshot', *Financial Markets Authority* (Report, 5 December 2019) <https://www.fma.govt.nz/news-and-resources/reports-and-papers/peer-to-peer-and-crowdfunding-sector-snapshot> ('FMA Sector Snapshot').

[20] For a discussion of the risks associated with crowdfunding, see Francesca Tenca and Chiara Franzoni, 'Crowdfunding: Risk, Fraud and Regulation' in Hans Landström, Annaleena Parhankangas and Colin Mason (eds), *Handbook on Research on Crowdfunding* (Edward Elgar, 2019) 323–337.

[21] Joseph E Stiglitz, *Economics of the Public Sector* (W W Norton & Company, 3rd ed, 2000) 588.

[22] Russell Krelove, 'Taxation and Risk Taking' in Parthasarathi Shome (ed), *Tax Policy Handbook* (International Monetary Fund, 1995) 55, 58.

[23] See, eg, Paul Battista, 'The Taxation of Crowdfunding: Income Tax Uncertainties and a Safe Harbor Test to Claim Gift Tax Exclusion' (2015) 64(1) *University of Kansas Law Review* 143; Stephen Graw, 'Crowd-Sourced Funding – Was Tax Considered?' (2018) 13(1) *Journal of the Australasian Tax Teachers Association* 85.

depreciation, or by not taxing capital gains or taxing them upon realisation), risk undertaking increases.[24]

An understanding of the role that income tax may play in the growth of equity crowdfunding requires a holistic analysis of the interplay between crowdfunding regulations and tax legislation, including the effects of specific tax incentives on equity crowdfunding. This article, which has a jurisdictional focus on New Zealand albeit broader relevance,[25] engages in this analysis.

Relevantly, this article is structured to provide a further explanation of equity crowdfunding in New Zealand (Part II) and its tax implications (Part III), prior to discussing the desirability of tax incentives for equity crowdfunding and drawing conclusions in Part V.

## II Equity Crowdfunding in New Zealand

Equity crowdfunding requires three types of participants: a fundraiser, an intermediary and investors. The aim of the intermediary is to match the capital demands of a fundraiser with the supply of funds from investors.

Different motives drive crowdfunding participants. The lack of alternative financial instruments, minimum formalities and lower costs of investment,[26] and an opportunity to market one's own products, are the typical reasons for crowdfunding's appeal to fundraisers.[27] Meanwhile, willingness to help, to enjoy a small risk undertaking, to learn from leading investors or share an investment risk with the crowd, along with an expectation of a material return from a contribution, tend to motivate investors. An intermediary focuses on making profits by matching fundraisers' demands to the supply of funds from investors.

The effectiveness of equity crowdfunding depends on the ability of an intermediary to first, control the high risks associated with investing in early-stage start-ups, and

[24] Stiglitz (n 21) 589–590.

[25] For a critical discussion of equity crowdfunding in Australia, see Akshaya Kamalnath and Nuannuan Lin, 'Crowd-Sourced Equity Funding in Australia – A Critical Appraisal' (2019) 47(2) *Federal Law Review* 288. For an analysis of the taxation of crowdfunding in Australia, see Fiona Martin and Ann O'Connell, 'Crowdfunding: What Are the Tax Issues' (2018) 20 *Journal of Australian Taxation* 16. See also Graw (n 23).

[26] Ajay Agrawal, Christian Catalini and Avi Goldfarb, 'Some Simple Economics of Crowdfunding' (2014) 14(1) *Innovation Policy and the Economy* 63.

[27] Qualitative research into German start-ups found the following reasons for their pursuing equity crowdfunding: fundraising, marketing, the speed of the funding process, the favourable company evaluation, the minor impact on the shareholder situation (if voting rights are not transferred), and the opportunity to find more investors after the campaign. See Martin Angerer et al, 'Start-Up Funding via Equity Crowd-Funding in Germany – A Qualitative Analysis of Success Factors' (2017) 17(1) *Journal of Entrepreneurial Finance* 1, 5–9.

therefore, to earn trust among investors, and second, to match appropriate fundraisers and investors.[28]

Equity crowdfunding in New Zealand is 'target-based', which means if the project's fundraising objective is not met, the project is regarded as unsuccessful and all money should be returned to investors. In 2019, the number of equity crowdfunding projects that met their minimum funding target fell to 19 (from 28 in 2018 and 34 in 2017).[29]

In 2019, 84.4 per cent of investments made through equity crowdfunding platforms in New Zealand were below NZD5,000 (88.5 per cent in 2018).[30] There could be many reasons for investors' unwillingness to undertake substantial financial risks. First, investments in loss-making companies are highly risky. Second, because equity crowdfunding is a relatively new form of investment vehicle, there is negligible empirical data on average return on investment. Third, the absence of a secondary market for crowdfunded shares limits investors' exit opportunities. Finally, fundraisers commonly offer non-voting shares, in part, to avoid the voting control implications of the takeovers regulations,[31] with the result that the investor may not enjoy the rights associated with ordinary shares, including the right to vote on the appointment and removal of directors.[32]

Offers of securities in New Zealand are subject to the disclosure requirements of the *Financial Markets Conduct Act 2013* (NZ), subject to certain exclusions. Generally, a fundraising company and its directors must comply with extensive and often expensive disclosure requirements. However, the crowdfunding exclusion shifts this compliance responsibility to an intermediary that provides a crowdfunding service (i.e. a crowdfunding platform).[33] Therefore, this intermediary acts as a gate-keeper — a quasi-stock exchange with some delegated regulatory functions. The crowdfunding exclusion applies when relatively small amounts of money are exchanged for shares in a fundraiser through a crowdfunding platform.[34]

Crowdfunding platforms operating in New Zealand must be licensed by the Financial Markets Authority ('FMA')[35] and must meet certain other requirements.[36] For the year ending 30 June 2019, seven New Zealand crowdfunding platforms held licences issued by

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[28] Victoriya Salomon, 'Evolving Crowdfunding Models' in Landström, Parhankangas and Mason (eds) (n 20) 358.

