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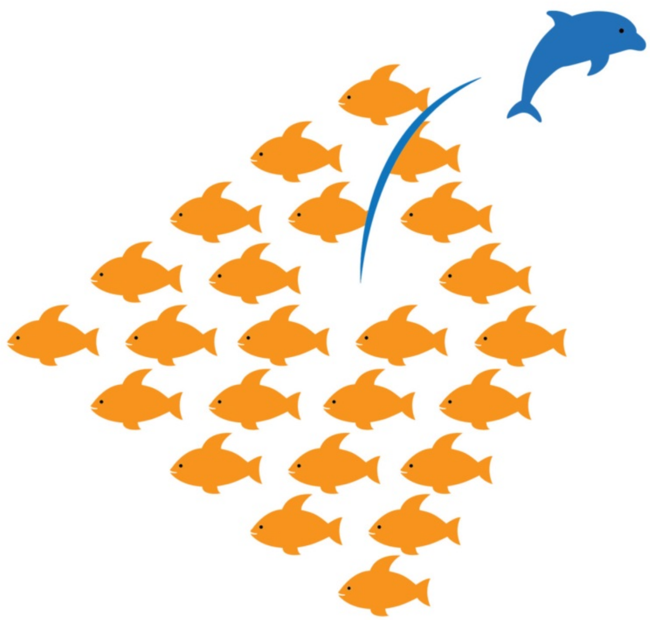

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Crowdfunding (and Crowdfinance) 101

Luan Cox

Here are four things you need to know before you ask for other people's money.

Crowdfunding has paved a new avenue for entrepreneurs to raise capital for their growing businesses and has generated billions of dollars for start-ups. Some do it well (think innovators such as "Generation Why Not: 35 Under 35"). Others, like New York City Opera, struggled with executing a winning campaign. New York City Opera used crowdfunding site Kickstarter to try to raise $1 million the opera needed to stay open through September 2013. It got $301,019 from the twenty-two-day campaign—not even close to its target—and filed for bankruptcy soon thereafter. Although this was not the sole reason the NYCO shut its doors (it needed to raise another $6 million from private investors but only got $2 million), entrepreneurs can learn valuable lessons from the failures of their online campaigns.

First, the NYCO did not clearly define what it was producing with the funds. Kickstarter's guidelines state that the site is not to be used for direct charity or cause funding, therefore a project from a nonprofit organization must have a clear end and focus on what is being created. Second, the campaign began a mere nine days before the 2013-14 season that it was supposed to be funding. Some thought this gave off a sense of desperation and looked like poor planning on the part of the NYCO. Both of these illustrate how lack of understanding and preparation can produce poor results in an online crowdfunding campaign.

How can you do it right? Do you even want to? Before jumping into a crowdfunding campaign, here are four things you need to know.

1. Crowdfunding is not one size fits all—you have four options.

- *Donation-based crowdfunding*. People contribute to a cause or campaign that they believe in with no expectation of returns. This is ideal for philanthropists or those wanting to support their community. Sometimes referred to as civic crowdfunding, this type of crowdfunding works best for charitable causes, community projects and other socially conscious campaigns.
- *Rewards-based crowdfunding*. A reward is given that usually corresponds with the amount contributed. Though rewards-based crowdfunding is not a new concept, it has been thrust into popularity by sites such as Kickstarter and Indiegogo. Popular with musicians, artists, movie producers and start-ups producing consumer goods, contributors are often rewarded with a prototype or some other tangible reward.
- *Debt-based crowdfunding*. This involves the person or entity essentially getting a loan from contributors and paying them back with interest. These types of loans are growing in popularity, particularly with businesses looking to expand but not give up equity in their company.
- *Equity-based crowdfunding*. This is associated with the passage of Obama's 2012 JOBS Act, which eased federal regulations regarding fund-raising and gave individuals the

opportunity to become investors in private companies. With the implementation of Title II on September 23, 2013, private companies can publicly solicit funds from accredited investors. This usually happens online through a portal such as AngelList, EquityNet or EarlyShares. When Title III is implemented, unaccredited investors will be able to invest in these private companies as well. This type of campaign entails the most legal and regulatory complexity, as it involves the sales of securities. Many project that soon this sort of fund-raising will be a vital tool for small businesses and start-ups to raise capital.

2. Crowdfunding has its own rules and regulations that you must follow.

Listing your company on a crowdfunding site may seem simple, but much regulatory compliance is required for each type of crowdfunding campaign, and a lot of legwork is involved in having a successful raise. The work on your crowdfunding campaign actually begins far before you even list your raise on a website. Social media has become a powerful (and free) marketing tool for building momentum and encouraging engagement. Take the time to develop your network; it is a personal investment in what you are trying to achieve.

However, even before you begin building the hype, you need to research the hundreds of portals out there to decide what type of campaign and site are right for you. Take your time, and make sure that you understand the regulatory compliance required for your campaign. Talk to a lawyer if you have questions, especially if you choose to go with an equity crowdfunding campaign, as consulting with a lawyer beforehand will be much less costly than paying one after something has gone awry. There are plenty of tools and resources out there to help you, such as books, blogs and videos, so take advantage of them.

3. You should not crowdfund without a business plan.

Having a proper business plan is important, especially in an equity crowdfunding raise. You want investors to know that you are serious. They want to know your priorities, and that you not only have a great idea or product, but that you have put in the time to figure out how to make it profitable. Having a good business plan can inspire the investor with confidence, trust and belief. The respective intermediary you choose may not have the most stringent requirements for posting a listing, but the more information you provide to potential investors, the better. These investors are savvy, and there are a lot of companies seeking capital; you need to stand out. Clearly explain your business goals and how you plan to achieve them.

4. You need to keep crowdfunding even after you have raised all your funds.

If your campaign is over and you were successful, don't forget that the work is not finished. Do not stop your communications afterward. Keep updating your social media with your progress, and don't lose momentum. Stay focused, and make sure that you keep your investors informed. You will not be able to prepare for everything, but the more roadblocks you are equipped for, the better you can manage any unforeseen bumps.

Following these guidelines will help you avoid many common crowdfunding pitfalls that new businesses face when using this type of fund-raising. Choosing the right crowdfunding strategy for your business will enable you to define your capital-raising needs and the level of involvement that you would like contributors to have. Doing your regulatory homework will prepare you for the road ahead; you will not be surprised by any fees or compliances required of you. Finally, having a clear and succinct business plan will not only provide you with the framework that you need to build your business, but it will also enable you to establish your brand through social media in a genuine and professional manner.

KAY'S TAKEAWAYS:

- Decide if you want a charity, reward, equity or debt crowdfunding campaign.
- Prepare your social media marketing campaign and launch in advance.
- If you choose an equity campaign, have your business plan and documents reviewed by legal advisors and be ready to go the day you launch.