

Issue: Crowdfunding

Crowdfunding

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Will Internet-based financing change how businesses raise capital?

Executive Summary

The explosive growth of social media and the Internet have paved the way for crowdfunding, a means of raising small amounts of money online from a large number of people without any financial intermediaries. Crowdfunding, say proponents, democratizes the fundraising process by helping start-ups, nonprofits, artists and others overcome barriers such as gender and geography to gain access to capital. Besides raising money, crowdfunding provides a way to test the popularity of a product or creative idea and solicit feedback from potential customers. In the United States, the JOBS Act of 2012 legalized investment crowdfunding, which allows for the issuance of debt or equity to both accredited and unaccredited investors. However, the rules implementing crowdfunding for the latter group have yet to be finalized. Some critics worry that ordinary investors will become victims of fraud or will simply make bad investment decisions, but the data remain too sparse to confirm those fears.

Overview



Entrepreneur Ryan Grepper, inventor of the Coolest Cooler, a battery-powered picnic chest with a built-in blender, USB charger and waterproof Bluetooth speakers, raised \$13.3 million via crowdfunding site Kickstarter in 2014. (Courtesy Coolest)

In 2005, three years after her father's death from brain cancer, Mikki Glass sought a way for her sister to include him on her wedding day. She crafted an ankle bracelet with a locket bearing their father's image, so he could, in spirit, accompany her sister down the aisle. A few years later, when Glass got married herself, she drew comfort from wearing that same locket.

Soon, friends were asking her to make them similar jewelry with pictures of their loved ones. That idea eventually grew into the small company With You, which produces a line of lockets, made of precious metals and stones and designed "with a modern vintage look and feel."¹

Glass, a veteran entrepreneur who runs her own branding consultancy, Tilden Marketing, in New York City, had invested a substantial amount of her money to cover start-up costs, but she lacked the cash to actually produce the rings, bracelets, anklets and necklaces. "It is hard to get funding," Glass says. "I went to a bank first, and that's not the easiest road. They were willing to give us a loan, if I moved all my money into their bank, but I didn't." Glass says she also wasn't ready to seek outside investors, which would have required giving up equity.



Mikki Glass, founder of crowdfunding jewelry maker With You, wears one of her company's lockets. (Courtesy Mikki Glass)

Instead, Glass undertook a campaign on Kickstarter, one of the oldest and most popular crowdfunding platforms, with a goal of raising \$40,000 to finance her inventory production. Crowdfunding allows individuals, artists, nonprofits, entrepreneurs and even big brands a way to raise money from a broad spectrum of people, using the Internet, without standard financial intermediaries.²

In less than a decade, Internet-based crowdfunding platforms, such as Kickstarter and Indiegogo, have helped filmmakers, video game producers and artists to finance their creative projects. They've also boosted numerous fledgling entrepreneurs like Glass, who want to raise start-up funds or test market demand, and they've helped the already-famous finance new projects. In some locales, crowdfunding has allowed small investors to take an ownership stake in businesses. U.S. regulators are working on rules that would permit wider use of this type of equity offering, which federal rules now largely limit to wealthier investors. Boosters see crowdfunding as a way to open up access to capital to those who might not be able to get money through more traditional routes, and thus to help the wider economy by creating businesses and jobs. Others, however, worry about the possibilities for fraud and abuse.

For Glass, under Kickstarter's rules, the company would get nothing if she fell short of her fundraising goal; backers wouldn't pay a cent. But if she succeeded, everyone who pledged money would be charged for their contribution and Kickstarter would receive 5 percent of the take. With You would also pay credit card transaction fees.³ Looking back on the process, Glass says the 30-day campaign was time-consuming and stressful. But, ultimately, it paid off: When the campaign ended on Aug. 8, 2014, With You had raised \$42,000 from 248 backers, with the help of a compelling video and various rewards—a selection of different lockets, based

on the level of contribution.

Still in its infancy, crowdfunding campaigns of all types raised almost \$2.7 billion worldwide in 2012, including \$1.6 billion in North America.⁴ The industry has its own trade associations, publications and research organizations. It boasts a growing roster of

professionals, from accountants to lawyers to crowdfunding consultants.

Crowdfund Capital Advisors, a San Francisco-based research and consulting firm that has been a crowdfunding advocate, estimated in a report commissioned by the World Bank that there were at least 672 crowdfunding platforms around the world in 2013.⁵ Sherwood Neiss, a principal in the firm, says that number has almost doubled by now, with the greatest growth in Asia, Latin America and Europe.

Crowdfunding sites fall into four categories:

- Rewards- or perk-based, where businesses solicit money in return for gifts or products, but not ownership interest.
- Donation-based, which are usually for nonprofit organizations or for individual causes.
- Peer-to-peer lenders, where groups of investors lend to individuals or companies for a fixed return.
- Equity, where investors get shares in the crowdfunded company.

Investment crowdfunding, which can be for debt or equity, is legal in many places, including the United Kingdom, France, Italy, the Netherlands and Australia.

Crowdfunding Models Vary by Project, Funding

Crowdfunding models, by project type and average funding sought

Crowdfunding Model	Most Suitable Project Type	Average Funding Sought (\$U.S.)
Donation-based	Arts	Less than \$10,000
Reward/presale	Project/product	Less than \$100,000
Microfinance	Microdevelopment	Less than \$1,000
Social lending	Microdevelopment	Less than \$50,000
Investing/equity	Technology innovation	Less than \$250,000

Source: "Crowdfunding's Potential for the Developing World," World Bank, 2013, p. 34, <http://tinyurl.com/o423cn8>

Some crowdfunding campaigns are better suited to specific projects, such as donation-based crowdfunding for community and arts projects or social lending for small enterprises. Models designed for smaller projects and short-term lending also set lower funding targets than models for entrepreneurial projects or larger business transactions.

Danae Ringelmann, co-founder of Indiegogo, which started in 2008, says rewards-based crowdfunding mitigates three common risks she learned about in entrepreneurship classes at the University of California, Berkeley, where she got her MBA: the risk an entrepreneur won't get sufficient financing; market risk, which means that demand for the product is insufficient; and the risk of poor execution—solving a need but doing it the wrong way or charging the wrong price.

Crowdfunding, at its best, addresses all these issues: "We help you find and grow your business idea before you launch, and we allow you to refine your product before you launch," Ringelmann says.

Even venture capitalists, hoping to discover the next Facebook or Google, are looking carefully at companies that successfully raise money from the public, particularly for new tech hardware.

"It's a really good validation of market demand, in my opinion," says Victoria Song, a principal at Flybridge Capital Partners, a venture capital (VC) firm in New York City and Boston that does early-stage investing. "In these cases, crowdfunding is actually very valuable and takes the risk away. It allows companies to raise money at higher valuations."

Since Kickstarter's founding in 2009, more than 74,000 projects have raised \$1.2 billion via the site, according to the company. The potential for crowdfunding to transform access to capital is even greater in the developing world, said the World Bank study, which

estimates that as many as 344 million households could invest in local businesses and deploy up to \$96 billion a year by 2025, with some \$50 billion coming from China alone.⁶

China Leads Developing World in Crowdfunding Potential

Crowdfunding potential in the developing world, by region, in \$U.S. billions



Note: Estimates are averages of high and low projections for the potential crowdfunding market size in 2025. Analysts' projections are based on estimates of the number of households capable of making crowdfund investments; households' available funds to invest; and the amount of money investors will reallocate from savings and equity holdings.

Source: "Crowdfunding's Potential for the Developing World," The World Bank, 2013, p. 42, <http://tinyurl.com/o423cn8>

While crowdfunding now is concentrated in developed countries, analysts predict China will have the largest crowdfunding market potential of any developing region by 2025 at \$48 billion. The next-largest potential regional markets will be Europe and Central Asia (\$13.8 billion) and Latin America and the Caribbean (\$11 billion).