[29] FMA Statistical Report (n 18); FMA Sector Snapshot (n 19).

[30] 'Crowdfunding Sector Summary' in FMA Sector Snapshot (n 19).

[31] A 'code company' includes a company that has 50 or more shareholders. See Takeovers Regulations 2000 (SR 2000/210) reg 3(1).

[32] See *Companies Act 1993* (NZ) s 36.

[33] *Financial Markets Conduct Act* (n 17) s 6, sch 1 cl 6. See also Schwartz (n 16) 249.

[34] Financial Markets Conduct Regulations 2014 (NZ) regs 185(1)(a), (4) ('Financial Markets Conduct Regulations').

[35] Ibid regs 186(1)(d), 390.

[36] For details see *Financial Markets Conduct Act* (n 17) ss 186, 197, 202.

the FMA, down from 8 in 2018.[37] Most of these platforms have operated since 2014 when equity crowdfunding was first permitted. Regulations do not impose a cap on individual investment but prescribe a fundraising threshold — up to NZD2 million through licensed crowdfunding platforms in any 12-month period. This threshold applies in aggregation with any fundraising under the small offers exclusion or any peer-to-peer lending.[38] New Zealand crowdfunding regulations are light-handed in that they: have no residency restrictions for fundraisers or investors; place fundraisers outside the disclosure regime; and have no direct investors' cap.[39]

According to Schwartz, equity crowdfunding in New Zealand has the following particular features: 'syndication', which means 'the crowd invests alongside a large and sophisticated '"lead" investor';[40] preferences to invest in local businesses;[41] and the importance of reputation for both fundraising companies and crowdfunding platforms.[42] Keeper describes the New Zealand equity crowdfunding regime as 'one of the most progressive and innovative operating in the world today'.[43]

## III Equity Crowdfunding: Income Tax Implications

This part of the article outlines the income tax implications for participants of equity crowdfunding in New Zealand.

### A *Fundraisers*

The three main income tax events for fundraisers include the receipt of contributions, incurring of expenses and payment of dividends.

Income tax assessability of contributions depends on the nature of the funds in the hands of the recipient. In particular, money raised through equity crowdfunding does not constitute income, rather it is capital in the hands of the fundraiser. (A share issue is an exempt supply for goods and services tax ('GST') purposes.[44])

A crowdfunding initiative can be a mix of equity and reward crowdfunding. If a fundraiser not only issues shares but also provides rewards (for example sells products the business

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[37] FMA Sector Snapshot (n 19).

[38] *Financial Markets Conduct Act* (n 17) s 6, sch 1 cl 6, 12–14.

[39] An investor can invest in multiple fundraisers but may not, of course, invest more than NZD2 million in one particular fundraiser.

[40] Schwartz (n 16) 245, 262–265.

[41] Ibid.

[42] Ibid 246, 270–272.

[43] Trish Keeper, 'Equity Crowdfunding in New Zealand: A Progressive Experiment' (Working Paper No 103, Centre for Accounting, Governance and Taxation Research, Victoria University of Wellington, September 2016) 2.

[44] *Goods and Services Tax Act 1985* (NZ) ss 14(1)(a), 3(1)(d) ('*Goods and Services Tax Act*').

usually produces in advance), money received for the rewards may be regarded as the fundraiser's income[45] from a business or profit-making scheme.[46]

The use of share capital for non-capital business purposes gives rise to deductions, if the general permission rule[47] — which requires a link with the profits or a business — is satisfied, and no limitations apply.[48] For example, money spent on advertising, establishing a crowdfunding project and relevant legal expenses are generally deductible. The capital limitation rule, which denies the deductibility of expenses of a capital nature[49] should not apply in such a case because expenses are incurred to raise funds and, therefore, improve the business's cash flow and operation. Therefore, these expenses should be regarded as revenue-related, rather than as capital expenses.[50] (If a fundraiser is GST registered, it can claim certain inputs, for example, GST paid to a crowdfunding platform.[51])

Fundraisers incur various direct costs, including intermediary's fees and advertising expenses (and they also bear the opportunity costs experienced in fundraising). Generally, a fundraiser can deduct business-related expenses in the year they are incurred;[52] unexpired expenses are deemed income of the fundraiser[53] but can be deducted in the following income year,[54] unless certain exemptions apply.[55] If the deduction of expenses, including those related to raising equity through a crowdfunding platform, results in a net loss for the income year, the fundraiser may carry this loss forward and offset it against future profits.[56] Sometimes losses can be offset against net income of a company related to a fundraising company through loss grouping,[57] although small and medium size companies are typically stand alone.

