Chapter 4

THE REQUIREMENT OF AUDIT AND ASSURANCE FOR CROWDFUNDING, AS AN ALTERNATIVE FINANCING METHOD

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New financing models are being devised these days, to meet the financing requirements of enterprises. One of these financing models is the Crowdfunding, which has recently been effective in financial markets. As information technologies evolve and digitalization is adopted by many entities, there are also many entrepreneurs who wish to realize their ventures on Internet platforms. Crowdfunding is a bridge between these entrepreneurs and investors who voluntarily provide funds to them, creating a new financing source for entrepreneurs. In this system, a lot of investors provide funds to a single project. Thanks to this system, enterprises in the USA and in many European Union countries have access to a new form of financing. Likewise, people who have saved from their earnings now have a new opportunity, crowdfunding, to place these savings. However, there are some risks of crowdfunding and it is a field which is vulnerable to fraud. Therefore, to protect investors, existing rules of audit and assurance should be implemented with care. A significant step in this direction is the recent regulations brought by the lawmakers and official authorities. Independent audit, which has been applied to certain areas of business, is now a necessity for enterprises and investors, as industry and technology evolve rapidly. The purpose of this study is to set forth the conceptual framework of crowdfunding, and to explain the requirement for audit and assurance in crowdfunding, from the perspective of investors. The study also contains the Turkish practice of crowdfunding, and the regulations issued for its supervision.

INTRODUCTION

New ventures require resources to succeed, and one of the most critical of these is financing. How good an idea an entrepreneur may conceive, financing is an important step in realizing it (Gompers & Lerner, 2004; Gorman & Sahlman,

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1989). This stage involves both choosing, and accessing the appropriate source of financing. Crowdfunding has been a source of financing recently, as a method very different from the conventional financing sources. Entrepreneurs choosing this method realize their ideas by accessing capital through information technologies. Financial crises affecting many countries worldwide shrank the funding opportunities in various developed and emerging markets for entrepreneurs, small and medium sized enterprises (SME) (OECD, 2018; Fenwick et al., 2017). Thanks to the advances in technology, alternative solutions to bank loans could be devised, leading to crowdfunding to become a financing source. Crowdfunding is a relatively novel internetbased non-banking funding instrument, which has been designed mainly for early stage companies having little financial power and insufficient resources and/or without bank loan eligibility or for nonprofit institutions. Companies usually resort to crowdfunding in order to finance projects involving research ideas or innovative, creative, artistic products and services, while non-profit organisations seek for donations that serve a greater cause – prosocial campaigns (Fanea Ivanovici, 2018). The main interest of crowdfunding is the financial aspect. However, it also creates an opportunity for communication and creates a real community. Its role is becoming increasingly important and is presented as an alternative financing system to traditional modes of financing (Sannajust et al., 2014).

1. CONCEPTUAL FRAMEWORK OF CROWDFUNDING

In recent years, crowdfunding has emerged as novel way for entrepreneurial ventures to secure funds without having to seek out venture capital or other traditional sources of venture investment (Mollick, 2014). Crowdfunding enables entrepreneurs to present their project to the crowds and to acquire funds from a lot of investors in a short period of time, thanks to the opportunities of the Internet. Investors choose a project and fund the entrepreneur of this project. In return for the funds they provide, investors expect shareholding, rewards or pre-ordering rights, and sometimes they provide funds as a donation (İşler, 2014)

Crowdfunding originated from the word *crowdsourcing*. Crowdsourcing, as described by Howe (2006), is the process of taking a task traditionally performed by a designated internal agent or employee and give it to an undefined outside person or agent, in the form of an open call. The expanding Internet encourages crowdsourcing initiatives. In this era, information flows to users faster, and with much less obstacles on the way (Brady & Bigham, 2015). Therefore, users are more effective, and they can contribute more easily. As the number of internet users increase, the interaction between the parties also increase, leading to more crowdsourcing initiatives to emerge. In addition to the Internet, there are a number of other factors paving the way to crowdsourcing. For example, flexibility with respect to time and place attracts users. Participants of a crowdsourcing facility do not need to be tied to a certain time or place. People are able to provide funds to a crowdsourcing facility in their spare time, outside the hours of their regular work. It is possible that the spare time activity makes a return as well. Another factor is the open source. Open source brings more resources, and more exchange of information (Yuan et al., 2014).

