CROWDFUNDING 101

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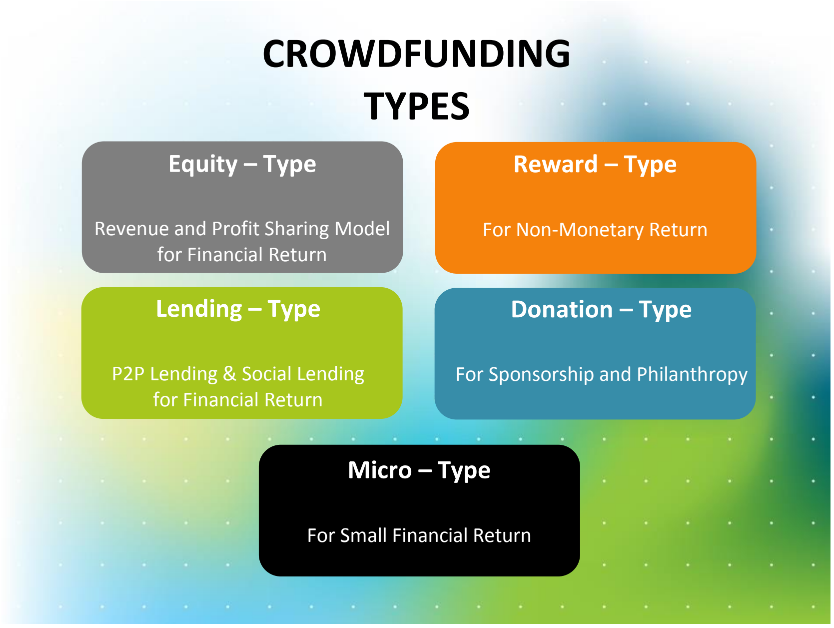
Crowdfunding 101: Types, Applications & Resources

Crowdfunding, the trend of raising money on the Internet, is becoming extremely popular these days. Unfortunately, it is also causing a great deal of confusion, as there are so many different types of crowdfunding occurring, all with dramatically different rules for entrepreneurs to follow.

Types of Crowdfunding



In **donation-based crowdfunding**, the crowd gives money or some other resource because they want to support the cause. One example is a youth baseball team raising money to travel to a tournament. The crowd gives money and gets nothing in return, other than the good feeling that comes with knowing the team can travel to compete.

In **reward-based/royalty crowdfunding**, individuals forming the crowd give money to a business in exchange for a “reward,” typically the product or service that the company produces or provides. Reward-based crowdfunding has been made popular by crowdfunding sites such as Kickstarter and Indiegogo.

With **equity-based crowdfunding**, members of the crowd become part-owners of the company that is raising funds. In other words, the company sells some or all of its shares to the members of the crowd. As equity owners of the company, the crowd realizes a return on its investment and receives a share of the profits in the form of a dividend or distribution. This is a result of the Jumpstart Our Business (JOBS) Act and is on hold while the SEC creates the rules and framework.

Debt crowdfunding, also known as **peer-to-peer lending**, is where the company raising money does not sell shares but instead borrows money from the crowd. The individuals lending the money receive the company's legally binding commitment to repay the loan at certain time intervals and at a certain interest rate.

Regulation D crowdfunding, is the use of electronic platforms to raise capital for regulation D offerings. These platforms are using the existing regulation D framework to raise capital from investors the companies already have a pre-existing relationship with or investors who have gone through a 30-day cooling period. This is currently legal and used for raising money on the internet for a private equity offering. There are two types of regulation D crowdfunded offerings: ones conducting a 506c offering (generally soliciting capital, legalized by the JOBS Act) and ones conducting a traditional regulation D offering (through the use of an online portal, often referred to as a crowdfunding platform).

Donation and Reward Crowdfunding Models

Donation- and reward-based crowdfunding portals like Kickstarter and Indiegogo generally use one of several different models and fee structures. Note that a donation/reward-based portal does not promote nor facilitate any fundraise that offers equity in exchange for funds.

- **All or Nothing (AoN) –** When the fundraising period is over, money is only collected from the contributors if a pre-determined minimum amount of money has been pledged. If the goal is not met, no money is collected.