A fundraiser which seeks funds from the crowd is usually in a loss-making situation. Without income from other sources, such a fundraiser could only carry forward its tax

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45 *Income Tax Act 2007* (NZ) s CB 1 ('*Income Tax Act*').

46 Ibid s CB 3.

47 A taxpayer may deduct an amount if the expenditure or loss is incurred in either deriving assessable income or in the course of carrying on a business. See *Income Tax Act* (n 45) s DA 1(1).

48 *Income Tax Act* (n 45) s DA 2.

49 Ibid s DA 2(1).

50 See special rule for legal expenses under *Income Tax Act* (n 45) s DB 62.

51 *Goods and Services Tax Act* (n 44) s 20.

52 *Income Tax Act* (n 45) s EA 3.

53 Ibid s EA 3(5).

54 Ibid s EA 3(3).

55 See 'Determination E12: Persons Excused from Complying with Section EA 3 of the Income Tax Act 2007', *Inland Revenue Department* (Report, 4 March 2009) <https://www.classic.ird.govt.nz/technical-tax/determinations/accrual/determinations-persons-excused-from-complying.html>.

56 *Income Tax Act* (n 45) s IA 2(2).

57 Ibid s IA 2(3).

loss but 'the lost time value would impose a significant discount'.[58] To utilise its tax losses, the fundraiser would need to bring in an outside investor with sufficient tax liability from other sources.[59] However, that outcome may not be possible, or may result in the extinction of transferable losses. Continuity[60] and commonality[61] of shareholding rules and certain anti-avoidance provisions[62] restrict loss offset and transferability of losses to new investors. Moreover, New Zealand crowdfunding regulations do not allow flow-through entities such as partnerships and limited partnerships to crowdfund.[63] This regulatory limitation blocks direct access to a fundraiser's losses. A company, unless it is a look-through company, cannot pass its losses through to its shareholders. Notwithstanding, a look-through company, risks losing its flow-through tax status if the equity finance it receives through a crowdfunding platform (or otherwise) results in the breach of the five or fewer look-through counted-owners' limitation.[64]

A fundraiser distributes income and gains to its shareholders through dividends. These distributions, if made by a company resident in New Zealand, are subject to imputation rules,[65] and may also trigger resident withholding tax ('RWT') if investors are local tax residents.[66] If investors are foreign tax residents, non-resident withholding tax ('NRWT'),[67] and sometimes, foreign investor tax credits ('FITC')[68] may apply. Consequently, a fundraiser should withhold either RWT or NRWT from dividends it pays but also may qualify for FITC, if a supplementary dividend is paid to foreign investors.

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58 Felix Mormann, 'Beyond Tax Credits: Smarter Tax Policy for a Cleaner, More Democratic Energy Future' (2014) 31(2) *Yale Journal on Regulation* 303, 309. The mathematical formula for calculating the present value of an individual cash flow is PV = F / [(1 + i)*n]; where, PV is 'Present Value', F is 'Future payment' (cash flow), i is interest rate, n is the number of periods in the future. For instance, for an effective annual interest rate of 10 per cent (i), receiving $100 (F) in five years (n) the present value (PV) is $62.90.

59 Ibid.

60 In terms of *Income Tax Act* (n 45) ss IA 5 (2), (3), a group of persons should hold for the continuity period minimum voting or market interests in the company that add up to at least 49 per cent.

61 In a group of companies, none of which is a multi-rate portfolio investment entity ('PIE') or a listed PIE, the same group of persons should hold common voting or market interests that add up to at least 66 per cent. See *Income Tax Act* (n 45) s IC 1(1).

62 For instance, see *Income Tax Act* (n 45) ss GB 3 ('arrangements for carrying forward loss balances: companies'), GB 4 ('arrangements for grouping tax losses: companies').

63 Financial Markets Conduct Regulations (n 34) regs 185(1)(a), (4).

64 *Income Tax Act* (n 45) ss HB 1, YA 1 (definition of 'look-through company').

65 Ibid sub-pt OB.

66 Ibid sub-pt RE.

67 Ibid sub-pt RF.

68 Ibid ss LP 2–LP 6.

### B *Investors*

The tax implications of equity crowdfunding for investors depends on the type of investor and their tax residency status. Two events are relevant: making an investment and receiving a dividend.

If a crowdfunding project meets its target, an equity investor becomes a shareholder of the fundraiser. Shares received in a fundraiser constitute capital in the hands of an investor. The absence of a secondary market for shares obtained through crowdfunding makes it implausible to regard these shares as revenue account property. Under the capital limitation rule,[69] contributions made by the investor in the course of equity crowdfunding are a non-deductible expense to this investor. However, because the shareholding can potentially generate dividend income for the investor, this investor may claim a deduction for interest paid on money borrowed for equity investment made through a crowdfunding platform.[70]

Distributions from a company to its shareholders constitute dividends, unless an exclusion applies.[71] Dividends are assessable income in the hands of a shareholder.[72] Amounts of the RWT/NRWT and imputation credits attached to dividends must be added to the net dividend to calculate the shareholder's tax liability.[73] After this liability is calculated, RWT/NRWT credits and imputation credits (if a shareholder is a New Zealand resident) can be credited against this liability.[74] Non-resident shareholders cannot use imputation credits attached to satisfy their income tax liability[75] but, in some circumstances, can receive supplementary dividends equal to their imputation credits.[76] Distributions from a company to its shareholders invariably constitute dividends. Therefore, distributed capital gains are usually taxable in a shareholder's hands, unless distributed on liquidation.[77]

As shares in a fundraiser constitute capital in the hands of an investor, their subsequent distribution does not have income tax consequences, unless they are in the business of dealing in shares.[78] Any gain on disposal is not normally taxable, and any loss is not a deductible expense.[79]

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[69] Ibid s DA 2(1).

