The Innovative Finance ISA Guide

2023

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Risk warning

Past performance and forecasts are not reliable indicators of future results. Tax treatment of any of the investment offers will depend on the individual circumstances of each investor and may be subject to change in the future. If you are unsure about any aspect of the information provided by the company, you should seek advice from an independent financial adviser. Do not invest more than you can afford to lose. Investing in start-ups and early stage businesses involves risks, including illiquidity, lack of dividends, loss of investment and dilution, and it should be done only as part of a diversified portfolio. Investing in start-ups may expose the individual concerned to a significant risk of losing all of the money or other assets invested. Peer-to-business lending through Crowd2Fund is not the same as holding a bank or building society savings account. When making a peer-to-business loan, your capital lent to a borrower is not covered for compensation in the event of a loss by the Financial Services Compensation Scheme. It may prove impossible to recover all or part of the loan by calling in the business assets held as security on that loan. Reward and Donation funding types are not regulated by the Financial Conduct Authority.

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Registered No. 08472687 Registered Address: 242 Acklam Road, London, W10 5JJ.

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Contents

“For entrepreneurs, by entrepreneurs: Growing innovative businesses, and giving entrepreneurial investors control”

Established in 2014, Crowd2Fund is a leading investment platform, building long-term relationships between investors and the great British businesses they invest in.

Crowd2Fund was the first platform to offer the Innovative Finance ISA in the UK. We were recently awarded Triple Gold ‘Most Innovative Platform’ for the third year running at the prestigious 2023 MoneyNet Awards and named the ‘One to Watch’ Best Peer-to-Peer Lender at the 2019 Growth Finance Awards.

GROWTH FINANCE AWARDS | 2019

moneynet Award WINNER 2023

moneynet DOUBLE GOLD 2022 & 2023

Innovative Finance ISAs generate tax-free earnings as you help British business grow.

Introduction to Innovative Finance ISAs

IFISAs give the public the opportunity to get involved in innovative businesses and exciting new markets, and see potentially great returns on their investments — appealing to the entrepreneur inside us all. Launched in 2016, the popularity of Innovative Finance ISAs, or IFISAs, is growing fast.

With average bank interest rates hovering around 1% for nearly a decade, IFISAs are increasingly popular with savers looking to increase their income, as well as with investors looking to diversify their portfolios. IFISAs can both outstrip the levels of return offered by Cash ISAs — although bank savings in Cash ISAs and IFISA investments are very different in terms of risk — and potentially provide less volatile returns than Stocks and Shares ISAs.

According to the Peer-to-Peer Finance Association, by the end of 2022, investors interested in supporting growing British businesses had subscribed £1 billion through IFISAs across more than 40,000 accounts. For engaged investors looking to support entrepreneurial businesses, and tap into new and exciting markets, an IFISA is an excellent opportunity to explore.

Innovative Finance ISAs give everyone the power to back entrepreneurs and businesses they believe in — while funding a vital part of our economy and, ideally, seeing healthy returns on their investment at the same time.