Rewards-based crowdfunding has fueled the popular imagination: Come up with a good idea, or even a harebrained one, then work furiously to build support on your social networks and you, too, can raise thousands or even millions of dollars. Highly successful campaigns are in the minority—just 40 percent of Kickstarter campaigns succeed.⁷

Even so, the success stories have been widely covered. The space video game "Star Citizen" from Roberts Space Industries had raised \$63 million from fans as of late 2014, mostly from its own website, to fund new features in a game that hasn't even shipped yet.⁸

In 2012, the Pebble E-paper Watch turned to Kickstarter to raise \$100,000 for a customizable smartwatch; instead, 69,000 backers gave \$10.3 million. Equally noteworthy was the campaign for Oculus Rift, where 9,522 people contributed \$2.4 million in September 2012 for the creation of 3-D virtual reality glasses.⁹ That company went on to get millions in venture financing and was acquired by Facebook for \$2 billion, stirring furor among some backers who, in retrospect, would have preferred a slice of the cash to a T-shirt.¹⁰ And in August 2014, Ryan Grepper, the creator of the Coolest Cooler, a battery-powered picnic chest with a built-in blender and waterproof Bluetooth speakers, pulled in \$13.3 million. His Kickstarter page lists 40 media outlets that covered the story.¹¹

Until 2012, all U.S. Internet crowdfunding platforms by law were either reward-based or donation-based. People who contribute to a campaign aren't investors because they're not getting any ownership stake in the company in return for their money. Most rewards-based campaigns promise perks or gifts ranging from T-shirts to products not yet on the market, a practice known as "presale." Some rewards are intangible, such as a shout-out on a film's credits.

While rewards-based crowdfunding platforms continue to proliferate—there are niche crowdfunding sites for cannabis-related businesses and for athletes aspiring to compete in the Olympics—a whole new class of investment-oriented platforms has launched in the past two

years to take advantage of the changing legal landscape. In April 2012, President Obama signed the JOBS (Jumpstart Our Business Startups) Act, which included provisions that for the first time allow companies to go directly to the public to solicit investments through crowdfunding.¹²

“Because of this bill, start-ups and small business will now have access to a big, new pool of potential investors—namely, the American people. For the first time, ordinary Americans will be able to go online and invest in entrepreneurs that they believe in,” Obama said at the signing ceremony.¹³

However, until the Securities and Exchange Commission (SEC) releases final regulations for the law's Title III, which allows “unaccredited investors” to invest in private companies over the Internet, crowdfunding platforms may solicit funds only from “accredited investors” under what's known as Title II of the law. Accredited investors are those individuals with sufficient financial resources to risk investing in unregistered securities—earnings of at least \$200,000 in each of the prior two years for individuals (\$300,000 for a couple) or net worth of more than \$1 million, not counting a primary residence.¹⁴

Academics have begun to study crowdfunding to understand what contributes to entrepreneurial success as well as how crowdfunding might affect the economy. “The research seems to suggest, if you have a slicker pitch, a better video, you're more likely to get support,” says Jason Greenberg, an assistant professor of management at New York University's Stern School of Business.

It's one thing to throw in some money to be the first on your block to get your own cooler, but it might not make sense from an investment perspective to bet on its success as a going enterprise, given that a small number of players already dominate the industry. “This is where the equity-based model is going to be very intriguing,” Greenberg says.

As this financing mechanism matures, here are some of the questions that entrepreneurs, investors, policy makers and researchers are asking:

Is crowdfunding a viable source of capital for start-ups and entrepreneurs?

Proponents say crowdfunding could democratize fundraising by providing access to capital for start-ups and creative projects. That is particularly true for those who can't attract investments from angel investors—the term for the very earliest investors in companies—or venture capitalists, often because of an entrepreneur's gender, ethnicity, location or industry.

“The beauty of crowdfunding, in general, is that it helps you [gain] access to larger pools of people that are motivated to help people like you,” says Greenberg, who has studied rewards-based crowdfunding. He and his research colleague, Ethan Mollick, assistant professor of management in the Entrepreneurship Group at the University of Pennsylvania's Wharton School, found that female tech entrepreneurs on Kickstarter were 13 percent more successful than men in meeting their goals, and that they were primarily attracting investments from other women, who wanted to support female-led ventures.¹⁵

Minority and female entrepreneurs benefit from crowdfunding because it allows them to “raise capital for their businesses directly from investors in an open marketplace of ideas,” Crowdfund Capital Advisors wrote in a July 2014 report. “While individual lenders may carry their own prejudices or may simply have a lower tolerance for the risk, the ability of crowdfunding to connect millions of potential investors with an entrepreneur's idea ensures that a greater cross section of society will be empowered to decide if the business plan has merit and if there is profit to be made.”¹⁶

Neither venture capitalists nor banks have invested proportionally in women and minorities, according to that report. While women own about 41 percent of U.S. businesses, one study the researchers cited found that just 8 percent of women-owned firms got venture backing. Another study put that figure at 12 percent. “Crowdfunding can provide an alternative method of finding minorities and women, while providing investor protections and enabling risk sharing among a community,” according to the report.¹⁷

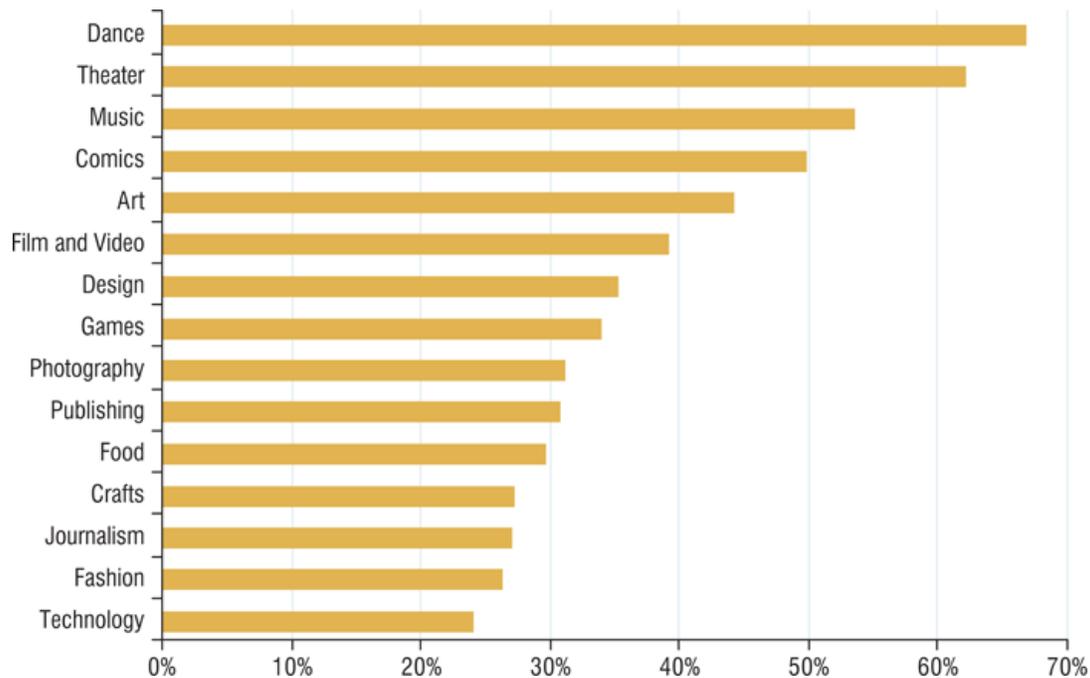
Sutian Dong, a senior associate with FirstMark Capital, a New York-based venture fund that invests in early-stage companies, thinks crowdfunding may have the potential to help entrepreneurs in geographic areas that VCs ignore. “All the larger cities have a start-up culture,” Dong says. “Outside of that, it's very hard to raise financing.”

In addition, she says, some types of business don't make sense for angels or VCs, who generally look for high growth and scalable businesses, mostly in the tech sector, and who want to cash out their investment within seven years. “If you want to crowdfund a neighborhood bar, that might be an excellent way to get community support, but that's not a great investment for an angel, or for a VC,” Dong says. Some entrepreneurs have no desire to give up equity or to eventually sell, she says. Depending on what the entrepreneur wants, crowdfunding could provide a better-fitting alternative. Says Dong: “A question is, do you want part of a watermelon, or a whole grape?”