[70] Ibid s DB 6(1).

[71] Ibid s CD 4.

[72] Ibid s CD 1.

[73] Ibid s CD 15(1).

[74] Ibid s LA 2.

[75] Ibid s RB 3(4).

[76] Ibid sub-pt LP.

[77] Ibid s CD 26.

[78] Ibid ss CB 3, CB 4, CB 5.

[79] Ibid ss DA 1, DA 2(1).

### C *Intermediaries*

Fees received from fundraisers are included in the business income of an intermediary and are taxed accordingly.[80] Expenses related to the operation of the crowdfunding platform, including licence fees paid to the FMA are deductible business expenses.[81] (Intermediation services constitute a taxable supply and are, therefore, subject to GST if an intermediary is (or is required to be) GST registered.[82])

No specific tax is levied on crowdfunding platforms in New Zealand. Discussion on the introduction of a digital services tax ('DST') — a tax levied on the services of platform firms — took place in 2019.[83] Relevantly, a flat tax charged at three per cent on the gross turnover attributable to New Zealand of certain digital businesses, applied on a consolidated group basis, was proposed.[84] However, any DST would most likely have turnover-based *de minimis* thresholds in order to target large multinationals — a EUR750 million of consolidated annual turnover threshold and a New Zealand specific annual threshold of NZD3.5 million.[85] Given the small size of both New Zealand's economy and its domestic crowdfunding platforms, it is unlikely that any domestic crowdfunding platforms might ever exceed the *de minimis* thresholds proposed for the DST, if it were to be introduced. Crowdfunding platforms might also be exempt from a DST.

## IV Incentivising the Crowd

Tax incentives can be expected to benefit fundraisers.[86] However, incentives may not be even-handed and may therefore skew investment decisions. This part of the article considers tax incentives for innovative companies and how these incentives may impact on the informing principle of equity crowdfunding.

### A *Tax Incentives in Equity Crowdfunding*

Equity crowdfunding investors naturally expect a return on their investments.[87] This return can be negative (if the enterprise fails), zero (if investors are not able to assess the returns from the investment because a valuation of the entries has not been observed),

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80 Ibid s CB 1.

81 Ibid s DA 1(1).

82 *Goods and Services Tax Act* (n 44) ss 5(1), 6(1), 8(1).

83 In June 2019, the Inland Revenue Department invited public submissions on a DST proposal. See Grant Robertson and Stuart Nash, *Options for Taxing the Digital Economy: A Government Discussion Document* (Report, 4 June 2019) <http://taxpolicy.ird.govt.nz/sites/default/files/2019-dd-digital-economy.pdf>. For a discussion of the DST proposal, see Ben Walker, 'Analysing New Zealand's Digital Services Tax Proposal' (2019) 21(2) *Journal of Australian Taxation* 86.

84 Robertson and Nash (n 83) [3.17].

85 Ibid [3.25].

86 See, eg, Graw (n 23) 106.

87 Magdalena Cholakova and Bart Clarysse, 'Does the Possibility to Make Equity Investments in Crowdfunding Projects Crowd Out Reward-Based Investments?' (2015) 39(1) *Entrepreneurship Theory and Practice* 145.

or positive (if an enterprise is able to launch another crowdfunding campaign, receive finance from venture capitalists or business angels, or be subject to a merger or an acquisition).[88] The income risk of crowdfunding investors tends to be very high because a fundraiser is typically a start-up — or in a loss-making situation.

The tax system can share in income risk with investors by, for example, incentivising initial investment and income distribution. It can also share in capital risk by incentivising the investor's disposal of the investment. In both cases, investors are expected to assume the initial investment risk by contributing capital to a fundraiser.

Tax incentives for initial investment and income distribution effectively subsidise the cost of investment and, therefore, increase its value to an investor. These incentives may stimulate investments in start-ups because they reward new capital, instead of creating windfall gains for existing investors.[89] Tax incentives for the disposal of an investment are generally considered desirable if they incentivise investors to support the development and growth of the fundraiser, create jobs and lead to productive innovation.[90] From a broader economic perspective, tax incentives for the disposal of the investment encourage 'fast failure' of poorly performing businesses and thereby liberate capital that can be invested in better performing businesses.[91] The same tax incentive may sometimes encourage both investment risk and capital risk.

New Zealand encourages capital risk through its depreciation regime and light-handed taxation of capital gains. New Zealand's depreciation regime is well-developed,[92] with accelerated depreciation for eligible assets acquired before 21 May 2010.[93] New Zealand does not have a comprehensive capital gains tax ('CGT') regime. After intensive discussions, in 2019 the Labour-led government decided not to proceed with the Tax Working Group's recommendation for a comprehensive CGT.[94] New Zealand, therefore, will continue sharing the capital risk with investors. However, this sharing affects only sole traders and investors in flow-through entities[95] and therefore, is irrelevant to equity

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88 Andrea Signori and Silvio Vismara, 'Returns on Investments in Equity Crowdfunding', *SSRN* (2016) 4 <https://ssrn.com/abstract=2765488>.