- **Keep it All (KiA) –** Whether the project goal is met or not, all of the funds collected (minus commission) are handed over to the entrepreneur. If he or she has insufficient funds to meet the objectives, then it is up to the recipient to refund them to the contributors.

Investment Crowdfunding in the United States

This type of crowdfunding is causing a great deal of confusion. While technically conducting a standard regulation D offering or using the 506c exemption to generally solicit, people who are currently raising funds online for an equity-based offering are often said to be crowdfunding. The main difference is the type of offering and the accreditation status of their investors. Please note that true crowdfunding to unaccredited investors as legalized by the JOBS Act has not gone into effect yet. Companies will not been able to use the law's new crowdfunding provisions until the Securities and Exchange Commission finalizes rules, which could be as soon as this summer. In the meantime, many states are enacting intrastate crowdfunding regulations, which will allow unaccredited investors who reside in the state where the issuers (companies) are domiciled to invest limited amounts into crowdfunded offerings.

Title II—Rule 506c—Generally Soliciting

In September 2013, the SEC implemented rules that overturned the 80-year-old ban on general solicitation (advertising and marketing the fact that you are raising money), as mandated by Title II of the JOBS Act. These new rules allow companies (aka "issuers") to advertise private securities offerings as long as only verified accredited investors are allowed into the offering. Accredited investors are defined as individuals making more than $200,000 annually ($300,000 for married couples) or who have a net worth exceeding $1 million, excluding their primary residence. They would need to file a 506c offering instead of the standard 506d that most private companies use to raise capital. While this does allow people to share the fact they are raising capital with the general public, it also requires stricter investor verification standards, meaning that investors can no longer self-certify. It also means you cannot have up to 35 unaccredited investors in an offering, which you can have if you are conducting a standard regulation D offering (what people do now).

Title III –Allows you to Raise Money from Unaccredited Investors

This provision of the JOBS Act would allow private companies to raise up to $1 million dollars from unaccredited investors all across the nation. To protect unaccredited investors from making high-risk investments there are limits on the amount they can make in a single year, based on income. Specifically, in the case of an investor having annual income and net worth of less than $100,000, the investor would only be permitted to invest $2,000, or five percent, of such investor's annual income or net worth (whichever is greater). Companies can do a Title III raise (up to a million dollars, where all of their unaccredited investors can invest), while also doing a standard regulation D offering (for an unlimited amount, where all of the accredited investors will invest). While these rules are going through the regulatory process at the SEC, there are a number of issues that may make them very expensive, such as initial and on-going audit requirements. Companies also have to go through crowdfunding portals to raise capital. These regulations have not gone into effect as of June 2014.

Intrastate Investment Crowdfunding

With long delays and rules that some say may be unworkable for startups, many states are enabling their citizens to perform "intrastate crowdfunding." Intrastate offerings allows a company to crowdfund (e.g. raise private equity) from residents within the state in which it resides. States are adopting intrastate regulations at a very fast clip, with states like Texas enacting rule changes; we could see dozens of new states adopting rules in 2014 and 2015 if the federal regulations have not caught up. More information can be found courtesy of CrowdCheck, and please note this table is current as of April 2014: http://www.leverage-pr.com/wp-content/uploads/2012/11/Summary-of-Intrastate-Crowdfunding-Exemptions-4.2.2014.pdf

Crowdfunding in Texas

Texas released **proposed** rules in April of 2014, which are being said to go into effect as soon as August. While we are in the comment period, and these rules may change, below are some of the main provisions:

- Unaccredited investors can invest up to $5K/year in a startup.
- Startups raising $1M or less need only have the CEO certify their financial statements rather than provide audited statements.
- Texas crowdfunding portals need only fill out a form and pay a standard filing fee, which basically provides a background check. The portal needs to track investor/issuer comments and all communications must take place on the portal. Portals do not need to sit for exams and must maintain records of transactions for five years.

Debt Crowdfunding – Peer-to-Peer Lending

Debt crowdfunding allows consumers and businesses to borrow money through online portals, generally at a fixed interest rate. Lending Club and Prosper are the two most popular peer-to-peer (p2p) lending platforms in the U.S. and have issued billions of dollars in consumer loans to date. Many borrowers use these loans for bridge funding for their small businesses, and more and more small business-specific platforms are emerging to cater to this specific market, including IOU Central, Dealstruck and Quarterspot. There are also real estate-related ones like AssetAvenue emerging, as well as peer-to-peer platforms such as StreetShares (for military and veterans) only serving certain groups.

