

Crowdfunding gears up for a fresh start

November 15 2012, by Kristin Tillotson

Ben Edwards hasn't always depended on the kindness of strangers. Now he wishes he'd started doing it sooner.

His Minneapolis company SmartThings recently raised more than \$1.2 million in just 30 days on the crowdfunding site Kickstarter.com to launch a product line that allows users to monitor their homes by remote control.

"We would never have gotten that far without it," said Edwards, one of seven partners in SmartThings. "They have a built-in, already primed audience, so we could just focus on the message and the product."

Crowdfunding - a way of gathering an online community of financial supporters to rally around a specific project - has captured the public imagination, bringing an "it takes a village" mentality to the funding of individual dreams.

Now that village could become a stampeding horde. As part of a new law to encourage small business, federal regulators are getting ready to allow crowdfunding donors to receive an ownership stake in return for their money.

Websites battling for niches are already sprouting across the Internet. Indiegogo has an international bent. RocketHub funds [science research](#). Mobcaster is for TV projects. Fundable aims at startup businesses.

Last year, nearly \$1.5 billion was raised by 452 crowdfunding sites,

according to the industry website Crowdsourcing.org.

Kickstarter remains the kingpin.

Since its 2009 launch, it has collected more than \$345 million, mostly for artistic endeavors. This year, it will distribute more money than the National Endowment for the Arts.

It works like this: You post a project on the site and seek donations at various levels in exchange for "rewards" that might range from T-shirts to private parties to the first batch off the assembly line. (SmartThings offered free products and more for contributions up to \$10,000.) You have a monetary goal and a deadline, typically 30 days. If you make both, your project is fully funded, and Kickstarter earns 5 percent of the take. If not - which happens 55 percent of the time - nobody's credit card gets charged.

Crowdfunding has caught on by appealing to a basic urge of the human psyche: the feeling of playing a part in producing something new, whether it's an indie movie or a craft beer.

Minneapolis blues pianist Scottie Miller recently raised \$5,000 to help produce his eighth CD.

"At first I didn't want to do it. It looked like we were pleading for help," Miller said. "But then I saw it as a promotional tool. I figured if we made our goal, we'd be getting our CD into the hands of people who would buy it anyway."

The average Kickstarter donation is \$25; the average goal is \$5,000. The site's co-founder, Yancey Strickler, said a key to its success has been participants' ability to think small.

But bigger names are joining in, too. In September, Oscar-winning filmmaker Charlie Kaufman raised \$406,000 on Kickstarter for his next movie, motivated by the prospect of avoiding studio demands.

Crowdfunding is being eyed increasingly by entrepreneurs such as the SmartThings group - one of only 15 Kickstarter projects to reap over \$1 million.

The number of crowdfunding sites and hopeful entrepreneurs is expected to explode when the Securities and Exchange Commission approves a provision of the 2012 JOBS Act, expected as soon as January.

The new law opens up a previously nonexistent avenue for U.S. companies to raise up to \$1 million via crowdfunding from small investors who are now off-limits because of federal rules to protect against fraud.

Soon they won't be donors - they'll be co-owners.

For small businesses in flyover country, where venture-capitalist interest is much scarcer than in Silicon Valley or the East Coast, the concept is especially appealing.

"Crowdfunding helps open up capital for companies located in areas that do not have well-defined startup ecosystems," said Eric Corl, president of Fundable, which was launched last spring.

Fraud has not been a problem in England or Australia, where crowdfunding has been legal for several years, according to Crowdsourcing.org.

Kickstarter doesn't plan to get into the equity business, said co-founder Strickler. But it does accept a few small businesses that fit its ideal of

celebrating creativity, such as the Lynn on Bryant, a small locavore restaurant in south Minneapolis that opened a month ago.

It got more than \$34,000 in pledges on a \$25,000 goal. It also benefited from the buzz of being on Kickstarter, said co-owner Jay Peterson.

"You generate interest and social-media traffic just by being there," he said. "People who live in the neighborhood saw it. People ... saw it on Facebook and contributed, which was heartwarming."

The change in federal law will broaden the pool of potential funders. Still, not everyone thinks it will be a cash cow for every budding entrepreneur - or newbie financier.

"I'm a fan of crowdfunding, but it's not the business for me," said Dana Severson, whose St. Michael, Minn., company Wahooly uses a different type of crowdsourcing, connecting startups with social-media influencers. He warns against a gold-rush mentality.

"There isn't a big enough payday. 'Angel' investors and venture capitalists know that if they put \$1 in 120 companies, they're going to get a payoff of \$250 to \$350. But 95 percent of what they invest in is going to fail. The average person might not realize that when you invest \$100 in a company that's worth \$3 million, the chances of a huge payoff are slim to none."

Rob Weber, co-founder of W3i, a Minnesota company that connects apps to users, has been on both sides, as an entrepreneur and angel investor.

"Sophisticated angels aren't going to do this kind of microinvesting," he said. "But when you look at the success of microloans in developing countries, the sort of small business that doesn't need millions could

benefit."

Ultimately, both men said, crowdfunding isn't about making money.

"It's social karma," Weber said. "People lucky enough to have a little extra money might say: 'Hey, I want to make an impact for someone else.' "

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