In the World Bank's 2013 report (World Bank, 2013), crowdfunding was described as collecting funds from donors and investors through the Internet, and as being an effective way of extending the base of entrepreneurship, and making new ideas to be realized.

Crowdfunding is an open call to people to provide or contribute small amounts of money either in exchange for a reward or as a donation. In this way, those seeking funds appeal directly to the crowd for financing an investment, through the internet, thus sidestepping traditional financing systems like banks (Tomczak & Brem, 2013). Crowdfunding is a way of collecting many small contributions from the crowd, through the use of online funding platforms, to finance projects or enterprises. It is a novel method for funding a variety of new ventures, allowing individual founders of for-profit, cultural, or social projects to request funding from many individuals, often in return for future products or equity. Crowdfunding projects can range greatly in both goal and magnitude, from small artistic projects to entrepreneurs seeking hundreds or thousands of dollars in seed capital as an alternative to traditional venture capital investment (Mollick, 2014; Hemer, 2011).

According to Morduch (1999) crowdfunding draws inspiration from concepts like microfinance and crowdsourcing, but represents its own unique category of fundraising, facilitated by a rowing number of internet sites devoted to the topic.

The main elements of crowdfunding are technology, capital financing and the power of the crowds (Bealieu et al.,2015). The use of social media-based applications has been increasing, thanks to the technological advances of recent years. This has provided an opportunity to entrepreneurs, as the ability to use the virtual world to establish a business, realize projects and attract investors. The crowdfunding model is popular in the USA, where the projects based on innovations in technology have been realizing for a long period of time. The model has spread to the world starting with Europe and has taken the attention of fund seekers in Turkey lately, as an alternative financing method (Vural, 2019).

Capital Markets Board (CMB) defined crowdfunding in 2019, in their Decree numbered 30907 as; a method of financing where entrepreneurs collect funds from the public through crowdfunding platforms, with the purpose to realize their business ideas or personal projects (Deniz, 2019).

Looking at the reasons of this emergence of crowdfunding, one can see the insufficiencies of conventional methods. For example, entrepreneurs may not have adequate market knowledge, they may not have adequate business experience, and they may not provide the collateral required to have access to funds from conventional financing channels. It is observed that, mainly due to this reason, new entrepreneurs refer to the savings of their own, their families or their immediate circle during early-stage financing (Gedda et al., 2016; Kovtun, 2014). As the Internet expanded, entrepreneurs who are short of capital and do not have a corporate identity could be able to access financing through the virtual world. Crowdfunding is a new method of funding which emerged as the result of the difficulties faced by early-stage entrepreneurs in accessing funds, decreasing confidence in banks especially with the crisis, which had been the prominent actors among financial institutions, and the reluctance of people to invest when they have a limited amount of savings (Ata, 2018).

The first crowdfunding platform is Kiva, which was established as an online lending platform in the USA, with the social purpose to enable the citizens of developed countries to lend money to low-income people of the world (Cheney, 2017). Today, there are more than 2,000 crowdfunding platforms around the world. Using crowdfunding to collect capital for a business became applicable with the ***"JOBS Act"*** in the USA, which was enacted in 2012 (Infodev, 2013). When first launched, crowdfunding model was "donation-based", where the volunteer participants did not expect commercial gains. Later, reward-based models were observed, and in the recent years, earnings-based models involving shareholding and creditor-debtor relationships took their place in the financial scene (Griffin, 2012). Today, through the Internet, without using the conventional methods and referring to financial intermediaries, entrepreneurs can finance their ideas by the small contributions of investors or donors, with lower costs, and in a much quicker way (Golić, 2014).

2. THE PARTIES TO CROWDFUNDING

There are three distinct parties in the crowdfunding model; fund seekers, fund providers, and the crowdfunding platforms that match the fund seekers with fund providers on an Internet platform (Ordanini et al., 2011;Vural & Doğan, 2019).

Fund Seekers: They are the entrepreneurs seeking capital for their projects. Fund seekers design a product or service, and offer this design to fund providers through the Internet platforms. In addition to the funding purpose, in using such a platform, entrepreneurs also aim to collect feedback from the market for their products and services, and to create publicity for their venture (Bealieu et al., 2015).

Fund Providers: They are investors or donors who support the projects financially. When participating to a crowdfunding model, fund providers act both on extrinsic motivators such as financial gain and reward, and on intrinsic motivators such as being part of a community, and to be a involved in a charity (Moysidou, 2017). Fund providers search the platforms, and based on their own interests and wishes, decide which project to support.