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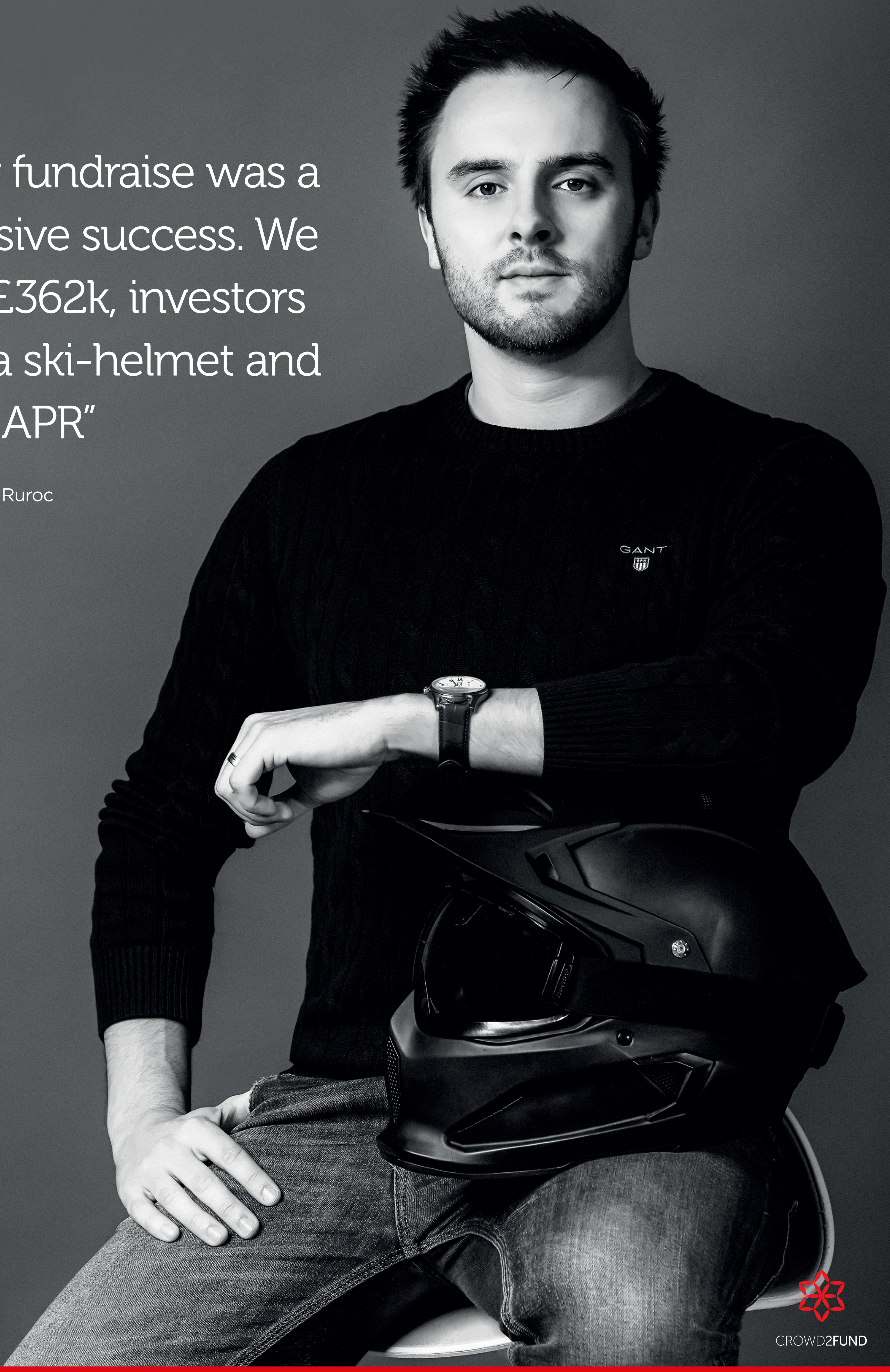
“Our fundraise was a massive success. We got £362k, investors got a ski-helmet and 10% APR”

Dan Rees, Ruroc



What is Innovative Finance?

The financial services sector has long been in need of drastic modernisation. The UK is leading the charge to upgrade capitalism, offer more choice to consumers, and deliver prosperity and social mobility through new financial technologies — otherwise known as FinTech.

Innovative Finance refers to sectors like peer-to-peer lending, or debt-based crowdfunding. IFISAs are a new method of lending that bypasses banks by investing in individuals or businesses directly, in exchange for a return. The platforms in this space have developed an innovative way to offer more direct, higher-paying investments.

Historically, investors have been restricted to investing in a small number of multinational corporations that make up a typical stocks and shares portfolio — which are often inefficient and may carry ethical concerns. These limitations are not unique to the UK, and constantly flooding the same global corporations with investor money poses a systemic danger to our economies.