89 'Position Paper on Tax Policy', *The Angel Association New Zealand* (Report, April 2018) [17]–[18] <https://www.angelassociation.co.nz/wp-content/uploads/2018/05/AANZ-Position-Paper-on-Tax-Policy-2018.pdf>.

90 Ibid. It is submitted, however, that tax incentives should be proportionate, inasmuch as they should rationally connect an express policy to a desired outcome.

91 Ibid.

92 *Income Tax Act* (n 45) sub-pt EE.

93 'General Depreciation Rates, IR265', *Inland Revenue Department* (Guide, April 2019) 2 <https://www.classic.ird.govt.nz/forms-guides/keyword/businessincometax/ir265-guide-general-depreciation-rates.html>.

94 Jacinda Ardern, 'Government Will Not Implement a Capital Gains Tax', *New Zealand Government* (Media Release, 17 April 2019) <https://www.beehive.govt.nz/release/government-will-not-implement-capital-gains-tax>.

95 According to the Tax Working Group, there were 469,000 sole traders, 97,500 general partnerships, 1,800 limited partnerships, and 254,100 trusts and 322,300 ordinary companies in New Zealand. See 'Tax Working Group Information Release' (Release Document, September 2018)

crowdfunding due to the requirement for a fundraiser to be a company. Furthermore, the depreciation regime and CGT are related to the disposal of investments and therefore, do not directly affect fundraisers — equity crowdfunding is an instrument for raising capital, rather disposing of it.

There are no crowdfunding tax incentives in New Zealand; the tax system therefore does not share investment risk with investors participating in equity crowdfunding. At the same time, specific tax incentives for fundraisers, such as incentives for start-ups[96] or innovative entities, may 'distract' crowdfunding investors and therefore, undermine the basic principle of group investment. The distraction problem is particularly relevant to New Zealand because of its syndication model — once a lead investor becomes distracted, the crowd is likely to follow. The next sections examine this problem.

### B *Tax Incentives for Innovation*

New Zealand seeks to incentivise investment in innovation by extending income tax concessions for research and development ('R&D').[97] These incentives may nudge investors towards incentives-eligible over incentives-free fundraisers.

A company which derives assessable business income may claim a deduction for R&D expenses.[98] This general incentive is supplemented by two specific incentives: an R&D loss tax credit[99] and an R&D tax credit.[100] After 1 April 2015, an unlisted New Zealand-resident company qualifies for the R&D loss tax credit, subject to certain thresholds, and provided public entities hold fewer than 50 per cent of its shares.[101] The R&D loss tax credit allows an innovative resident company in a loss-making situation to improve its cash flow.[102] Up to 28 per cent of business losses from eligible R&D expenditure within

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<https://taxworkinggroup.govt.nz/sites/default/files/2018-09/twg-bg-appendix-1--types-of-business-entities-in-new-zealand-and-how-they-are-taxed.pdf>. In fact, the number of trusts is unknown, since only trusts with taxable income must register with any government authority. Furthermore, the number of registered companies exceeds 600,000. See Jonathan Barrett and Ronán Feehily, *Understanding Company Law* (LexisNexis, 4th ed, 2019) 14.

96 Tax Working Group, *Future of Tax: Final Report Volume I — Recommendations* (21 February 2019) 17, 73–74 <https://taxworkinggroup.govt.nz/resources/future-tax-final-report-vol-i-html>. See also, Grant Robertson and Stuart Nash, 'Business Tax Changes Back Kiwi Companies to Innovate and Grow' (Media Statement, 23 September 2019) <http://taxpolicy.ird.govt.nz/news/2019-09-23-tax-initiatives-announced-support-businesses> ('Business Tax Changes Media Statement').

97 New Zealand Accounting Standards Board of the External Reporting Board, *New Zealand Equivalent to International Accounting Standard 38 Intangible Assets* (NZ IAS 38, 2014-18) [8] defines 'research' as 'original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding' and 'development' as 'the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use.'

98 *Income Tax Act* (n 45) ss DB 34, DB 35.

99 Ibid sub-pt MX.

100 Ibid sub-pt LY.

101 Ibid s MX 2.

102 It is presumed that research and development ('R&D') expenditure is a proxy for innovation.

existing thresholds can be refunded, instead of being carried forward. The amount of an R&D loss tax credit is the lesser of the following: NZD476,000 for the tax year 2019–2020 (NZD560,000 from the tax year 2020–2021); or 28 per cent of the company's net loss or total R&D expenditure for the year; or 28 per cent of the company's total R&D labour expenditure for the year multiplied by 1.5.[103]

From the 2019–2020 income tax year, eligible persons can seek the R&D tax credit.[104] This credit is available to individuals who are residents in New Zealand and entities which are either resident in New Zealand or carrying on (or are treated as if they are carrying on) business in New Zealand through a fixed establishment.[105] The key elements of the R&D tax credit regime include a specific definition of 'research and development activity',[106] which is distinguished between 'core research and development activity'[107] and 'supporting research and development activity;[108] the necessity to file an R&D supplementary return[109] and either obtain (from the 2020–2021 income year)[110] a general approval for R&D activities (if expected R&D expenditure is less than NZD2 million)[111] or apply for recognition as a 'significant performer' (if expected R&D expenditure is NZD2 million or more).[112] A taxpayer who is eligible for the R&D tax credit must spend at least NZD50,000 on qualifying R&D,[113] and may claim 15 per cent eligible expenditure as an R&D tax credit, subject to a cap of NZD120 million.[114] From the start of 2020, R&D expenditure totalling less than NZD10,000 is immediately deductible.[115]