Funding Platforms: These are websites which bring fund seekers and fund providers together. The content and manner of application of internet platforms vary according to the purpose of their establishment (Ordanini et al., 2011).. Platforms provide technical services to improve the quality of venture projects, legal services to protect project ideas, and the rights of entrepreneurs and investors, and advertisement services, to reach bigger crowds by way of promotion. Crowdfunding platforms are for-profit websites, and they charge a fee by a certain rate over the total funding amount (Vural, 2019).

3. TYPES OF CROWDFUNDING

Crowdfunding is done in four ways (Zeoli, 2014):

1. Donation-based crowdfunding: Donation-based crowdfunding is in practice the most widespread model. Its essence is a platform (website) to communicate with the crowd of participants and reporting of project offers, such as the collection of funds for a specific, philanthropic goal or social sponsorship In this model participants are not rewarded

2. Reward-based (sponsorship model) crowdfunding: Reward-based crowdfunding allows people receive non-financial rewards in return for their contribution to projects. Donors are offered usually low-value items. Often this type of funding is tiered which means the more participant will donate the better reward he will receive. Sponsorship systems tend to focus on supporting the creative projects or units. Participants from the network "crowd" invest their funds in the Project, in order to support them. Fundraising for the project is clearly defined time, usually takes a few weeks to several months. Entrepreneurs or artists crowdfund the production cost of their record, movie, .game or product and allow the

donors to be first recipients one the production is complete (Pazovski & Czudec, 2014.

3. Loan-based crowdfunding: People lend money to individuals or businesses in exchange for that person's or business's commitment to repay over a time interval, together with interest payments. Lending-based crowdfunding enables the direct borrowing of funds, bypassing the traditional financial institutions, such as banks. This type of crowdfunding is largely an evolution of the peer-to-peer model of lending pioneered by firms. Two approaches can be distinguished: microfinance and social lending. Peer-to-business resembles micro-financing so projects and businesses seeking debt apply through the platform uploading their pitch, with members of the crowd taking small chunks of the overall loan. Micro-lending solution is a financial aid usually used by the poorest, offered in small amounts, collected and distributed by non-profit and social focused platforms. Others like social lending operate as an investment – free funds are allocated and lent to certain rules. Payment plus interest might be returned in a lump sum or along some sort of payment schedule (Gulati, 2014). Social lending relate to higher amounts making it the second largest category of world crowdfunding market, as measured by the monies raised. Crowd lending is considered a threat to the big lending businesses as global banks.

Type	Form of Contribution
1.Donation Based Crowdfunding	Donation
2.Rewards Based	Donation/Pre-Purchase
3.Lending Based Crowdfunding	Loan
4.Equity Based Crowdfunding	Investment

Source: Pazovski & Czudec, 2014

4. Equity-based crowdfunding: Equity based crowdfunding is the collective effort of individuals who network and pool their money, usually via Internet to investing for equity, or profit/revenue sharing in businesses or projects. Contributors are rewarded an equity stake in a company in return for their investment. The value preposition being offered is company ownership or voting rights (Gulati, 2014). This embodiment provides range of solutions to assist start-ups and companies in early stage of development. Project initiators and their partner platforms define o time period and a target amount of money which serves as a threshold (Hemer, 2011). Money target is divided into equal slices which are offered via the platform as equity shares (or stocks) to the crowd at fixed prices. Collecting money lasts until the threshold is reached and then investment phase begins. In

this type of crowdfunding three models can be recognized. First is collective investment which combine the assets of various individuals (e.g. business angels), and organizations to create a larger, well-diversified portfolio. In return investors expect dividends or share in future profits. Business angels investments require a high return rate as they are at high risk (Dziuba, 2012). Second is investment fund which can be defined as a supply of capital belonging to numerous investors that is used to collectively purchase securities while each investor retains ownership and control of own shares. Benefits in the form of shares allow to separate distinct securities-based (equity) model. Securities-based funding gives ownership, or a promise of future revenue to investors in equity or debt. This model implies the sale of shares and transfer property rights to online investors. Internet platforms with the most technological advancement support equity-based model (Pazovski & Czudec, 2014.

4. CROWDFUNDING PROCESS

With a simple explanation, crowdfunding is collection of funds by entrepreneurs or project owners, for the venture or project they would like to get realized, from big crowds and in small amounts from each individual, through the Internet. With crowdfunding, entrepreneurs obtain the funds they need through the power of crowds, without depending on corporate financing sources (Deacon, 2018). Figure 1 indicates the crowdfunding process.