With an IFISA, we can now unleash money from the control of these corporations and invest in small and medium-sized businesses — which actually account for 90% of the UK economy.

Bank of England base rate: 3.5%

(As of 30 Jan 2023)

Target IFISA return = 6% to 18% before fees, bad debts and depending on investment grade

What does IFISA stand for?

IFISA stands for Innovative Finance Individual Savings Account. All ISAs are tax-free savings vehicles, introduced by the UK government to encourage saving and investing. With an IFISA, you can invest in “innovative finance”, tax-free. It’s important to understand that this differs from a Cash ISA, which is a savings account held in a bank, and while IFISAs offer higher rates of return, they are also are higher risk.

How do IFISAs differ from other ISAs?

With Stocks and Shares ISAs, returns come from dividends, or the increase of a company’s share price — however they are highly volatile and market dependent. Returns on Cash ISAs are generated by interest on the amount deposited in the savings account — as they carry very little risk, they also offer very little reward, with low rates of return.

Unlike these, IFISA returns are generated from the interest on loans made to growing businesses. These loans are issued through a public platform by small and medium-sized businesses.

With IFISAs, you are lending your money to businesses via an online platform, rather than putting it in the bank. IFISAs can offer higher rates of return, but they are riskier than Cash ISAs. Some of these ventures may fail — there is the risk of losing your capital, or not receiving the target returns. However, the vast majority of these businesses repay the loans in full, with interest. It’s important to build a diversified portfolio to manage your risk; if one business you lend to fails, the interest earned on other investments should be able to cover the loss.

The Five I's of IFISAs

There's a simple way to remember what makes the Innovative Finance ISA different – The Five 'I's of IFISA.

INVESTMENT - Not savings
The most obvious difference between an IFISA and a Cash ISA is that an IFISA typically advertises a higher rate of return. That's because they are an investment in businesses which carries higher risk, rather than a basic deposit account. Returns are also higher because IFISA platforms cut out the middle-man between the investor and the business seeking the loan.

INTEREST - Not equity
A Stocks and Shares ISA purchases the equity of publicly traded companies that are listed on a stock exchange, often via larger funds which can incur fees. An IFISA allows you to lend directly to businesses and entrepreneurs, and these loans are repaid directly by the business, with interest.

ILLIQUID - Not liquid
Buying equity shares in the stock market through a Stocks and Shares ISAs means the value can rise or fall in line with the performance of a company, fund or index. As you can usually sell your shares at any time, stocks and shares are considered liquid. With an IFISA, you are investing your money through a loan, in anticipation of a certain level of interest — and returns depend on successful repayment. Because the IFISA investments are debt-based, they are usually offered for a fixed term.

If you need access to your capital, then you may be able to sell your loan to another investor. Many IFISA platforms allow their customers to buy and sell loans to each other. For example, Crowd2Fund operates The Exchange, where investors can simply buy and sell their loans through the platform. The seller of the loan sets the interest rate, and it's possible for both parties to make money through selling loans at a higher rate or picking up bargains from sellers setting a lower rate to encourage a quick sale. Access to your capital is not guaranteed because it may not be approved for listing on the Exchange by Crowd2Fund or there may not be investor demand to purchase it from you via the Exchange after listing.

INVOLVED - Not passive
Many IFISAs allow you to lend directly to businesses that you choose. This gives you full control over where your money is going. You can invest in businesses that you believe in, causes you care about, and entrepreneurs you want to see succeed. With Crowd2Fund, you can also ask questions directly to the businesses through the platform.

INTERACTIVE - Not stagnant
IFISAs are offered by internet based FinTech platforms. This creates a unique investing experience that can be accessed from anywhere, at any time. These platforms are often user friendly and built to make the investing process simple and transparent. For example, you can manage your Crowd2Fund IFISA through the intuitive mobile app whenever and wherever you want.

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"I've been in hospitality for 30 years and wanted to pay 10% interest back directly, and invite investors along for a margarita!"