Despite the hype about crowdfunding and its ability to help businesses gain visibility, develop vital marketing intelligence and raise capital, success is not guaranteed. To do it right, entrepreneurs need to invest in a good video, a strong marketing campaign and professional public relations, says consultant Sandeep Sood, CEO of both Monsoon, an app developer, and the RainFactory in Berkeley, Calif., which helps companies conduct crowdfunding campaigns. He says his clients spend an average of \$200,000 on each fundraising effort.

Performing Arts Most Successful on Kickstarter

Success rates of Kickstarter campaigns, by project type



Kickstarter campaigns created for dance (67 percent), theater (62 percent) and music (54 percent) projects have the highest success rates for meeting funding goals. By contrast, fewer than 30 percent of campaigns created to fund craft, journalism, technology, fashion and technology projects have met their goals.

Preparing for and running a campaign can be expensive and time-consuming. Although entrepreneurs on many rewards-based sites don't have to pay the crowdfunding site a commission if they don't raise enough money, the time they invested can't be recouped. The failure rate on crowdfunding campaigns is high—Kickstarter, which updates the statistics on its website daily, says 40 percent of some 197,000 campaigns have met their fundraising goals since the company's founding in 2009.¹⁸ (With Kickstarter's all-or-nothing funding model, missing a goal means getting nothing.)

Entrepreneurs raising money online pay fees charged by the platforms, which run as high as 8 percent for a partially funded campaign on Indiegogo, plus 2 to 3 percentage points for credit card processing. There are other costs. For instance, money raised on rewards-based crowdfunding sites may be subject to taxation by the Internal Revenue Service and by states, which may levy a sales tax, although rulings are ambiguous.¹⁹

Accounting for the money can be tricky, and people should consult a tax accountant to make sure they get it right, says Neiss of Crowdfund Capital Advisors. Generally, equity investments go into Owners Equity on the balance sheet, while a loan goes under debt. For nonprofit organizations, donations are reported as donation income.

It behooves companies to follow through on their promises whether they have a legal and fiduciary responsibility to investors on debt and equity platforms, or a moral obligation to backers of rewards and donation campaigns. "Your reputation is on the line and will forever be scarred if you don't follow through," Neiss says. Best practices dictate that entrepreneurs are open and forthright with investors on how the funds are being used.

Successful crowdfunding, in theory, should help companies attract follow-on financing because successful crowdfunders demonstrate themselves to be "accountable, reliable and transparent," he adds.

Boris Kogan, the CEO of start-up SwarmBuild, based in Tel Aviv, Israel, and Cedar Rapids, Iowa, is building a digital marketplace where hardware start-ups and designers connect with manufacturers. He sought \$50,000 in October 2014 on Kickstarter, concurrent with efforts to raise a seed round from angels and venture investors. The campaign attracted little interest in its first 31 days, raising just \$2,504, so

the partners canceled their Kickstarter effort and moved to another platform where they perceived their chances would be stronger. The site, called Startup Rounds, allows 100 start-ups at a time to compete for presales and a pool of seed investment funds—significantly fewer than on Kickstarter. “We were competing for eyeballs with a thousand other tech projects on Kickstarter,” Kogan says.

Even if they hit their crowdfunding goals, tech start-ups such as like SwarmBuild seldom raise all the money they need to sustain themselves through the early stages of building a business. “Had we raised a round on Kickstarter, it would not have been enough to get us past a couple of months,” says Kogan, who developed his business at the Iowa Startup Accelerator in Cedar Rapids.

Is equity crowdfunding dangerous for investors?

Because equity crowdfunding for unaccredited investors won't take effect in the United States until the SEC releases the final rules implementing Title III of the JOBS Act—regulations that are long overdue and not expected anytime soon—criticism to date revolves around hypotheticals. No one knows if people will make bad investments or become victims of fraud.

But the possibility that unsophisticated investors of limited means might lose their savings concerns even some fans of crowdfunding, such as NYU's Greenberg. “It's hard enough for professional investors with large and deep networks to do this properly,” Greenberg says. “I do worry that it might become a casino of sorts. It's much more like gambling than investing because it's remarkably difficult to have a good sense of a very new idea succeeding.”

Trying to determine how unaccredited investors might fare, Michael Dorff, a professor at Southwestern Law School in Los Angeles, reviewed studies tracking the performance of investments selected by angel investors. “What we see is that angel investing only makes sense on average because of a relatively few big winners,” says Dorff.

“I just think it's fundamentally a bad idea,” he says of unaccredited equity crowdfunding. “During the years that it will likely take for the middle class to see equity crowdfunding for the alluring trap that it is, investors are going to lose a lot of money. And these are not people who can afford the losses.” In his article, Dorff said the only companies to go through the process of issuing equity on crowdfunding sites to unaccredited investors will be those with poor investment prospects and no other options.²⁰

The U.S. Chamber of Commerce Foundation also raises flags about equity crowdfunding for unaccredited investors, even as it acknowledges its virtues. In a March 2013 blog, Rich Cooper, vice president of research and emerging issues, called crowdfunding a “legitimate and growing phenomenon.”

He wrote, “While VC and other investments will always be a critical element in fostering new business, the explosion of digital capabilities has created a world-wide town hall that gives consumers an opportunity to directly support the products and services they want.”²¹

However, Cooper said, crowdfunding carries risks: “In any new business, there is the potential that the company will fold, given changing consumer demand, business costs, competition and other factors that can depress the potential for success. Investors understand failure looms large in entrepreneurship, and it is a risk they are willing to take. Will the public accept this risk? Do they fully grasp that failure is a natural part of the entrepreneurial process?”

William Cunningham, a crowdfunding consultant, economist and author of “The JOBS Act: Crowdfunding for Small Businesses and Startups,” says that the SEC's proposed caps on investments in crowdfunded ventures won't shield all people from financial ruin. “You'll get somebody who lost the bulk of their savings through some fraudulent campaign the same way people lost their houses to an underwriting guy in subprime lending, but the downside is far lower and the potential for social and financial returns are so high that, in my opinion as an economist, it makes sense to pursue this.”

Proponents also laud crowdfunding as an equalizing force in investing, a way to narrow the gap between the rich and everyone else by letting the masses participate in wealth creation before companies go public and their valuations soar.

“The JOBS Act lets ordinary investors invest easily for the first time,” says Amy Cortese, author of a book about investing in one's local community to stimulate economic development and support area businesses.²² She says crowdfunding is good not only for small companies and start-ups that can't raise money from VCs or get a bank loan, but also for the small, unaccredited investor who was previously shut out of investing in private companies. Crowdfunding rules will allow investors to lend money to companies, which means investors might be able to get a return much sooner through interest payments, Cortese adds.

David J. Paul, chief strategy officer of the real estate equity crowdfunding site [Propellr](#) and co-chair of [Crowdfund Intermediary Regulatory Advocates](#), an advocacy group for equity crowdfunding platforms, has been active in negotiations over rules for Title III of the JOBS Act. He says that for years, regulations barred unaccredited investors from participating in the trillion-dollar market for private equity offerings. Right now, he says, it's an asset class that's available to only about 8 million wealthy families, and just about 1 million of them are participating. “If we get Title III close to right, it'll be available to everybody.”

Paul says that the proposed caps on how much unaccredited investors can sink into any one deal could safeguard against losses. However, he adds: “No one should be putting more than 5 to 20 percent of their assets into alternative investments. At the end of the day, I

think it's the government's job to protect people from fraudsters, but it's not necessarily the government's role to protect people from themselves, from the failure of a business. There's a difference between a company that genuinely tries and doesn't succeed and one that tries to rip you off."

Is crowdfunding good for the economy?

Besides democratizing the fundraising process, the White House and other proponents of crowdfunding say they hope it can foster viable enterprises that spur job creation and economic development in communities.