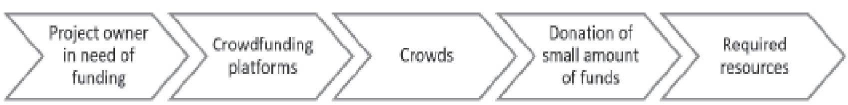

Figure 1. Crowdfunding Process

Crowdfunding system helps the ones that require funds to realize their projects, without borrowing, effectively and rapidly. At the same time, the system enables fund providers to support the projects they value, in return for rewards. The system as a whole is promoting entrepreneurship. The projects in question can be an innovative product, and/or service delivery and marketing, and they can also be social benefit projects. For example, a crowdfunded project might be about a high technology commodity or service, another one might have social or economic content. There are two different approaches to crowdfunding. In the first one, the crowd supports the project only financially. If the project owner reaches the targeted amount, it gives rewards to fund providers in proportion to their funding. In the second approach, the crowd both provides financial support and may become a part of the creative process Sakarya & Bezirgan, 2018; Hemer, 2011).

Crowdfunding process includes these steps: In the first step of the process, entrepreneurs submit their project to a selected online crowdfunding platform. The application may include a presentation, text, drawing or video, according to preferences. In the second step, if the project is accepted by the platform, the amount of funds required to realize the project should be announced, and a term should be determined, during which funds will be collected (Buysere et al., 2012). Another task of this step is to specify the benefit or advantage that will be provided to the persons supporting the project, in return for their contribution. The entrepreneur sets the financing target for a specified period of time and shares the project information on the online platform that will connect the entrepreneur to potential investors. This means an opportunity for investors or the public in general, to invest in the announced ventures. As the campaign moves forward, project owners should disclose developments of the process to investors, continuously updating information. The last step is, where the funds are collected. Investors examine the proposed projects, select the one they like most, and invest in an amount they would like to. The crowdfunding platform also acts as the payment agent. As may be allowed by the infrastructures of platforms, payments can be made by credit card, PayPal, virtual card, electronic fund transfers or other types of money transfers. If the targeted amount of funds is collected within the specified period, then the platform deducts a fee of 5% to 10% and pays the remaining amount to the project owner. If the targeted amount cannot be collected within the specified time period, some platforms return the funds to contributors without deductions, while some others transfer the funds to the project owner after deducting their fee, even if the targeted amount was not reached (Türe, 2019). Even though this system functions effectively, there are always risks that may affect the confidence in the system, so the parties should be aware of those risks.

5. RISKS ASSOCIATED WITH CROWDFUNDING

Investors usually wish to participate in crowdfunding initiatives, but there are some risks associated with it, especially from the perspective of investors. Major risks are as follows.

Fraud: Fraud constitutes the biggest threat to crowdfunding campaigns (Collins & Pierrakis, 2012). Traditional reputational and legal enforcement methods may not work with such campaigns. First, sellers traditionally want to protect their reputation and goodwill because they often want repeat customers; however, the incentives to not receive a bad review or a bad reputation may not work within the context of crowdfunding because of the anonymity of the Internet and because they do not repeatedly fundraise (Weinstein, 2013). While fund-seekers may not be repeat players, platforms are. To succeed, these platforms have incentives to avoid a reputation as a bad marketplace, to avoid attracting fraudulent schemes and to perform due diligence for each project and throughout the campaign (crowdsourcing.org., 2013): platforms may associate with banks that have experience evaluating fraudulent projects; platforms can stagger the fund release to limit the size of the funds affected (Collins & Pierrakis, 2012); etc. Markets, accordingly, have a place to play to prevent fraud. Second, legal enforcement may also fail because each individual investor does not have enough incentive to sue for fraud or breach of contract, because crowdfunding relies on small investments from many investors instead of large investments from a few investors; hence, these small amounts do not provide each individual investor with enough incentive to investigate and report fraud. Consequently, crowdfunding investors can become targets for fraudulent activities including fraudulent and pyramid schemes. Fraud is a real risk but platforms and the crowd have their place to play in preventing fraud (Ramos, 2014).

