



# Crowd Funding

## The Alternate Funding Option

'Crowd-funding' connects the Crowd (which means the supporters to the projects) directly to those who need Funds. Crowdfunding is the process of raising money to fund what is typically a project or business venture through many donors using an online platform, such as Kickstarter, Indiegogo and Crowd funder. The fundraising window is usually finite -- 90 days, for instance -- and the fees and rules vary across platforms.

**How:** Crowdfunding is typically done through an online platform that allows the fundraiser to set up a public campaign for accepting donations. The campaign will advertise details such as the nature of the project or venture, the amount of money the company is hoping to raise and the campaign's fundraising deadline. People can donate a specified amount through the fundraising campaign's website and often receive some sort of acknowledgement or reward in return for their donation.

**Applications of crowdfunding:** This can range from charitable and educational projects to creative projects -- like funding films -- as well as supporting scalable businesses. Crowdfunding platforms each tend to cater to specific categories, such as Kickstarter which focuses on creative projects or Crowd funder, an equity-based platform which is used for businesses looking to raise investment capital. Crowdfunding is a way of raising finance by asking a large number of people each for a small amount of money. Until recently, financing a business, project or venture involved asking a few people for large sums of money (**Private Equity or Angel Investors**).

Crowdfunding switches this idea around, using the internet to talk to thousands – if not millions – of potential funders. Typically, those seeking funds will set up a profile of their project on a website. They can then use social media, alongside traditional networks of friends, family and work acquaintances, to raise money. There are three different types of crowdfunding: donation, debt and equity.

### A. Donation/Reward crowdfunding

People invest simply because they believe in the cause. Rewards can be offered (often called reward crowdfunding), such as thanks giving & acknowledgements on an album cover, free tickets to an event, regular news updates, free gifts and so on. Returns are considered intangible. Donors have a social or personal motivation for putting their money in and expect nothing back, except perhaps to feel good about helping the project.

### B. Debt crowdfunding

Investors receive their money back with interest. Also called peer-to-peer (p2p) lending, it allows for the lending of money while bypassing traditional banks. Returns are financial, but investors also have the benefit of having contributed to the success of an idea they believe in.

### C. Equity crowdfunding

People invest in an opportunity in exchange for equity shares. Money is exchanged for a shares, or a small stake in the business, project or venture, if the project is successful the value goes up, If not, the value goes down.



## **Technology & Electronic money**

- Developed under PHP/Drupal, the web platform is based on modern and secure technology, according to current web standards.
- All the funds (payments, account management...) are managed by a payment partner, which has the "Payment Service Provider (PSP)" authorization. It acts as a real trusted third party to receive the funds.
- The platform allows a personalized access according to your profile, entrepreneur, administrator, investor etc..
- The platform is customizable: URL, logo, design, contents... the web design is built with you the website that suits you.
- You can also manage a personalized news section (articles, blog, videos...) and your own community of online investors, the details of the project, business development, projections etc....
- The platform allows to manage several languages and currencies.

One could contribute whatever amount, become part of a community, and see the impact of one's contribution over a period of time.

## **Creative crowdfunding helps:**

- Get instant validation for your idea. Reduce the amount of time you spend on ideas that turn out not to be viable.
- Test markets and assess demand for your project.
- Generate buzz around your brand and establish a marketing platform that resonates with the target market.
- Receive instant feedback during the project-building testing stage. Continue improving your project and receiving feedback at each stage of your crowdfunding process. Improve your project before it launches on a larger scale.

## **The Indian Scenario**

SEBI had released a Consultation Paper on Crowdfunding in India. This consultation paper aims to provide a brief overview of the global scenario of crowdfunding including the various prevalent models, the associated benefits and risks, the regulatory approaches in different jurisdictions etc. The paper also covers the extant legal structure governing the fund raising for start ups and SMEs in India. Crowdfunding is solicitation of funds (small amount) from multiple investors through a web based platform or social networking site for a specific project, business venture or social cause. Crowd sourced funding is a means of raising money for a creative project (for instance, music, film, book publication), a benevolent or public-interest cause (for instance, a community based social or co-operative initiative) or a business venture, through small financial contributions from persons who may number in hundreds or thousands. Those contributions are sought through an online crowd-funding platform, while the offer may also be promoted through social media.

## **Benefits of Crowd funding**

- I. Crowdfunding provides a much needed new mode of financing for start-ups and SME sector and increases flows of credit to SMEs and other users in the real economy.
- II. Financial crisis (2008) resulted in failure of number of Banks and, consequently the Basel III Capital adequacy norms have been made applicable to Banks. As a result, Banks have become increasingly constrained in their ability to lend money to the ventures or start-ups which may have high risk element. Hence, there is a need for funding for SME through alternative sources.
- III. SMEs are able to raise funds at lower cost of capital without undergoing through rigorous procedures in this mode.
- IV. Crowdfunding provides new investment avenue and provides a new product for portfolio diversification of Investors.
- V. It increases competition in a space traditionally dominated by a few providers (providing finance to Start-ups and SMEs).
- VI. The operators of a crowdfunding platform may engage in vetting or due diligence of projects to be included on their website, to maintain their reputation



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### Risk in Crowd Funding

Crowd is also associated with many risks, The risk of failure is further increased by the fact that the funding is potentially by participants who do not have the skills and experience needed to assess the risk before investing/lending, as compared to the VCF/PE Investors, banks or other financial institutions who provides funds under the traditional business model.

For Example - Bubble and Balm was a fair trade soap company, who were also the first company to raise funding for their start-up through the equity crowd-funding platform Crowd cube, based in the UK, in 2011. It raised £75,000 in return for 15 per cent of the company's equity from 82 investors, who contributed between £10 and £7,500 each. In July 2013 the business closed overnight, leaving no way of contacting the company or a way to recover losses. The investors lost 100% of their investment. There is possibility of genuine websites being used by fraudsters claiming to be promoters of projects or of false websites being established, simply to defraud the investors or to entice individuals to provide credit card details etc. Thus, there is a risk of misuse as well as cyber-security and/or identity theft.

**Conclusion:** Crowd Funding is therefore is a new concept which requires a lot of study & may call for many amendments in the Companies Act 2013, SEBI Regulations & Foreign Exchange Management Act for issue of shares on private placement basis, issue of shares to non-residents who may become members of a company just by making on line payments, what FEMA regulations are applicable?? If there are more than 200 members in a crowd funding, does the company have to comply with Public Issue guidelines?? Does the company become a public company??? Does crowd funding attract the Information Technology Act?? & DATA Protection rules? How do we make the applicant sign application forms??? What Tax implication would a crowd funding have?? all these and many more are thought provoking it would be interesting to see how the government would handle this concept, while it is in nascent stages even across the globe.