"The implication and opportunities for crowdfunding are much broader than just the piece of the world that VCs focus on," says Ellie Wheeler, a principal in New York City at Greycroft, a venture capital firm with \$600 million under management.

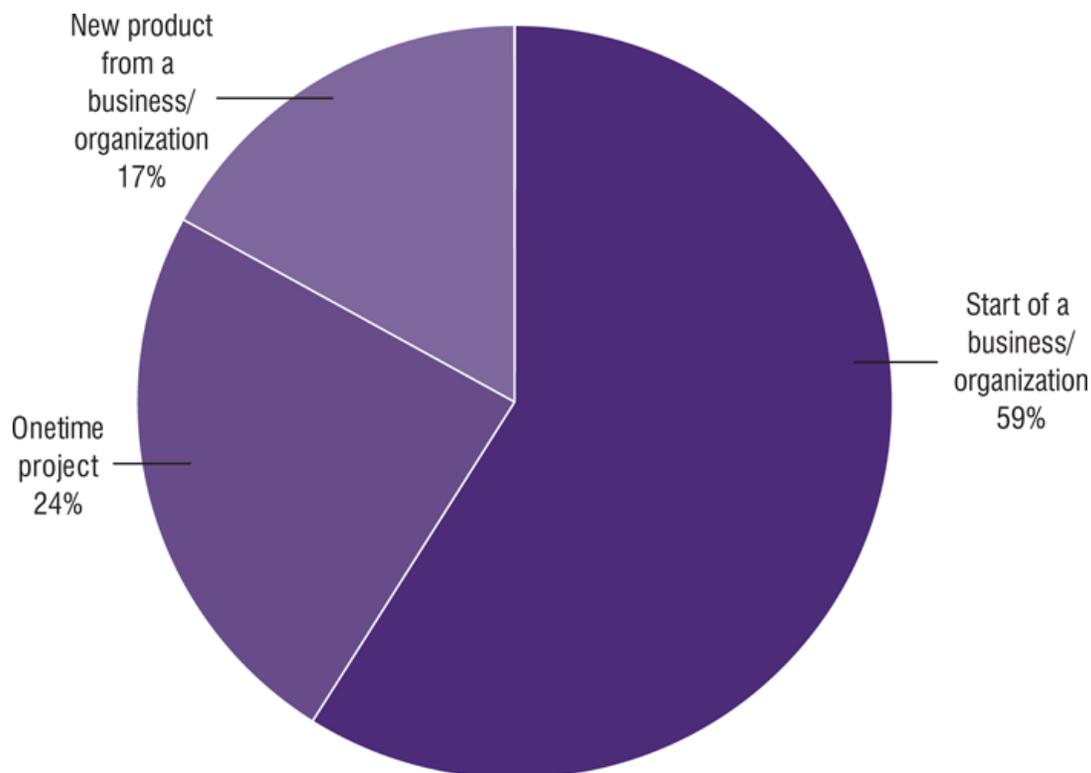
Indications of crowdfunding's potential to transform businesses and to boost the economy come principally from anecdotes about reward-based and donation-based crowdfunding and in limited data from equity crowdfunding outside the United States.

The economic impact of a small business on its community can be powerful. The business can serve as a visible anchor on Main Street as well as a source of employment and tax revenue. Consider Lainie's Way in Port Jefferson, N.Y., a debt-strapped educational toy store that was on the verge of shutting down after suffering extensive damage from Superstorm Sandy in 2012.

Owner Lainie Litovsky took to the crowdfunding platform Tilt in March 2014, appealing to her community to save her store. With help from local media coverage and postings on social media, she raised \$91,135 in donations, just slightly short of her \$94,000 goal but past the "tilt" amount of \$89,000, the bare minimum the store needed to stay open. On March 24 at 11:16 p.m., Litovsky posted a thank-you to the community: "Lainie's Way will be open tomorrow, and for many years to come. Good night." ²³

Survey: Most Kickstarter Creators Aim to Launch Businesses

Kickstarter creators' reasons for seeking crowdfunding



Source: Ethan R. Mollick and Venkat Kuppuswamy, "After the Campaign: Outcomes of Crowdfunding," UNC Kenan-Flagler Research Paper No. 2376997, January 2014, <http://tinyurl.com/q3t9lk8>

Fifty-nine percent of Kickstarter campaign creators using the platform between 2009 and July 2012 launched their campaigns to start new businesses. Twenty-four percent used Kickstarter to fund onetime projects, while 17 percent were business owners seeking funding to develop new products.

Particularly for businesses in places not well served by venture capitalists, crowdfunding can spur economic growth. “The crowdfunding of securities under the Crowdfund Act has the potential to give rural entrepreneurs, farmers and small business owners a new source for venture capital and other business finance. What they choose to do with it, we can only wait and see,” wrote University of Colorado law professor Andrew A. Schwartz.²⁴

Crowdfunding lets people vote with their dollars to support their local economies and causes they believe in, says James Beshara, the CEO and founder of Tilt, which has raised funds for thousands of projects. “As people see the fruits of these platforms, they tend to think more through the lens of what can we do with our money,” Beshara says.

Crowdfund Capital Advisors, which pushed for the JOBS Act, touted the economic benefits of successful crowdfunding in a 2013 study of 73 firms: crowdfunding campaigns by for-profit businesses on both rewards-based and equity based platforms in North America, Asia and Africa.²⁵ The consultancy found:

- Crowdfunded companies overall saw a 24 percent quarter-to-quarter increase in revenue, not including sums raised through crowdfunding.
- For equity-crowdfunded companies, revenue increased 351 percent from quarter-to-quarter.
- 39 percent of companies hired an average of 2.2 employees after crowdfunding.
- 48 percent indicated they planned to use the proceeds of their campaign to hire more staff.
- Every hour invested in a successful crowdfunding campaign returned \$813.
- 71 percent of companies that were successful with crowdfunding either had received or were in conversations to accept follow-on investment.²⁶

Wharton's Mollick has also found that successful rewards-based crowdfunding on Kickstarter can benefit entrepreneurs and, by extension, the economy. In a survey of large design, technology and video game projects that had raised money on Kickstarter, 90 percent were still in business one to four years after their campaign. Moreover, Mollick and his survey co-author said that 32 percent reported revenue of more than \$100,000 a year after their Kickstarter campaign.²⁷

Circle Up, an equity crowdfunding site for accredited investors that specializes in consumer product companies, has been amassing data on the performance of its companies since 2012. Companies that raised money on the platform grew 80 percent on average in the year after their successful campaign, says Rory Eakin, co-founder and chief operating officer.

While crowdfunding can boost a business and its local economy, Southwestern Law's Dorff worries that middle-class investors might divert money from retirement, college savings or debt reduction into a crowdfunded business that is either fraudulent or just fails to deliver as promised.

Mollick found in a 2013 study that 75 percent of successful rewards-based campaigns experienced delays in producing the promised reward for backers, and that the more money received, the later they were likely to be.²⁸

The blog Drop Kicker, which tracks crowdfunding flops and frauds, has devoted a lot of coverage to the Scribble Pen. Prospective funders raised doubts about the veracity of its creators' demo promising that the pen can write in any color by using a scanner that can replicate the hue of any surface. The company halted its campaign on Kickstarter in August 2014, after Kickstarter requested a new video within 24 hours.²⁹ Later, the campaign reopened on Tilt, but problems arose there too.³⁰

Tilt's Beshara wrote in his blog that Tilt had learned about discrepancies in information given to Scribble Pen backers and potentially misleading representations in the demo video; Beshara requested additional information from the campaign organizers and gave them a deadline to provide either a new video of a working prototype or an in-person prototype. “Since these conditions were not satisfied, we decided that the best course of action to protect our community—both contributors and organizers—was to discontinue the campaign and refund 100% of all payments over the next three days.”³¹

On Sept. 6, 2014, Scribble Pen noted on its website that a working prototype was never a condition of fundraising on Tilt. “Scribble is not a figment of our imagination or an attempt to defraud anyone in any way. We have been working tirelessly for the last two years to design and manufacture a product that we believe will change the world, and we are closer than ever to making that a reality.” The company discontinued its crowdfunding efforts and is seeking to raise the money privately, according to the blog.³²

Responding to a request from SAGE Business Researcher for comment, the “Scribble Team” said in an emailed statement in January 2015 that the company had “launched a little too early” on Kickstarter and Tilt. “As you know, we are creating an innovative product, never seen before, and we experienced some technical issues with the advanced color sensor that the pen uses. We shall be launching a finished consumer version of the Scribble Pen this year.”