*Incompetence:*Apart from intentional fraud, projects may unintentionally fail because entrepreneurs are incompetent or have miss-calibrated their projects. The wisdom of the crowds and the all-or nothing model temper issues of incompetence because the crowd gravitates towards projects that send the correct signals and enough investors must perceive the same signals for the project to become viable. Much like with fraud, the level of investment from friends and family sends signals about the quality of the entrepreneur (Agrawal, Catalini, & Goldfarb, 2013).

Lack of efficient secondary market for equity-based crowdfunding Investors, much like campaign creators before them, may struggle to price their investment when they exit if they cannot use market mechanisms. For equity-based crowdfunding, the slow development of a secondary market (Agrawal, Catalini, & Goldfarb, 2013) also slows the development of the primary market. While investors join a project for different reasons, the majority participates with the expectation to break even (Schwienbacher & Larralde, 2010). In order to recoup their investments, they must sell their shares back to the entrepreneur or to other investors (Ahlers, Cumming, Günther, & Schweizer, 2013).

*Security of the Crowdfunding Portal or Platform:*In recent years, hackers have displayed an alarming ability to break into seemingly impenetrable data repositories of leading companies and financial institutions and steal credit card details and other valuable client information. A similar risk exists for crowdfunding portals and platforms, which are vulnerable to attacks from hackers and cyber-criminals. So in addition to researching the investment itself, make sure to look closely at the platform, too (Picardo, 2020).

Years to Materialize: Every investor expects some future return. However, returns on equity crowdfunded ventures may take many years to materialize if at all. For example, management may deviate from the business plan or have difficulty scaling the business. Over time, this may lead to capital erosion rather than wealth creation. There may be an opportunity cost attached to your investment that you should consider since it ties up capital that could be used elsewhere (Picardo, 2020).

Lower-Quality Investments the Norm: For skeptics, the question arises whether a company would only use equity crowdfunding as a last resort. For example, if a company is unable to attract funding from conventional start-up funding sources like angel investors and venture capitalists, perhaps then it would turn to equity crowdfunding. If that is indeed the case, then equity crowdfunded businesses are likely to be more mediocre investment opportunities with limited growth potential.

6. TURKISH PRACTICE OF CROWDFUNDING

Crowdfunding model has helped to realize many ideas in the world since the beginning of the 2000s. In Turkey, however, it is quite a new concept, as the first platform of crowdfunding was launched in 2010. Until 2017, there has not been a legal regulation for the crowdfunding model in Turkey. This condition of non-regulation restricted crowdfunding platforms to offer only reward-based and donation-based models (Vural & Doğan, 2019).. Crowdfunding platforms operating in Turkey have supported the realization of many ideas since 2010. The law enacted in 2017 determined the principles to ensure confidence in these platforms, with regards to their operation, supervision, and audit. The Law also regulated the equity-based crowdfunding model (Münyas & Yıldız, 2019).

In 2017, amendments were made to the Capital Markets Law numbered 6362, which enabled financing in Turkish capital markets through crowdfunding. The Decree on "Equity-Based Crowdfunding", which was published in the Official Gazette dated October 3rd, 2019 and numbered 30907, detailed the technical and legal infrastructure of crowdfunding, which had been regulated in the Law in general terms (https://www.resmigazete.gov.tr/eskiler/2019/10/20191003.pdf).

The Decree set forth the rules and procedures for crowdfunding, which have been applied since then, in the crowdfunding processes in Turkey. There has not been any regulation on other types of the crowdfunding model. According to the new regulation, crowdfunding can be carried out through the crowdfunding platforms that are established with this purpose, and which have to obtain a permit from the Capital Markets Board (CMB). Any equity-based fund collection transaction carried out by another method or intermediary shall be null and void. As a rule, the whole process of a fund collection initiative (campaign) that runs on online platforms should be transparent and open to the public. Additionally, crowdfunding platforms are able to start operations only after obtaining a permit from the CMB, in other words, after being included in the related list (Kitle Fonlaması Tebliği- 35/A1, 2019).

A venture company that is in need of funds and would like to collect funds according to the Decree should have been completed its establishment procedures before starting a crowdfunding process. Fund seeking venture company connects with investors through the crowdfunding platform and collects funds in the form of investment. A campaign of fund collection starts when a venture company or entrepreneur applies to a crowdfunding platform, requesting to initiate a crowdfunding process (Kütükçüoğlu, 2019). The running campaign should finish before the same venture company or entrepreneur can start another campaign. The crowdfunding platform's investment committee approves the information form, which is then published on the campaign page of the platform's website. The campaign starts as of the date this form is published and can last for a maximum period of sixty days. Throughout the campaign, investors post their requests to fund the related venture company or entrepreneur to the platform. Funding can only take place by way of a capital increase. Following the increase of capital, collected funds are transferred to the venture company in the form of shares that are issued as the result of the capital increase.