### C *The Interplay between Crowdfunding Regulations and R&D Tax Incentives*

According to Graw, 'anything that encourages investors to support innovation is to be welcomed — particularly in the period between the initial stage of the business's lifecycle … and the commercialisation stage'.[116] However, it is crucial to note that in New Zealand the stated goal of equity crowdfunding is 'to facilitate the matching of companies which

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[103] *Income Tax Act* (n 45) ss MX 4(1)(d)–(i).

[104] *Taxation (Research and Development Tax Credits) Act 2019* (NZ) s 3 ('*Taxation (R&D Tax Credits) Act*').

[105] For more detail and exemptions see *Income Tax Act* (n 45) s LY 3.

[106] This definition differs from a definition of 'research and development activity' for the purposes of the R&D deductible expenditure and R&D tax loss credit.

[107] *Income Tax Act* (n 45) s LY 2(1).

[108] Ibid s LY 2(3).

[109] *Tax Administration Act 1994* (NZ) s 33E ('*Tax Administration Act*').

[110] For the 2019–2020 tax year, pilot rules applied. For more detail, see *Taxation (R&D Tax Credits) Act* (n 104) s 30.

[111] *Tax Administration Act* (n109) s 68 CB.

[112] Ibid s 68 CC.

[113] *Income Tax Act* (n 45) s LY 4(1).

[114] Ibid s LY 4(2), (3).

[115] Robertson and Nash, 'Business Tax Changes Media Statement' (n 96).

[116] Graw (n 23) 102.

wish to raise funds with many investors who are seeking to invest relatively small amounts'.[117] Unlike the United Kingdom or the United States, the New Zealand government has not expressly linked relaxed fundraising regulations with job creation, innovation or regional development.

Specific R&D tax incentives aim to boost innovation. The principal objectives of these incentives and of equity crowdfunding policy are different. There is a risk, therefore, that pursuit of innovation may undermine crowdfunding's principal objective and also breach the tax principle of neutrality. Of course, the government may be aware of these possibilities but, in the absence of any policy statement on a preference for innovative companies in equity crowdfunding, it may be assumed that any such preference is unintended.

R&D tax incentives and crowdfunding regulations may have the same overarching goal, that is, to build enduring businesses by improving their cash flows. R&D tax incentives improve the cash flow at the state's expense by reducing the income tax burden of eligible entities. Crowdfunding regulations improve the cash flow at the expense of private investors through the easing of security regulations for equity investments. However, two general differences distinguish the two policies. First, R&D tax incentives focus on innovative businesses, while equity crowdfunding aims to support any business that might generate a return on investment. For R&D tax incentives, 'innovative' is the core concept that determines whether an entity receives state support or not. In contrast, the financial support provided by private investors through equity crowdfunding depends on the ability of a fundraiser to demonstrate that it might generate a return on investment. Innovativeness does not matter in this context, in particular, because this quality itself does not guarantee a return on investment.[118] From an investor's perspective, R&D tax incentives encourage risk undertaking if an enterprise is innovative, whereas crowdfunding regulations encourage the undertaking of small risks in any businesses that can generate a return on investment. Furthermore, R&D tax incentives encourage innovative behaviour by a particular entity. Crowdfunding regulations incentivise group investment behaviour. These differences indicate that innovation by an individual entity should not undermine group investment behaviour.

Two abilities of a crowd are critical for choosing an appropriate fundraiser and building an enduring business — the ability to distinguish companies with good profit-making potential from those that are likely to fail ('screening ability'); and an ability to monitor the performance of fundraisers ('monitoring ability').[119] Tax incentives do not affect the monitoring ability of the crowd, however they may have an impact on the crowd's screening ability by distracting investors.

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[117] Financial Markets Conduct Regulations (n 34) reg 185(1)(a).

[118] See Kane (n 6) on job creation by start-ups in general, not specifically innovative start-ups.

[119] Wei Chen, Mingfeng Lin and Bryan Zhang, 'Lower Taxes, Smarter Crowd? The Impact of Tax Incentives on Equity Crowdfunding' (Research Paper No. 18-27, Georgia Tech Scheller College of Business, 2018) 2 <https://ssrn.com/abstract=3206256>.

If only innovative companies were to seek funds through crowdfunding, there would be no distraction for a crowd, and all fundraising companies would compete for funds on an equal basis. However, when innovative and non-innovative companies compete for funds, the former's tax advantages may distract the crowd and prevent it from picking a likely winner from the entire pool of fundraisers. The United Kingdom's Seed Enterprise Investment Scheme ('SEIS') illustrates this possibility.[120]

According to Signori and Vismara, 'firms with at least one non-executive director and offerings eligible for the SEIS tax relief are 2.9 times more likely to being able to raise additional capital in second offerings made through equity crowdfunding.[121] Conversely, Chen et al found that, if tax incentives encourage investment in particular enterprises, they do not change the performance of these enterprises but do shift investors' attention to incentive-eligible firms and therefore, decrease the crowd's screening ability in relation to non-SEIS firms.[122] This finding suggests that tax incentives can indirectly encourage risk undertaking in the equity crowdfunding industry albeit only for investments in fundraisers that are eligible for particular tax incentives.