When it comes to equity crowdfunding, it's still not clear how much the economy might be helped, or hurt, once unaccredited U.S. investors

are allowed to buy shares in private companies. To better understand how small investors make decisions, four academics from Canada and Germany studied offerings on the Australian equity crowdfunding platform ASSOB, in operation since 2006. Their conclusion: “Crowdfunding investors seem to pay a great deal of attention to the financial and governance material that firms provide. However, at this point, the industry is still in its infancy, and thus our data do not enable us to make a meaningful evaluation of firm outcomes yet.”³³

Background

Before the Internet

In 1783, composer Wolfgang Amadeus Mozart needed some cash, fast. His goal: to stage the performance of his three new piano concertos in a Vienna concert hall. Appealing to his bewigged and perfumed fans in a newspaper advertisement, he offered an incentive that wouldn't seem at all strange to modern-day aficionados of Kickstarter. “These three concertos, which can be performed with full orchestra including wind instruments, or only a quattoro, that is with 2 violins, 1 viola and violoncello, will be available at the beginning of April to those who have subscribed for them (beautifully copied, and supervised by the composer himself).”³⁴

Mozart, like many a Kickstarter hopeful, didn't make his number. But a year later, in 1784, he tried again, and 176 patrons contributed enough for him to introduce his concertos in a three-part series known as the Lenten Concerts. He thanked his patrons by publishing a list of their names.³⁵



The pedestal for the Statue of Liberty was financed in 1885 with small donations raised from readers of the *New York World*. (National Park Service)

Perhaps the best-known example of pre-Internet crowdfunding in the United States occurred in 1885, after the American Committee for the Statue of Liberty ran out of funds for the construction of the massive granite pedestal to hold the statue that was France's gift to America. Stepping forward to save the day, newspaper magnate Joseph Pulitzer appealed to everyday people to help. “Let us not wait for the millionaires to give this money,” Pulitzer urged in his newspaper, the *New York World*. “It is not a gift from the millionaires of France to the millionaires of America, but a gift of the whole population of France to the whole people of America.”³⁶

Pulitzer printed in his newspaper the names of everyone who contributed. “One Hundred Thousand Dollars!” the *World* trumpeted on its front page. The final tally was \$102,000, 80 percent of which came in donations smaller than \$1, allowing for the completion of the pedestal.³⁷

Internet Revolution

Crowdfunding, by its nature, requires some way to get the word out efficiently to potential donors or investors. In the pre-digital age, successful efforts shared some common traits, according to author Dave Milliken. “Crowdfunding required the leadership of major influencers—a famous writer, newspaper publisher, a prominent businessman with federal backing—with access to mass media to generate awareness and interest from the general public. Otherwise, the cost of building awareness was generally far too great.”³⁸ The Internet simplified getting the word out to large numbers of people in a community of like-minded individuals, regardless of their physical location. In 1997, the cash-strapped British rock band Marillion became the first to use the Internet to crowdfund, according to then-band member Mark Kelly. By appealing to fans via email, the band raised \$60,000 to finance its U.S. tour.³⁹

Crowdfunding took off after the global financial crisis in 2008. Entrepreneurs and artists alike were looking for alternative funding as bank loans and other traditional sources of capital dried up.⁴⁰

Indiegogo, founded that year and now one of the world's leading crowdfunding sites, explains its genesis on its website: “Danae Ringelmann was an MBA student trying to open an Off-Broadway play. Eric Schell searched for funds for a Chicago theater company in his spare time. Slava Rubin started a charity event for myeloma cancer research after losing his father to the disease. Their struggles to find funding revealed a fundamental flaw in the system: For centuries, access to funds has been controlled by a select few. Danae, Eric, and Slava started Indiegogo in order to revolutionize the flow of funding, so it can reach and grow the ideas that matter.”⁴¹

A year later, Kickstarter debuted, and other players have since piled into the reward-based crowdfunding sector, including RocketHub in 2010 and Crowdfunder (now called just Tilt) in 2012. Donation-based crowdfunding, including sites such as GoFundMe, are a close cousin of rewards or perk-based models, helping people and nonprofit organizations raise money for personal needs and causes by reaching out through their social networks.



Danae Ringelmann, one of the founders of crowdfunding site Indiegogo, says that crowdfunding reduces many of the risks of entrepreneurship that she studied in business classes. (Bloomberg/Getty Images)

Investor Protections

After the stock market crash of 1929, the federal government moved to protect investors with the Securities Act of 1933 and the Securities Exchange Act of 1934.⁴² All securities sold to investors had to be registered with the newly created SEC, unless they fell into certain exempt categories, such as private offerings under Regulation D, which exempts small companies from SEC regulation for selling securities in a private placement. They must file an electronic form that includes the names and addresses of the company's promoters, executive officers and directors and some details about the offering.⁴³

Those securities rules, which among other things prohibited issuers from "general solicitation" and advertising of their offering, continued, without major changes, for decades. It took another disaster, the 2008 financial crisis, to open debate on new ways to encourage business innovation and job formation.

Entrepreneurs Sherwood Neiss, Jason W. Best and Zak Cassady-Dorian, now principals in Crowdfund Capital Advisors, helped form the Startup Exemption, a group that helped develop the framework for the crowdfunding portion of the JOBS Act.⁴⁴ Neiss recalls: "The capital markets had seized up for people who create businesses, who innovate and create the majority of jobs. Our frustration led us to go to Washington."

Crowdfunding was just one of the measures of the JOBS Act, whose provisions aimed to help companies raise capital more easily by easing regulation. The act, signed into law by President Obama on April 5, 2012, drew support from the National Venture Capital Association, the Small Business and Entrepreneurship Council, the U.S. Chamber of Commerce and the International Franchise Association.⁴⁵

Arguing that crowdfunding would endanger investors were groups such as AARP, which represents senior citizens, and the North American Securities Administrators Association, which represents state securities regulators.⁴⁶ The SEC also worried that equity crowdfunding might lead to more lackluster companies—what some refer to as "zombie companies." As a result of such objections, Congress revised the bill, including requiring a crowdfunding company to provide audited financials when raising more than \$500,000.⁴⁷

The JOBS Act enabled companies to publicly solicit and advertise private placements. The regulations for Title II took effect on Sept. 23, 2013, allowing companies to crowdfund from accredited investors.⁴⁸

However, Title III, which legalizes equity crowdfunding for unaccredited investors, still hasn't taken effect. Congress mandated that the SEC issue these rules by the end of 2012, but the agency didn't issue its proposed regulations, which weighed in at 585 pages, until September 2013. To date, a final version has not been issued.⁴⁹

The proposed rules would let small companies raise up to \$1 million over the Internet from ordinary investors. These firms would no longer have to comply with certain reporting requirements that public companies must follow, such as disclosing executive compensation. Individual investors wouldn't be allowed to invest more than \$2,000, or 5 percent of their net income, if their net worth is less than \$100,000. Wealthier investors could spend 10 percent of their net income up to a "maximum aggregate amount sold of \$100,000."⁵⁰

"This could revolutionize everything because people who could not get access to capital will be able to do so on terms that are reasonable," says Cunningham, managing partner of the consultancy National Crowdfunding Services in Washington.

Industry Growth

Since the release of Title II rules, numerous Internet portals have gone into operation to serve businesses seeking debt or equity from accredited investors. Niche sites specializing in real estate are among the fastest growing, according to Crowdfund Capital Advisors' Neiss. He says that may be because a tangible asset such as a building gives investors a sense of security.