Phillip Oppenheim - Cubana

ISAs: Key Information

- You can invest up to £20,000 per tax year and your earnings will be tax-free.
- You can easily transfer an old ISA free of charge into an Innovative Finance ISA.
- You can only have one IFISA in a tax year, with one provider.
- You can use your ISA allowance in a combination of Cash or Stocks and Shares, Innovative Finance or Lifetime.
- The £4,000 maximum you can put in a Lifetime ISA is part of the £20,000 maximum ISA limit — so you still have £16,000 to invest or save tax-free.

What are the different types if ISA?

	Limit	Risk level	Typical interest/return	Features
Cash ISA	£20,000	Low	Low <2%	Allows savers to deposit savings up to the annual limit in accounts covered by the Financial Services Compensation Scheme.
Stocks and Shares ISA	£20,000	Low to high depending on type of fund or shares held	Varies depending on risk level, performance and fees. Equity not debt and therefore capital growth rather than interest	Up to £20,000 can be mix of stocks and shares and cash, can be "flexible" so you can take money out and put it back in without losing the tax-free status of that bit of your allowance.
Junior ISA	£4,260	Low to high depending on type of fund	Varies depending on risk level, performance and fees. Capital gains rather than interest	Cash or stocks and shares or a combination of the two. In the child's name so does not form part of your £20,000 annual allowance. The child can access the pot when they reach 18.
Innovative Finance ISA	£20,000	Medium to high depending on diversification/ interest rate	Varies – around 5 to 15%. Debt-based, therefore pays interest not capital growth	Introduced April 2016. Only one innovative finance platform per ISA per year. Can invest in a range of projects or credit profiles on the same platform to diversify. Can also invest in other types of ISA alongside, up to the maximum annual limit.
Lifetime ISA	Up to £20,000 (but only first £4,000 eligible for the bonus	Cash or stocks and shares. Low to high	Varies depending on type/risk level, performance and fees. Equity not debt, therefore pays capital growth not interest	Government will top up annual savings of up to £4,000 with a 25% bonus, meaning they will contribute a maximum of £1,000 in any one tax year. You must be over 18 but under 40 during the tax year to open a LISA and government will only pay the bonus up to the age of 50. Savings in the LISA must be used either to buy a house or towards a pension. Pension can be accessed from age 60. Part of annual £20,000 allowance (giving £16,000 left over). Cannot have one of these and a Help to Buy ISA.

Maximising your IFISA returns

By Chris Hancock, Founder of Crowd2Fund

Crowd2Fund believes that everyone should be backing entrepreneurs; they are the lifeblood of the economy and create new products and services for us. IFISAs present a brilliant opportunity to invest in the growing businesses you believe in, while seeing potentially great returns for your personal portfolios.

Take advantage of tax breaks

Investing in an IFISA allows funds to grow tax-free, as they are held within the ISA tax-free wrapper. This ensures that interest repayments are not subject to income tax, which is 20% for basic rate taxpayers on non-ISA interest above £1,000.

Additionally, no income tax is payable on IFISA funds when they are eventually withdrawn. This is one of the reasons the IFISA is such an attractive investment vehicle for building up wealth long-term. Also, while IFISAs do form part of an estate for inheritance tax purposes, they can also be passed on without incurring any associated tax if left to a spouse.

Use the full allowance

Each year, HMRC sets a tax-free savings allowance that can be spread across the whole ISA range. The current allowance is £20,000. This allowance isn't transferable between different years — unused allowance is lost forever when the new tax year rolls in. To shield as much of their savings as possible from tax, investors usually aim to use the entire allowance, or as much as possible, prior to the 5th April in any tax year. If you have used up your full allowance and are married, remember — you can take advantage of your spouse's allocation to shelter up to £40,000 per year from income tax.

Transfer historic lower yield ISAs

While the annual allowance for new investments is not transferable, it is possible to transfer historic ISAs into Crowd2Fund's IFISA — or any IFISA of your choice. This point is particularly useful for holders of Cash ISAs, as even the best performing easy access APR Cash ISAs currently generate a return of around 1% - 3% — again, cash and investments are very different in terms of risk.