Current p2p platforms operate under a different regulatory scheme than investment/equity crowdfunding; most of them only accept accredited investors or are even funded by institutional investors, versus being truly crowdfunded. They are legal in most states depending on banking regulations.

These platforms are most popular with established small businesses seeking anywhere between $1,000 to $100,000 for a short-term loan; interest rates vary between eight and 30 percent on average. P2P loans are more expensive than bank loans but have less stringent requirements for approval.

Regulation D Crowdfunding

Regulation D crowdfunding is the use of electronic platforms (AngelsList, MicroVentures, EquityNet) to raise capital for regulation D offerings. These platforms are using the existing regulation D framework to raise capital from investors the companies already have a pre-existing relationship with or investors who have gone through a 30-day cooling period. Companies that list on these platforms are not doing anything new; they are doing a standard regulation D offering. The difference is they are using electronic platforms and all of the tools that go along with them for the capital-raising process. These platforms are launching at a rapid rate, specializing in industry verticals such as real estate and consumer products, taking companies from all industries. One of the major benefits of these platforms is the ability to accept smaller amounts of investment from large groups of investors, made possible due to the JOBS Act increasing the amount of investors you can have on a capital table, from 500 to 2,000, before going public. Many platforms often manage the investor relations for the people who invest on the backend (lumping them as one entity on the company's capital table) so companies do not have to worry about managing an additional 100 small investors. Since companies are using existing regulations, this is being done now very successfully.

Useful Crowdfunding Resources

Non-profit organizations
Austin Chamber of Commerce Entrepreneurial Resources --
http://www.austinchamber.com/innovation/index.php#7
Crowdfunding Professional Association (CfPA) -- http://cfpa.org
Crowdfund Intermediary Regulatory Advocates (CFIRA) -- http://www.cfira.org
Texas Entrepreneurs Network -- http://texasenetworks.com

Donations/Reward-Based Platforms
Kickstarter.com
Indiegogo.com
Crowdtilt.com
FundAnything.com

Investment/Equity-Based Platforms
AngelList.com
EquityNet.com
CircleUp.com (consumer products only)
Fundable.com
Invested.In
MicroVentures.com (Austin-based)

Popular Debt/P2P Platforms
LendingClub.com (business and personal)
Prosper.com (personal)
AssetAvenue (real estate)
IOUCentral.com (business)
DealStruck.com (business)
QuarterSpot.com (business)
Upstart.com (personal and business)

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Coastal Shows

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On their 2014 agenda, they have upcoming conferences in June, covering crowdfunding investments’ effects on the alternative financial markets in New York, and a banking and lending summit in September, that will dive into the peer-to-peer lending world in San Francisco.

CFGE events bring together the most knowledgeable speakers to provide cutting edge information to their attendees in venues across the globe.

Register

Leverage PR

Leverage PR is a full-service public relations firm delivering strategic planning, media relations and communications strategies to companies within the financial, legal and technology industries. With more than fifty years' collective experience in securities, investor relations, legal, banking and finance within both traditional and alternative financial markets, Leverage PR's team possesses a deep understanding of the opportunities and challenges facing our clients. This understanding gives us the ability to communicate angles and opportunities to the media that others may miss. Our in-depth knowledge of the issues facing the financial and technology spaces has given us the great honor of becoming a go-to source for media. The result is an extensive track record of securing top-tier media coverage across TV, print, radio and online outlets and through social media channels.

CrowdBuilder

CrowdBuilder is an innovative platform that, builds your crowd of high-impact influencers, secures local and national media coverage and primes your network for a crowdfunding campaign or business-expansion phase. With automated media outreach services, in-depth guides to campaign messaging, crowdfunding campaign management and media relations, CrowdBuilder gives you all of the tools you need to look credible and polished in front of your crowd.

CrowdBuilder provides a team of professional writers, strategists, project managers and social media experts with extensive track records of success, ready to review and assist clients with messaging, strategy and tools to achieve campaign goals.