Commercial real estate developers have long raised money from groups of private investors, either through limited partnerships or real estate investment trusts (REITs). Real estate crowdfunding lets lots of people invest smaller amounts of money, but unlike REITs, investors can choose a specific building or project. Many real estate crowdfunding sites structure the investments as debt notes or preferred stock.

Fundrise, a real estate crowdfunding platform based in Washington, D.C., was founded in August 2012 by brothers Daniel and Benjamin Miller, who work in their family's commercial real estate business. They aimed to spur economic development that reflected the desires of a local community—the potential equity investors, Daniel Miller says. "A lot of the real estate companies we work with now are existing developers with a real track record. We're now convincing them to go online to raise capital."

Neiss says that it's hard for many real estate projects to get bank loans and even when they do qualify, it can take months. Crowdfunding can deliver the funds in a matter of weeks.

In Fundrise's deals, the platform puts up the full amount of money each developer is seeking and then sells notes to investors.

Chad Gessin, a partner in Chatham Development in Manhasset, N.Y., decided to test crowdfunding by seeking \$1 million on Fundrise in 2014 to build a house on Long Island. (Another \$1 million came as cash provided by partners and family. No banks were involved, and Gessin says they didn't really need the money from Fundrise.) "We're a relatively small shop, and we were looking for a way to open up our development projects, large and small, to more investors, not just through crowdfunding but also through private offerings to accredited investors," he says.

Fundrise gave Chatham the \$1 million upfront, then sold 10.5 percent preferred shares to investors. The investors will get their return on their investment before the developers, Gessin says. "It's a very safe deal for Fundrise, because \$1 million is what we paid for the land." He says he liked that his company had to vet only one investor, Fundrise, instead of many.

Experts caution that such investing is by nature speculative and risky and investors must be willing to tie up their funds long-term.⁵¹ Five financial consultants, interviewed by The Washington Post, don't recommend Fundrise to their clients because of concerns regarding risk, high fees and inadequate liquidity.⁵²

Success in rewards-based crowdfunding has also led to follow-on investing by venture capital firms. CB Insights, which tracks venture capital, looked at 443 technology hardware companies that successfully raised more than \$100,000 on Kickstarter or Indiegogo. The August 2014 report found that 9.5 percent of those companies raised venture capital funds, totaling \$321 million.⁵³

A case in point: After Oculus Rift's successful fundraising efforts on Kickstarter for its virtual reality headsets, venture capitalists came calling. The start-up secured two rounds of venture funding, \$16 million and \$75 million, respectively, on the strength of its crowdfunding success. Then in early 2014, Facebook acquired the firm. The Kickstarter backers didn't profit from the sale because they weren't shareholders; some complained about the deal and their inability to benefit. (Equity investing is still not legal for unaccredited investors, so the issue remains hypothetical.)



A woman tries on an Oculus Rift virtual reality headset. The company, a crowdfunding success, was later purchased by Facebook, upsetting some who chipped into its Kickstarter campaign but did not profit from the sale. (Roc Canals Arbolli/Getty Images)

A disgruntled backer who identified himself on Kickstarter as Carlos Schulte grouched: "I think I would have rather bought a few shares of Oculus rather than my now worthless \$300 obsolete VR [virtual reality] headset. What's two billion dollars amongst 9,522 friends? I'd be happy with my \$300 back."⁵⁴ Greg Belote, the co-founder of equity crowdfunding site Wefunder, said that if Schulte's \$300 donation had been an equity investment, he would have received about \$43,500, or 145 times his investment.⁵⁵

Still, some observers point out that even if equity crowdfunding had been a legal option, Oculus might not have chosen to sell equity so early, before it had a viable product.

David Marlett, executive director of the Dallas-based National Crowdfunding Association, says that the early backers of Oculus Rift got what they had signed on for, but adds the company could have behaved more sensitively. "The right thing would've been to take the \$2 billion and give everybody their \$300 back. What great PR that would've been."

Starting an Internet crowdfunding portal has become an attractive business venture in itself. Angel investors and venture capitalists have poured almost \$1 billion into the industry since 2006, with activity intensifying in 2013, a "breakout year for crowdfunding," according to Neiss at Crowdfund Capital Advisors. Investments almost doubled, to more than \$140 million, in the first three quarters of 2014, compared with the previous year, when investors put \$71 million into seven major deals, mostly lending and rewards-based platforms.⁵⁶

Most crowdfunding platforms are still privately held. However, Lending Club, a peer-to-peer-investing platform that lets individuals lend to other individuals profiled on the site, raised \$870 million in an initial public offering (IPO) in December 2014.⁵⁷ Peer-to-peer lending involves issuing SEC-regulated securities, and is legal for investors in as many as 30 states to date. Unlike equity crowdfunding, it's not considered a private placement and is not covered by Title III of the JOBS Act, according to securities law firm Pepper Hamilton.⁵⁸

It's also not clear when, or if, some of the biggest players in crowdfunding will go public. Speaking to interviewer Charlie Rose, Yancey Strickler, CEO of Kickstarter, said the co-founders have no intention of either selling or going public.⁵⁹ Indiegogo, which closed a \$40 million round of funding in early 2014—the largest amount raised at one time by any single crowdfunding platform—maintains that it chose investors who take a long-term approach to building the business and aren't looking for a quick exit.⁶⁰

Crowdfunding Goes Mainstream

As more of the famous and the well-heeled have turned to crowdfunding, some critics have complained that it is losing its populist spirit. An outcry ensued after director Spike Lee raised \$1.4 million on Kickstarter in 2013 to make “The Newest Hottest Spike Lee Joint.”⁶¹ A similar pushback accompanied the successful raising of \$5.7 million for Rob Lee’s “Veronica Mars” movie and the \$3.1 million backers contributed for the Zach Braff movie project “Wish I Was Here.”⁶²

Kickstarter’s co-founders defended such celebrity campaigns, maintaining that high-profile figures help increase the pie for everyone. “Spike Lee brought three decades of fans to Kickstarter when he launched his project. He introduced many of them to this new way of funding creative works, and to the thousands of other projects that are funding on Kickstarter. Of Lee’s backers, 47% had never backed a Kickstarter project before,” they wrote in a 2013 blog post. “In the past 90 days alone, more than \$21 million has been pledged to filmmakers on Kickstarter *not* named Rob Thomas, Zach Braff, or Spike Lee. Even without counting these projects, it’s been the biggest three months for film ever on Kickstarter!”⁶³

It’s not just entrepreneurs and publicity-conscious celebrities trying crowdfunding. Major brands are also embracing the concept, not because they can’t access capital, but because they want to market and promote new products, gauge consumer interest and foster a culture of innovation within the corporate environment. For example, in Japan, Sony Corp. is using crowdfunding to build employees’ managerial and entrepreneurial skills with the development of new products. “Launching a business from scratch and seeing it through is a very valuable lesson to have regardless of whether you’re becoming a Sony manager or going to other companies,” according to Hiroki Totoki, who heads Sony’s in-house entrepreneurship program.⁶⁴ Sony crowdfunded FES, a fashionable smartwatch with an e-ink display screen, without originally revealing its involvement.

Taking a different approach, consumer products giant Procter & Gamble in 2013 formed a partnership with the equity crowdfunding site CircleUp, which specializes in consumer products. P&G mentors some entrepreneurs vetted by the site and helps them bring ideas to market. The affiliation with CircleUp is also intended to help P&G keep abreast of consumer trends.⁶⁵

Current Situation

Regulatory Challenges

The U.S. investment crowdfunding industry is in a holding pattern, as it awaits the SEC’s final regulations for Title III of the JOBS Act. Since the act’s passage in 2012, the commission’s leadership has changed and it’s now up to the current chair, Mary Jo White, who took over in April 2013, to act. She told the Senate Appropriations Committee that completing the regulations and studies mandated by the JOBS Act is among her top priorities.⁶⁶

“No one knows when, or potentially if, the SEC is going to issue the equity crowdfunding regulations,” says Marlett at the National Crowdfunding Association, which formed in 2012 to negotiate with the SEC. “It’s such a political hot potato. If Obama puts it out there, and there is some fraud, he will get the blame, and there are not enough people with enough financial power pushing him to take that risk,” he says.