As has been the case for nearly a decade now, investors looking to increase returns beyond the 1% Cash ISA APR need to take on investment risk and peer-to-peer loans within an IFISA are one of the many options available. Cash ISAs can easily be transferred to the Crowd2Fund platform by downloading and filling in a form.

Reinvest and reap the rewards of compound interest

If you are a Crowd2Fund IFISA investor, you will receive repayments every month. You can redeploy these funds into new investment opportunities. This means you will continue to be paid interest on your earnings, which can multiply exponentially over time. To increase returns even further, you can reinvest your repayments on a monthly basis into a specific business, providing you are lending £100 or more. With Crowd2Fund, if your monthly repayments are lower than this, you can use the Smart-Invest feature — Smart-Invest automatically reinvests your repayments in the live investment opportunities that fit your selected risk profile, spreading your risk and diversifying your portfolio.

Diversify your portfolio with The Exchange

Spreading your risk is an essential tool for managing the inevitable element of risk that comes with any investment. Diversifying your portfolio across a range of different companies and sectors reduces your exposure to any single business risk. This means that should one loan go bad, you have plenty of others to fall back on.

In addition to the primary investment opportunities listed on the platform, investors are also able to use the Crowd2Fund Exchange to buy existing loans from other investors, increasing the range of investments available. Some investors who sell their loans may also be able to make a profit by selling at a higher rate for loans that perform well. Crowd2Fund is also the only IFISA on the market that gives you the choice to select the entrepreneurs you want to back rather than operating a pooled fund. Investors can personally assess and choose the companies and organisations they want to lend money to.

“Dr. Pedro Mendoza, founder of Keep Smiling - a cutting-edge Notting Hill dental practice raised £50,000”

Pedro Mendoza - Keep Smiling

The Crowd2Fund IFISA

With the Crowd2Fund IFISA, you control where your money goes. The flexible IFISA lets you choose the entrepreneurs you back, while potentially earning between 6 and 18% a year in returns before fees and bad debt, tax-free depending on the investment grade. Some businesses on Crowd2Fund even provide exciting tangible rewards to their investors, offering unique products or services in addition to great returns.

The investment platform is fully mobile responsive, and also boasts an IFISA iOS app. This makes it easier for you to manage your portfolio and engage with the businesses you invest in, whenever and wherever you want. To find out more visit www.crowd2fund.com/ifisa

Typical rates of return: Investments offer an interest rate between 6% and 18% a year before fees and bad debt, depending on investment grade. As of December 2020, the average interest rate was 11.07% before fees and bad debts. For updated loan book performance go to https://www.crowd2fund.com/loan-book-performance

Risk management: It is important that investors manage their risk by spreading their money across a range of different businesses, otherwise known as diversification. We also perform stringent due diligence processes and assessments and believe in transparency; investors have access to all the relevant information about each investment opportunity and can talk to the business owners directly through the Crowd2Fund platform.

Investor Fees: Investors are charged a 1% fee on interest and capital repayments. Based on this, an investor lending £5,000 to a business — at an APR of 9% over three years — would get back £5,723.95, minus £57 in fees and charges. To find out more, see: www.crowd2fund.com/amortisation

Business Fees: Crowd2Fund charges a business raising money a 6% fee on the total amount raised. To find out more visit, www.crowd2fund.com/fees

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“Our funding round had huge appeal. We got £42k, they got 12% APR and a case of the 2016 vintage.”

Linda Howard, - Giffords Hall Vineyard

Innovative Finance ISA FAQs

IFISA Pros and Cons - Why are rates of return on an IFISA typically higher than cash?