A company cannot collect funds by selling its existing shares. Also, shares issued via capital increase do not have voting rights. The payment of the funds in return for shares should be made in cash. At the end of every day, as the campaign continues, platforms report the contribution requests of investors to Merkezi Kayıt, İstanbul. Collected funds will accumulate in the accounts opened with an escrow agent, in the name of the venture company or the entrepreneur. The escrow agent will not allow the account owner to access the funds throughout the campaign and transfer them to the account owner when the conditions are met (Erdem & Erdem, 2019).

7. THE REQUIREMENT OF AUDIT AND ASSURANCE IN CROWDFUNDING AND THE RELATED REGULATIONS

Persons and entities comprising the society closely watch enterprises because of their economic interests. As the economy and technology evolve rapidly in today's society, ventures and enterprises also grow in this direction. Moreover, as enterprises become more effective, the number of parties interested in these enterprises is increasing. Users of information are; persons and entities which use and analyze the financial information disclosed by the enterprise management, and trust the auditor's opinion. Parties that are interested in an enterprise wish to have reliable and substantial information on the enterprise, in line with their own benefits. If inaccurate or unclear information is obtained from enterprises, persons and entities will make wrong decisions, leading to many adverse situations affecting the society and the national economy (Selimoğlu & Uzay, 2009). At this moment, it comes to mind whether the financial information of enterprises is reliable and unbiased.

There might be times when it is highly probable that the information is unreliable and biased. In the global economy, growing enterprises end up with an increased number of accounting transactions, which, at the same time, become more complex. This brings along an increased probability of erroneous and fraudulent transactions. Because many of the information users are away from the enterprise, they doubt the reliability of the information, and have difficulties in ensuring this reliability (Ittonen, 2009). Information providers, i.e. the managers of enterprises, may feed misleading information to users of information, intentionally or unintentionally. Therefore, as the need for reliable information increases, the information presented by enterprises is questioned more and more (Salehi, 2010). Right decisions cannot be made upon unreliable information, therefore it is important for users of information that this risk is mitigated. Users of information are in need of independent audit and assurance services, which would set the conformity level of the information according to independent and predefined standards (Sijpesteijn, 2011).

To point out briefly, crowdfunding requires independent audit and assurance services. Independent audit and assurance services are necessary, to oversee the use of funds collected via crowdfunding, to see whether they are being used efficiently and effectively, to protect the investors' benefits, and minimize their losses. Looking at the legal regulations on independent audit and assurance from the perspective of crowdfunding, other than the USA and a few countries in Europe, crowdfunding is not subject to a fully effective and efficient audit, because of lack of regulations. Existing regulations and capital market laws only cover the equity-based crowdfunding model (ASC, 2017).

Equity-based model of crowdfunding dates back to the year 2009. First legal regulations covering this model were enacted in the USA. As a requirement of the Securities Act of 1933, all securities offered to public have to be registered with the Security Exchange Council (SEC), and entrepreneurs are not allowed to request funds from unaccredited investors (Weinstein, 2013). These measures aiming to protect investors also had been a barrier in front of equity-based crowdfunding. With the JOBS Act (Jumpstart Our Business Startups) of 2012, crowdfunding regulations have started to be issued. The Act brought regulation and supervision to both entrepreneurs and crowdfunding platforms, aiming to create a secure investment environment for investors Rampton, 2016). The purpose of the JOBS Act is to create investing opportunities for small investors and to create domestic enterprise funding for small, entrepreneurial companies (Smith, 2019).

Audit is necessary in crowdfunding, especially because it is a field vulnerable to fraud. The basis for the regulations is clear: In order for crowdfunding to become a viable and lasting means of funding for emerging companies, fraud has to be limited; unsuspecting contributors, donors and investors must be protected (Cornell & Luzar, 2014). To prevent fraud, audit and supervision mechanisms should be run strictly, to protect investors. Fraud is a real risk but platforms and the crowd have their place to play in preventing fraud (Gabison, 2015). Crowdfunding regulations of the USA, where it developed, are as follows.