Paul, co-chair of Crowdfund Intermediary Regulatory Advocates, told a House subcommittee in January 2014 that if the commission implements its regulations as proposed, the crowdfunding industry for unaccredited investors won’t reach its potential. He said that the disclosure requirements for entrepreneurs raising \$500,000 to \$1 million are “actually more onerous and exhaustive than the current requirements for Regulation D offerings which does not mandate audited financial statements for issuers, nor ongoing annual audited disclosures.”⁶⁷

Ringelmann, co-founder of Indiegogo, doesn’t want to see any more delays, either.

“I hope the regulators will be able to put a first pass out there and be ready to reassess and iterate, just like an entrepreneur would, based on what they learn from the marketplace. I don’t know what needs to happen to make that happen,” she says.

Ringelmann adds, “From what we’ve learned with a perks-based business, there is a need and desire for people to want to shape the world around them, whether it’s to open a local restaurant or help a food truck get started, or get a school up and running or help a product launch.”

Until Title III regulations are released, crowdfunding portals are focusing on either serving the accredited investor community or continuing to offer rewards and donations-based models. Some new platforms that were poised to offer equity crowdfunding to unaccredited investors ran out of money and have disappeared, Marlett says. Impatient for the SEC to act, more than a dozen states, plus the District of Columbia, have legalized equity crowdfunding for unaccredited investors, using an SEC intrastate exemption. The catch: Businesses can raise funds from unaccredited investors only within that state’s borders. Other states are drafting regulations or have bills wending through legislatures.⁶⁸ In Texas, where crowdfunding became legal in October 2014, lawyer Lee Polson, a partner at Strasburger & Price in Austin, is helping an investment crowdfunding portal launch. “We have been working through some of the operational issues and how to make this work in Texas,” Polson says. “Texas is large enough, where somebody can raise some serious money operating these portals.”

Industry Growth

Even as regulatory inaction stalls the growth of U.S. interstate equity crowdfunding, rewards-based and donation-based campaigns grow in popularity.

“You can't put this cat back in the bag,” says Marlett, who is a senior research fellow in Arts & Emerging Media at the University of Texas, Dallas, and is leading the school's efforts to promote campus-based crowdfunding for professors' and students' projects. “Crowdfunding is a wonderful tool for vetting a project and developing a following.”

Marlett, a filmmaker and script writer who incorporates crowdfunding into class assignments, often tells his aspiring filmmaker students that they should be grateful equity crowdfunding for unaccredited investors is not yet legal. Once that happens, he says, it may become next to impossible for projects such as indie films to get funding without offering backers a piece of the action.

Legal Actions

In May 2014, Washington state Attorney General Bob Ferguson filed the nation's first consumer protection suit involving crowdfunding against Edward J. Polchlepek III, known as Ed Nash, and his company Altius Management. The suit, which is still pending, alleges that Nash's 2012 Kickstarter campaign failed to deliver the promised decks of Asylum playing cards with a retro-horror theme to backers by December 2012. Under Kickstarter's rules, companies that don't meet their promises to deliver rewards are supposed to refund the backers' money. Asylum raised \$25,146 from 810 backers in a campaign that closed on Oct. 31, 2012. The company hadn't communicated with these people since July 2013, the suit alleges.⁶⁹

“Consumers need to be aware that crowdfunding is not without risk,” Ferguson said in a statement. “This lawsuit sends a clear message to people seeking the public's money: Washington state will not tolerate crowdfunding theft.”⁷⁰

Assistant Attorney General Jake Bernstein, who is handling the case on behalf of those Washington state residents who contributed to the Altius campaign, says his office brought the lawsuit to draw attention to the issue. “We tried to settle and didn't get anywhere. We're essentially working toward a court resolution, and we've had trouble serving him. He decided to hide and has been hiding effectively for a while.”

Altius could not be reached for comment.

Meanwhile, backers, who contributed anywhere from \$9 to \$93, are outraged. “This project is dead and our money is long gone, we were all suckers and too many times now!” says a backer identified as Jericho in a Nov. 9, 2014, posting on the Kickstarter page.⁷¹

Looking Ahead

Becoming the Default

In a few years, crowdfunding as a term may become obsolete as the practice goes mainstream, some industry observers say.

Ringelmann, the Indiegogo co-founder, says crowdfunding “will become as common as buying” and that instead of crowdfunding, people will just be funding. Beshara, the CEO of Tilt, likens crowdfunding to blogging tools such as WordPress, which used to be considered novel but now are just the way people publish content on the Web. “The reason crowdfunding will seem archaic and dated is that it is just going to become the default of how people come together and make something happen,” he says.

“I think 10 years from now a billion people will be crowdfunding around the world and from their phones,” says Beshara, whose site recently released a mobile app. Most likely, he says, the majority of these global fundraising efforts won't be big, ambitious hardware projects but instead small “bite-sized” campaigns, such as raising money for a block party.

Beshara also sees a strong future for rewards-based crowdfunding for both small start-ups and major brands, based on Tilt's experience in selling an open-source crowdfunding tool to big brands to run major crowdfunding campaigns.

“I think we are going to see some massive crowdfunding campaigns, but it won't be dependent upon amateurs and early adopters,” he predicts. “I think it's going to be Mountain Dew crowdfunding a new drink, Nike a new shoe and Lululemon a new apparel line.”

Beshara says that as people grow more comfortable committing to buy items that haven't been produced yet, businesses will test demand before they spend a dime on production. “That is going to allow for what I call ‘perfect demand,’” he says.

Beshara says he has no plans to expand Tilt's domain to include equity crowdfunding, once the SEC releases its rules for unaccredited investors. Increasingly, backers on crowdfunding platforms—such as the fans of the much anticipated video game “Star Citizen,” who have

given more than \$60 million to the company to build out new features—are showing their willingness to pay for cutting-edge products that they won't see for months. “If you can sell directly to these customers and build a community and not give away any equity, why would you look at an old-world alternative?” Beshara asks.

Proponents of equity crowdfunding see the future a bit differently. If and when equity crowdfunding becomes legal for ordinary investors, Paul of Crowdfund Intermediary Regulatory Advocates says he thinks the market could be worth “hundreds of millions of dollars” within five years—still small compared with the trillion-dollar accredited investor private-equities market.

Neiss at Crowdfund Capital Advisors says he expects the industry to grow in a slow and “rational” way. He expects asset-backed businesses such as real estate will keep growing, and that debt-based crowdfunding will experience the greatest growth. Women and minorities will benefit in particular from the growth of equity crowdfunding, he says, with new specialized platforms arising to serve them.

As an industry, crowdfunding will generate new businesses and job-creation, predicts Dong at venture capital firm FirstMark Capital. “You'll have services, platforms and tools that crop up around crowdfunding, and someone has to provide them.”

Chronology

1700s–1800s	Poets, musicians and others appeal to patrons for money.
1713	British poet Alexander Pope asks patrons to finance his six-volume English translation of Homer's “Iliad.”
1784	Mozart raises money from patrons to finance a concert to introduce his three new piano concertos.
1885	New York World publisher Joseph Pulitzer raises \$102,000 from thousands of readers, in donations mostly under \$1, to complete construction of the pedestal for the Statue of Liberty.
1930s	Stock market crash of 1929 prompts securities regulation.
1933	Securities Act provides for the registration of securities to protect investors and exempts small offerings from certain reporting requirements.
1934	Securities Exchange Act establishes the Securities and Exchange Commission (SEC) to regulate the securities industry.
1950s–1980s	Invention of computers and the Internet pave the way for crowdfunding.
1958	President Dwight Eisenhower creates ARPA , the Advanced Research Projects Agency, to develop technologies that eventually lead to the Internet.
1962	J.C.R. Licklider of MIT envisions a “Galactic Network” of globally interconnected computers.
1969	ARPANET, the precursor of the Internet, is founded to connect four university sites in California and Utah.
1972	First email travels over the network.
1977	Apple introduces its first personal computer.
1981	IBM unveils its first PC.
1986	The National Science Foundation connects regional networks to a backbone network, the NSFNET, or Internet.
1989	AOL users hear “Welcome, you've got mail!” for the first time.
1990	HTML protocol allows users to send text along with graphics to create hypertext pages.
1990s–2000s	Internet Age crowdfunding appears.
1997	English rock band Marillion raises \$60,000 on the Internet from its fans to finance its U.S. tour.
2003	ArtistShare starts platform to help artists raise money online.
2004	Kiva.org , a crowdfunding and microfinance platform, makes small loans to business owners around the world.
2011–Present	Crowdfunding grows in popularity.