1. Higher risk.
Any company could fail, even if its historical performance has indicated a lower credit risk. The risk of failure of the company that you are lending to is one reason for the higher return. Remember, the nature of the risk varies between companies or projects — even when returns are similar. Debt-finance is also generally lower risk than equity. It's important to do your own due diligence and choose opportunities you are comfortable with. Crowd2Fund is transparent, and shares all relevant information about each investment opportunity, allowing investors to make their own balanced investment decision. Investors also have the ability to ask business owners questions through the platform if they have further questions.

2. Lower overheads.
Platforms that offer IFISAs are innovative in their own right. They are powered by the latest technology and are relatively new; they tend not to share the legacy of weighty overheads that larger, more traditional investment platforms have. These platforms pass on the savings from lower overheads to customers, in the form of higher returns.

3. Lower fees.
Partly because of the lower overheads, Innovative Finance platforms can afford to operate on lower profit margins than older businesses. This allows them to charge lower fees than banks for arranging finance deals between lenders and borrowers.

4. Choice and Responsibility.
If you back yourself as an investor, and select the right investments, you can potentially outperform the average through the success of the businesses you've chosen to support. Conversely, if you choose businesses that fail, your performance could be impacted. IFISAs give investors the chance to fully engage with the investing experience, and with that comes the responsibility of managing the outcomes. We always ask investors to do their own due diligence, and only take on risks they are comfortable with.

How much can I put in an IFISA?
For tax-free returns, up to £20,000 can be put in any type of adult ISA in a tax year, which runs from April 6th to April 5th of the following year. You could put the entire amount into an IFISA or split it between different kinds of ISAs. However, £20,000 is the annual tax-free maximum — regardless of the ISA type or types you choose.

For example:

Mr. Edwards is 38 and wants to take advantage of the Lifetime ISA for his retirement savings. He also wants to support smaller businesses and likes the idea of an IFISA. He has £10,000 to invest in this tax year; the maximum he can put in his Lifetime ISA is £4,000. Mr. Edwards chooses to take the full Lifetime ISA available and put the remaining £6,000 in an IFISA, to invest through a peer-to-peer lending platform, effectively splitting his investment.

Why would I choose to invest in an IFISA?

The answer to this question is varied, depending on the type of loan you are making, the type of borrower, and whether an IFISA is right for you as an individual.

1. You want to invest in entrepreneurs and support the local economy. You are prepared to invest in riskier investments and accept that your principal investment and any target returns are not guaranteed.
2. You want to support small businesses and develop meaningful relationships with your money.
3. You're an entrepreneurial investor with an interest in where your money goes.
4. You want to be in control of your money and engage with the investment process.
5. You want to receive additional tangible rewards, like new products and services.
6. You want to try investing through a different channel, other than banks and stockbrokers.
7. You'd enjoy investing on an innovative platform when it suits you, online or via a mobile app.
8. You want to diversify your current portfolio.
9. You want to allocate part of your savings to peer to peer lending. It's important to understand that you should only invest what you could realistically afford to lose as IFISA investments are typically higher risk.

For example, you might also choose an IFISA to complement a Stocks and Shares or Cash ISA you already hold, rather than replace them entirely. A Cash ISA investor curious about IFISAs may set aside a small amount in an IFISA to add a little more income to their investment portfolio, without sacrificing more security than they are comfortable with.

Some investors simply find IFISAs more interesting; they allow you to engage with the process, decide which businesses you think are good opportunities, and choose the investments you really like.

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“Our investor community helped our upcycling business grow – and they grew their investment by 8% each year.”

Marie Cudennec - Goldfinger Factory

How do I choose an Innovative Finance ISA platform?

Remember, you can only invest in one IFISA in a tax year.

If you are interested in lending to small businesses, Crowd2Fund offers the unique opportunity to pick and choose the individual entrepreneurs that you want to invest in. You can find entrepreneurs in industries and causes that you are already interested in — for example, some develop environmentally-friendly products, have a focus on social good, or are passionate about a sport or activity. You'll know exactly where and who your money is going to and control stays entirely in your hands.