### D *Discussion*

If a business is innovative, the state may choose to share investment risk with investors through general and specific tax incentives. However, only general tax incentives are

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[120] PwC for the European Commission explains the operation of SEIS as follows:

> SEIS provides individuals making investments in young companies with an upfront tax credit, a capital gains tax deferral for reinvestment, a capital gains tax exemption for chargeable gains realised on disposal and loss relief on more favourable terms than the baseline tax system for capital losses realised on disposal. The scheme's ranking was driven by high scores across scope, qualifying criteria and administration. SEIS uses a combination of age, size and specific sector exclusions to target entrepreneurial firms. It restricts the participation of related parties, but has introduced allowances for business angels. It targets newly issued ordinary share capital, imposing a maximum investment value attracting tax relief and a minimum holding period. In terms of administration, SEIS is administered on a non-discretionary basis and is subject to transparent annual monitoring of fiscal costs.

See PwC, 'Effectiveness of Tax Incentives for Venture Capital and Business Angels to Foster the Investment of SMEs and Start-Ups, Final Report (No TAXUD/2015/DE/330 implementing the Framework Service Contract No TAXUD/2015/CC/131)', *European Commission* (Report, June 2017) 4 <https://ec.europa.eu/taxation_customs/sites/taxation/files/final_report_2017_taxud_venture-capital_business-angels.pdf>.

[121] According to Signori and Vismara (n 88) 14–15:

> There are significant tax incentives for investing in small businesses in the UK. Two overlapping incentive programs are of particular interest to crowdfunding investors, as testified by the high visibility given to these programs on all the platforms. The Enterprise Investment Scheme (EIS) provides a tax deduction of 30 percent of the cost of shares purchased in qualifying private companies with a maximum tax benefit of £300,000. The Seed Enterprise Investment Scheme (SEIS) provides additional incentives by exempting shares up £150,000 in value from capital gains taxes. This amount is set as the standard maximum issuance sought by UK crowdfunding platforms such as Seedrs and Crowdcube, and exceptions can be granted only to issuers who present a "compelling proposition" subject to the platform's approval. EIS and SEIS are subject to a three year minimum holding period, with the relief being clawed back if shares are disposed earlier. This could create an incentive to postpone exit from crowdfunded firms.

[122] Chen Lin and Zhang (n 119).

available to non-innovative businesses. Both innovative and non-innovative companies may pursue equity crowdfunding, although innovative companies offer investors additional tax advantages.

Research into the effects of SEIS on the screening ability of a crowd indicates that specific R&D tax incentives introduced in New Zealand may similarly undermine the fundamental goal of equity crowdfunding and harm the interests of non-innovative companies. The crowd may focus on R&D-eligible companies and ignore non-innovative companies, despite their potential to produce a good return on investment. Investment in innovative companies does not guarantee a return on investment.

Moreover, such investments may be riskier than investments in non-innovative companies because of an observed negative association between innovativeness and subsequent firm survival.[123]

Tax incentives are generally regarded as violating principles of sound tax policy and may limit progressivity in a tax system.[124] In particular, if tax credits for businesses cannot be utilised entirely, and in the same year when they have become available, they cannot be justified on efficiency grounds because only some of their value funds the targeted activity.[125] High-income business entities extract most benefits from tax credits, which raises concerns over taxpayer equity.[126] According to Musgrave and Musgrave:

> Tax relief for investment which does not pay for itself in generating additional growth not only involves revenue loss without gain but worsens the state of income distribution, by giving the relief to high incomes. Judged on these grounds, tax incentives to investment have been generally wasteful and inequitable, so much so that many observers have been led to reject all incentive devices.[127]

New Zealand's 'broad base, low rate' income tax system, and its informing principles of efficiency, equity and neutrality,[128] provide plausible grounds for arguing against tax

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[123] See Ari Hyytinen, Mika Pajarinen and Petri Rouvinenb, 'Does Innovativeness Reduce Startup Survival Rates?' (2015) 30 *Journal of Business Venturing* 564.

[124] See, eg, David Bruoni, 'The Limits of Justice: The Struggle for Tax Justice in the States' in Joseph J Thorndike and Dennis J Ventry Jr (eds), *The Ongoing Debate: Tax Justice* (The Urban Institute Press 2002) 211.

[125] Mormann (n 58) 335–336.

[126] Stanley S Surrey, *Pathways to Tax Reform; the Concept of Tax Expenditures* (Harvard University Press, 1973) 134.

[127] Richard A Musgrave and Peggy B Musgrave, *Public Finance in Theory and Practice* (McGraw-Hill Book Company, 5th ed, 1989) 601–602.