Regulation Crowdfunding (17 CFR 227, 2016) was enacted under Title III of the Jumpstart Our Business Startups (JOBS) Act on May 16, 2016, to govern the offering and sale of small company equity and debt securities (here in referred to as "equity crowdfunding") to the public (Pub. L. No. 112-106, 126 Stat. 306, 2012). The act was intended to stimulate the economy and boost small business growth and capitalization by allowing many investors to make small investments online, while at the same time reducing the costs and burdens of making an initial public offering (IPO) (Securities and Exchange Commission (SEC), 2016). The "crowd" can be made up of both accredited and unaccredited investors. 1 Under Regulation Crowdfunding, a small business may offer unregistered securities up to $1 million (inflation-adjusted) in a 12-month period through an SEC-approved intermediary. The assurance and disclosure requirements vary with the size of equity crowdfunding campaigns. Each campaign is assigned to a tier that is determined by aggregating the issues in the previous twelve months, including the current offering's oversubscription amount. The oversubscription amount is the maximum amount the issuer will accept in the current offering. Tier 1 (campaigns less than or equal to $100,000 in 2016) requires the least assurance in that the financial statements and tax data must only be certified by an executive officer of the issuer. Tier 2 ($100,001 to $500,000) requires certification and an independent certified public accountant (CPA) review. Tier 3 ($500,001 to $1 million) requires certification and independent CPA review for the first issue under Regulation Crowdfunding, and audited financial statements are required for subsequent issues. All dollar amounts are adjusted annually for inflation. If the issuer has audited financial statements, they must be included at any tier.

A review provides much less assurance than an audit for a much lower cost.2 Each offering tier requires that the issuer disclose two years of financial statements, or since inception, if shorter. The required statements are the balance sheet, statement of comprehensive income, statement of cash flows, and statement of changes in stockholders' equity, all prepared in accordance with U.S. Generally Accepted Accounting Principles (GAAP). Notes to the financial statements are included and the financial condition of the issuer is discussed, which include material trends, uncertainties, historical data, liquidity, and capital resources. Additional required disclosures include the current number of employees and a discussion of the material risk factors of the administering the campaign. The intermediary may reasonably rely on the investor's representations including those regarding annual income, net worth and other investments made.

8. TURKISH REGULATIONS ON THE AUDIT OF CROWDFUNDING

It is important in crowdfunding that it is checked/examined whether the collected funds are used effectively and efficiently. The function of audit and assurance protects the interests of investors and minimizes their losses. Particularly, considering the risks of crowdfunding, control function needs to be supported by regulations. In Turkey, the Decree on *Equity-Based Crowdfunding* was issued by the Turkish Capital Markets Board (SPK), and was published in the Official Gazette dated October 3rd, 2019, and numbered 30907 (Küçükgüngör, 2019). This regulation is important for the protection of investors, and the creation of a more transparent and reliable market. Under the principle of transparency and

[2] "In a review of financial statements, the auditor seeks to obtain limited assurance as a basis for reporting whether the auditor is aware of any material modifications that should be made to the financial statements in order for them to be presented in accordance with an applicable financial reporting framework. A review is substantially less in scope than an audit, and often is performed for privately held companies that are required to provide financial statements to outside parties such as banks, creditors, or potential purchasers. Reviews of financial statements are conducted in accordance with the AICPA Statements on Standards for Accounting and Review Services , except for reviews of certain interim financial information that are conducted in accordance with the AICPA Statements on Auditing Standards."

full disclosure, obligations were imposed on the parties for matters such as the project's current status, and the use of funds (Fung, 2014). The regulation also imposes a mandatory independent audit under certain conditions. According to section 4 of article 20 of the Decree, a special purpose **independent audit report should be prepared**, for the audit of collected funds. That has been the first requirement of this kind, however, the required audit was not explained in detail.

The related articles of the regulation are as follows (SPK-Paya Dayalı Kitle Fonlaması Tebliği, 2019)