This is a very different investing experience compared to other platforms like Ratesetter and Zopa. These platforms pool all investors' money together and spread it out evenly across their loan books - both returns and losses are shared between all investors. These platforms decide where your money goes for you — as an investor, you have no control over where your investment is allocated. If you are interested in renewable energy investments, or perhaps property, there are also dedicated platforms for these particular opportunities such as Abundance Investment, Downing Crowd, Proplend and Property Crowd.

Why are IFISAs riskier than cash?
With Cash ISAs, you know you will receive the quoted interest rate — unless the bank or building society fails. IFISAs work differently. If you are lending to a group of individuals, there's a bad debt risk that may bring down your rate of return. This is why it's important to build a diversified investment portfolio and invest in multiple businesses. Cash ISAs with banks or building societies are covered by the Financial Services Compensation Scheme deposits cover, for up to £85,000. If the bank fails, any deposits up to that limit are protected. If an IFISA platform or your investment fails, you are not covered by the FSCS. Platforms that are regulated by the FCA — like Crowd2Fund — are required to have a wind-down plan in the event they decide to or are forced to stop trading. These plans are reviewed by the FCA but you are still not covered for bad loans.

How can I tell how risky an IFISA is?
Generally speaking, the higher the rate of return, the higher the risk level. You should always conduct your own due diligence on any investment opportunity. On further investigation of a higher rate offer, you may decide that the specific risks involved are ones you are prepared to live with — or not. Only invest in opportunities you are comfortable with. There should be a Campaign Page, Offer Document, or something similar, that clearly lays out what the risks are for any IFISA investment. Platforms usually state how much due diligence and credit-checking they perform, and should be happy to answer any questions you have directly.

Has anybody actually lost money through IFISAs yet?
Choosing a well-established, regulated platform with a strong reputation is important. Default rates are typically low, but there have been a few cases of peer-to-peer lenders failing, like BeTheLender in 2014 and Collateral in 2018. Not all these investors recovered their money. It's normal for any pioneering sector to have some failures, though these are limited. Unfortunately, a small number of Crowd2Fund investors have lost money — however, the earnings of the platform significantly outweighs the losses. You can learn more about Crowd2Fund statistics on: https://www.crowd2fund.com/fund-statistics.

Can I invest with different IFISA platforms in the same tax year?
No. All of your IFISA money has to be held with the same platform in that tax year. You are allowed to shift your IFISA pot between different platforms once a year, but you can't contribute to more than one at a time.

What happens if I transfer an existing ISA into my IFISA account during the tax year?
We make it easy for you to transfer and existing ISA into an IFISA using our ISA transfer form on our platform. When we've received the details of your old ISA and how much you wish to transfer, we work with your old ISA manager to move the funds to your Crowd2Fund account as quickly as possible.

What happens to my IFISA account if the company I invested in goes into default?
You will incur the loss of the loan if it is written off and not recovered. The loss will be reflected within your IFISA account where your balance will be reduced but it will not affect your annual subscription allowance. We have a well-established recovery process to maximise the chances of the recovery of distressed loans.

What happens to my IFISA account if Crowd2Fund goes into administration?
Crowd2Fund is a regulated business and therefore is required to have what is called a wind down plan. The operational function and loan book would be handed over to a third party who would manage your investment repayments. Additionally, the back-up servicer would have ISA permissions so that your investments would remain ISA eligible. You can find out more at https://www.crowd2fund.com/wind-down-arrangements

What happens when I withdraw or sell IFISA investments during the tax year?
You can easily withdraw or sell funds from your IFISA whenever you like. However, you should be aware that withdrawing funds will remove them from your ISA wrapper, but you can replace these funds within the same tax year without affecting your yearly subscription. If you sell an investment on the Exchange then the funds remain within your IFISA wrapper.

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"With real people behind the raise, we hope they're proud of what they're helping us achieve."

Chris Odling-Smee - Cardiff Marine

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Want to find out more?

Visit

www.crowd2fund.com/ifisa

and register for free