[128] See, eg, 'Financial Statements of the Government of New Zealand for the Year Ended 30 June 2019 Note 23', *The Treasury* (8 October 2019) <https://treasury.govt.nz/publications/year-end/financial-statements-2019>. See also the principles of responsible fiscal management as prescribed by the *Public Finance Act 1989* (NZ). Proposed principles for a good tax system typically include efficiency, administrative simplicity, flexibility, political responsibility (transparency), fairness (equity). See Stiglitz (n 21) 458.

incentives. However, according to Burman, 'voters like tax incentives',[129] and accordingly, the political pressure for tax incentives is likely to prevail.[130]

Musgrave and Musgrave emphasise that 'it is a task of tax policy to make sure that additions to growth are brought at the least equity cost'.[131]

Specific R&D tax incentives may contribute to the development of an innovative ethos among the New Zealand business community. However, encouragement of innovative behaviour through tax incentives should be distinguished from encouragement of group investments through equity crowdfunding. Otherwise, the former may undermine the latter, making crowd investment distorted, inefficient and unfair. Fundraising companies should be able to compete for investments on an equal footing, so that the crowd is able to pick a real 'winner'. Ringfencing equity crowdfunding from R&D tax incentives could help in reaching this policy goal and maintaining the well-balanced state's participation in risk-undertaking that New Zealand's light-handed crowdfunding regulations and its tax legislation have created. For example, equity crowdfunding could be ringfenced from R&D tax incentives by amending regulation 185(1)(a)(iii) of the Financial Markets Conduct Regulations 2014, by adding the phrase: '(other than recipients of R&D tax incentives)'. The amended regulation would then provide: 'the principal purpose of the facility is to facilitate the matching of companies [*(other than recipients of R&D tax incentives)*] which wish to raise funds with multiple investors who are seeking to invest relatively small amounts'.[132] Companies eligible for R&D tax incentives that wish to raise funds through equity crowdfunding should have the opportunity to opt-out from these specific tax incentives.

A theoretical alternative to the ringfencing proposed above could be a specific tax that would correct crowdfunding externalities. A tax levied on contributions made after a crowdfunding project has reached its funding goal would internalise overfunding externalities such as those caused by overshadowing other crowdfunding projects.[133] Similarly, it would be possible to impose a special tax on fundraising companies seeking finance through crowdfunding platforms but willing to receive specific R&D tax incentives. While it is not suggested that such measures are likely, the inconsistency between crowdfunding regulations and R&D tax incentives indicates the non-neutral treatment of innovative and non-innovative fundraisers which contradicts the basic rationale for equity crowdfunding.

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[129] Leonard E Burman, 'Pathways to Tax Reform Revisited' (2013) 41(6) *Public Finance Review* 755, 756.

[130] Musgrave and Musgrave (n 127) 601–602. Governments might also like to be associated with apparent winners, for example, blockbuster movies. See *Income Tax Act* (n 45) sub-pt DS.

[131] Musgrave and Musgrave (n 127) 601–602.

[132] Financial Markets Conduct Regulations (n 34) reg 185(1)(a)(iii).

[133] Jascha-Alexander Koch, Jens Lausen, and Moritz Kohlhase, 'Towards Internalizing the Externalities of Overfunding – Introducing a "Tax" on Crowdfunding Platforms' (Research Paper No 125, Association for Information Systems 28 November 2018) <https://aisel.aisnet.org/ecis2018_rp/125>.

### E *Contribution and Limitations*

The key research contribution of this article is to highlight the disjunction between the New Zealand government's crowdfunding policy and its R&D policy. It is not claimed that the article constitutes a major contribution to knowledge, nevertheless, it connects the research conducted in New Zealand on crowdfunding to R&D tax privileges. It is hoped the research will stimulate debate and, ideally, prompt discussion between crowdfunding regulators and tax policymakers. Tax practitioners advising a range of clients should be alert to differential tax treatment of otherwise similarly situated clients. As the research method employs analysis of key texts, it is principally descriptive in nature. It does not include other qualitative methods, such as interviews or surveys, or experimentation. Furthermore, it does not have quantitative features, such as original collection and analysis of data. The research should therefore be seen as an explorative exercise that could be expanded to include more qualitative and quantitative research methods.

## V CONCLUSION

Both R&D tax incentives and light-handed crowdfunding regulations may help companies to improve their cash flows. However, this article has demonstrated that the interplay between these two policies may create a competitive advantage for innovative companies that is not available to non-innovative companies. It has been argued that to even out cash-improvement opportunities for non-innovative businesses, the state should compensate these businesses for the disadvantages that specific tax incentives, such as the R&D tax loss credit[134] and R&D tax credit,[135] create. Such compensation could be effected by extending advantages to non-innovative businesses. Ringfencing equity crowdfunding to non-innovative businesses (and businesses that opted out of the R&D tax incentives) or a specific tax levied on recipients of specific R&D tax incentives could create such a compensatory advantage and therefore, equalise opportunities for innovative and non-innovative businesses to improve their cashflows.

Furthermore, the government might consider allowing an extension of fundraiser status to flow-through entities, notably limited partnerships, so that crowdfunding investors could gain direct access to the fundraiser's profits and losses, and reap the value of tax credits, accelerated depreciation rates, and other tax incentives available to a fundraiser. Possible effects of this extension on the behaviour of the crowd would however require further examination.

To reiterate, these proposed interventions are unlikely to be enacted, although policymakers should be alert to any tax policies that might militate against job creation. Nevertheless, they highlight how the uneven tax treatment of innovative and non-innovative fundraisers may impact equity crowdfunding. It is incumbent on the government to neutralise these distortions or otherwise to expressly align crowdfunding policy with the pursuit of innovation.

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[134] *Income Tax Act* (n 45) sub-pt MX.

[135] Ibid sub-pt LY.

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