1. A report shall be prepared by the venture company or the entrepreneur, explaining the purpose, and the usage areas of the funds collected. This report should be published on the campaign page of the website, as of the beginning of the campaign (Article 20).
2. Collected funds shall not be used to purchase, or to finance the purchase of the real estate, rights based on real estate and real estate projects, directly or indirectly.
3. Between the end date of the campaign and the date on which the collected funds are totally utilized, every six months, and in any case on the date the funds are totally utilized, announcements shall be made on the campaign page, containing the current status of the project and the usage areas of funds.
4. An independent audit company shall check and audit whether the funds collected are used in line with the purpose announced with the information form. This shall be carried out by an independent audit company which is included in the list according to the Law, and by way of a special purpose independent audit report. The special-purpose audit shall be conducted annually for venture companies collecting funds more than 1,000,000 Turkish Liras, starting with the date the funds are transferred to the venture company. For venture companies collecting less than this amount, the audit shall be conducted on the date announced in the information form when the funds will be totally utilized. In any case, without considering the collected fund amount, an audit should be conducted when the collected funds are utilized totally.
5. Reports stated in paragraph four shall be prepared in thirty days following the date of obligation, delivered to the venture company in five business days after they are signed, and announced on the campaign page and at the venture company's website in two business days after they are received by the venture company.
6. If the independent audit company's report stated in paragraph four detects that the funds were not used as announced in the information form, or if there have

been actions to prevent conducting the required examinations, the independent audit company shall inform the Board immediately on these matters.

7. The venture company's board of directors is responsible for ensuring that the funds collected are used in line with the previously announced purpose.
8. If the independent auditor's report stated in paragraph four detects that the funds were not used as announced in the information form, and this finding is reported to the Board, such case shall be reserved, where the Board reports it as a crime under the provisions of the Law numbered 5237.

In summary, there is a checking and auditing process in place, to detect whether the funds collected through crowdfunding are used for the right purposes. The company conducting the audit shall be an independent audit company which is included in the related list according to the Capital Markets Law. This company prepares a **special purpose independent audit report**. Consequently, the confidence in the system is supported by ensuring transparency. However, the independent audit obligation applies only to equity-based crowdfunding, and if the obligation is expanded to donation and reward-based models, this will improve the efficient and effective use of funds (Havrylchyk, 2018). The regulation should set forth the rules of checking and audit in detail, to prevent inaccurate information, to ensure the confidence of fund providers, thus ensuring an effective crowdfunding system. It is the duty of the lawmakers and regulators to extend the existing rules of accounting, governance, audit and assurance to new and alternative financing models.

Functioning as secondary legislation, the Decree regulates the equity-based crowdfunding model which is an innovative financing model. This new financing model regulated by the Decree has the potential of supporting economic development as was the case in other countries of the world, and it is encouraging for innovative and technology-focused entrepreneurs, with regards to the model's capacity to provide the required funding to realize technology and/or production activities. Increased transparency is key to the success of this innovative approach and to achieving the act's objectives. The transparency of the process can be economically achieved by relying on the crowdfunding platforms' operation through auditor reports. Auditors and accountants are in an excellent position to advise companies or investors on this new process and to increase the transparency and efficiency of these capital markets.

CONCLUSION

One of the vital elements of economic life is accessing capital, or providing financing. Technological advances of the recent years have led to the search of new financing models. One of the results of this search has been the crowdfunding model. This method based on crowdsourcing principle, helps entrepreneurs who cannot obtain loans from financial institutions, and the ones that are at the initial idea stage. Crowdfunding can be based on equity, donation or rewards, and it is still growing in the global markets. Despite the benefits being granted, crowdfunding also brings along significant risks such as fraud. Therefore, as the crowdfunding model gains popularity, it is important that risks are mitigated and precautions are taken, the major initiative being the regulatory framework. Audit and assurance services are important to reduce the risk of fraud. From this perspective, the CMB's regulation of equity-based crowdfunding is considered as an important step.

In crowdfunding, entrepreneurs are able to reach a wider audience of investors, comprised of both experienced and inexperienced ones. Thanks to this model, they can overcome the monopolistic power of banks, lower their costs, while at the same time providing new investment instruments to the market and deepening the capital markets. Excluding a couple of countries, audit of crowdfunding activities is not effective and efficient enough, lagging behind the audit activities for other financing models.

Therefore, it is necessary that both the International Accounting Standards Board (IASB) and the Public Oversight Accounting and Auditing Standards Authority (KGK) of Turkey regulate crowdfunding and create a mechanism for the audit of investors and fund collectors. Regulations should aim to mitigate the risks of crowdfunding, serving for a more transparent and reliable investment environment. Crowdfunding has an increasing momentum these days, with regards to the purposes of strengthening the capital structure, making use of the economies of scale, and creation of well-organized corporate structures. When crowdfunding activity is carried out through online platforms, transparently and as being subject to audit, investors are protected better, and the confidence of markets are maintained. Regulations will ensure that investors and entrepreneurs will match in a secure environment, attracting more foreign investors in the meanwhile.

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