- 2011** Georgia allows companies to issue stock for up to \$1 million without registration and to accept up to \$10,000 from an unaccredited investor.
- 2012** [President Obama signs](#) Jumpstart Our Business Startups (JOBS) Act, allowing companies to go directly to the public to solicit investments through crowdfunding. ... [Pebble blows past its](#) \$100,000 goal and raises a record \$10.3 million on Kickstarter. ... Oculus Rift raises \$2.4 million for its virtual reality headset from 9,522 backers on Kickstarter, on a goal of \$250,000. ... Philadelphia becomes the first city to crowdfund on Citizinvestor; it fails to raise \$12,875 for [Tree Philly](#) to plant 15,000 trees.
- 2013** SEC issues draft proposals regulating equity crowdfunding for unaccredited investors. ... Oculus Rift raises \$75 million from venture capital firms. ... Michigan passes intrastate crowdfunding legislation, called Michigan Invests Locally Exemption (MILE) law.
- 2014** Facebook acquires Oculus Rift for \$2 billion, with some backers of the crowdfunding campaign complaining that they didn't get any of the money. ... U.K. equity crowdfunder Seedrs acquires U.S. broker dealer/investment adviser Junction so it can move into American market. ... Washington state Attorney General's Office sues the creator of the Asylum Playing Cards crowdfunding project on Kickstarter, for failing to deliver on its promises to deliver retro-horror themed playing cards. ... Social media site Reddit launches beta version of [Redditmade](#), a new crowdfunding platform. ... Intrastate crowdfunding rule takes effect in Texas.
- 2015** In January, Tennessee and Oregon allow intrastate crowdfunding. ... Kentucky Legislature discusses proposed crowdfunding legislation.

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Kirsner, Scott, "A tale of two crowdfunding ventures," The Boston Globe, Sept. 21, 2014, <http://tinyurl.com/n9k6525>. Two Boston-area crowdfunding campaigns demonstrate how some, but not all, entrepreneurs have been able to raise money online.

Robb, Alicia, "Why Crowdfunding Closes the Gender Gap," Inc., December 2014-January 2015, <http://tinyurl.com/p6cskzp>. More female entrepreneurs are seeking backing through crowdfunding platforms, which have a relatively high proportion of female investors compared with venture capital and angel investor communities.

Investors

Fikes, Bradley J., "Science gets help from the crowd," San Diego Union-Tribune, Nov. 5, 2014, <http://tinyurl.com/mtbvzym>. Some researchers who work for biotechnology laboratories that use crowdfunding platforms to raise money say the experience has improved their engagement skills with traditional investors.

Parmar, Neil, "Crowdfunding is Opening Investment Doors," The Wall Street Journal, Nov. 9, 2014, <http://tinyurl.com/mazb6pa>. More investors are using crowdfunding websites, such as CrowdStreet and CircleUp, to purchase equity in real estate and consumer product opportunities that once were open only to larger investment institutions.

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Marketing

Dave, Paresh, "Gamers' funding fuels meteoric rise of 'Star Citizen,'" Los Angeles Times, Oct. 19, 2014, <http://tinyurl.com/mroancg>. A massive crowdfunding campaign for videogame company Cloud Imperium to develop its "Star Citizen" game has enabled the company to spend its marketing budget on engagement programming, such as live events and video updates, for its backers.

Gumz, Jondi, "Fast start needed to generate buzz in crowdfunding efforts," Santa Cruz (Calif.) Sentinel, Dec. 27, 2014, <http://tinyurl.com/n6eushg>. Founders of Santa Cruz, Calif.-based companies with crowdfunding experience say the success of a campaign is tied to the size of a project's fan base, its social media marketing presence and its engagement with backers.

Schultz, E.J., "Newcastle 'Crowdsources' Local Super Bowl Ad," Advertising Age, Jan. 12, 2015, <http://tinyurl.com/mnp7fhp>. Heineken is funding a Super Bowl advertisement for its Newcastle Brown Ale brand by offering to include other companies' logos in the ad in exchange for contributions.

Successful Campaigns

Bajarin, Tim, "Pebble and Glyph: How Crowdfunding Is Creating Disruptive New Products," Time, Jan. 27, 2014, <http://tinyurl.com/kahqrrh>. Crowdfunding has enabled small companies to develop technologies, such as smartwatches and wearable video displays, that will lead to new consumer product categories, according to the president of a market intelligence firm.

Heber, Alex, "A Campaign To Teach Kids An Hour Of Code Has Just Smashed The Indiegogo Crowdfunding Record," Business Insider (Australia), Nov. 5, 2014, <http://tinyurl.com/lvoh95r>. The "Hour of Code" campaign, launched on the crowdfunding platform Indiegogo in October 2014 to fund computer science education initiatives around the world, raised more than \$2.8 million in about one month.

Tate, Ryan, "How You'll Fund — And Wildly Profit From — The Next Oculus Rift," Wired, April 4, 2014, <http://tinyurl.com/ogxdabx>. Pending U.S. Securities and Exchange Commission rules will allow backers of crowdfunded projects to purchase equity shares in those companies, unlike investors in the Oculus Rift virtual reality headset, who put up \$2.4 million but didn't benefit from the company's sale to Facebook.

Organizations

Council of Better Business Bureaus

3033 Wilson Blvd., Suite 600, Arlington, VA 22201

<http://www.bbb.org/council>

Self-regulatory group that provides information about businesses to consumers, including warnings about scams.

Crowdfund Capital Advisors

1688 West Ave., #802, Miami Beach, FL 33139

www.crowdfundcapitaladvisors.com

For-profit advisory, research and education organization dedicated to promoting access to capital through crowdfunding.

Crowdfund Intermediary Regulatory Advocates

1345 Avenue of the Americas, New York, NY 10105

www.cfira.org

Advocacy and trade group for the equity crowdfunding industry.

Ewing Marion Kauffman Foundation

4801 Rockhill Road, Kansas City, MO 64110

816-932-1000

www.kauffman.org

Nonprofit research and grant-making organization that supports entrepreneurship.

National Crowdfunding Association

213-208-2148

www.nlcfa.org

Trade association of crowdfunding professionals, portals, venture capital firms, angel investors, lawyers, accountants, software vendors, educators and students.

Securities and Exchange Commission

100 F St., N.E., Washington, DC

202-942-8088

www.sec.gov

Federal agency that regulates the U.S. securities industry and is preparing regulations for investment crowdfunding for unaccredited investors.

National Federation of Independent Business

1201 F St., N.W., Suite 200, Washington, DC 20004
202-554-9000

www.nfib.com

National advocacy and lobbying organization for small businesses.

North American Securities Administrators Association

750 First St., N.E., Suite 1140, Washington, DC 20002
202-737-0900

www.nasaa.org

Organization that represents state-level securities regulators.

Small Business Administration

409 3rd St., S.W., Washington, DC 20416
800-827-5722

www.sba.gov

Federal agency that supports entrepreneurship and makes loans; offers online course, "Introduction to Crowdfunding for Entrepreneurs."

U.S. Chamber of Commerce Foundation

615 H St., N.W., Washington, DC 20062
202-463-5500

www.uschamberfoundation.org

Nonprofit affiliate of the Chamber of Commerce, a business lobbying group, disseminates information on the economy and employment issues, including crowdfunding.

About the Author

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