MICHIGAN ECONOMIC
DEVELOPMENT CORPORATION

INVESTMENT-BASED CROWDFUNDING FIELD GUIDE

September 2020

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Disclaimer

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INVESTMENT-BASED CROWDFUNDING FIELD GUIDE

The purpose of the "Investment-Based Crowdfunding Field Guide" is to provide community development organizations, including local units of government, downtown development authorities, Main Street programs, and other economic and community development organizations, with information to help support a small business owner interested in pursuing investment-based crowdfunding as a means to access capital to start or grow a business.

Many terms are used interchangeably when referencing investment dollars collected from a "crowd" of people, instead of just a handful of high net worth individuals or from institutions:

- Community capital
- Community investment
- Local investment
- Local financing
- Direct investing
- Peer-to-peer lending
- Investment crowdfunding
- Equity crowdfunding

This field guide provides those on the frontline working with new and expanding small businesses throughout Michigan with the knowledge and resources needed to navigate investment-based crowdfunding as a viable way to access capital for their small business needs. This guide provides an overview of community capital and the opportunities under the federal Jumpstart Our Business Startups Act, or JOBS Act (2012), and the Michigan Invests Locally Exemption (MILE) legislation (2013), that allow small businesses to raise funds directly from the community. In addition, it provides step-by-step action items to assist a small business owner as they research, consider and prepare to raise capital.

WHAT IS COMMUNITY CAPITAL?

Community capital is simply money that comes from the community and goes to the community. This type of democratized capital that yields a return for its investors can be a viable financial resource to start or grow a small business. This guide will use the term investment-based crowdfunding to describe the practice of directing capital from investors to small businesses.

WHY IS THE MEDC PRODUCING A GUIDE ON COMMUNITY CAPITAL?

Many small businesses have difficulty gaining access to capital through traditional financing sources. For women, people of color, those with less than perfect credit, or even startups, it is even harder. Investment-based crowdfunding can be a game-changer for small businesses, who are the cornerstone of what makes Michigan's downtowns unique and authentic. Investment-based crowdfunding provides an innovative financial tool to support the creation, retention and growth of businesses on Main Street.

MEDC is committed to enabling long-term economic opportunities for all Michiganders. In 2019, the organization engaged in the creation of a five-year strategic plan. MEDC evolved its mission, vision, guiding principles and strategic focus areas in pursuit of its commitment to enable long-term, high-wage and equitable economic growth in every region of the state, from rural areas to its urban cores. One strategic focus area includes the continued effort towards developing attractive places. For this reason, MEDC continues to strengthen local communities, downtowns, and historic neighborhoods through technical assistance efforts. The organization recognizes the importance of supporting main street businesses and the role they play in vibrant and sustainable communities. Community capital is one way for main street businesses to access capital and engage the local community.

DONATION-BASED CROWDFUNDING VS. INVESTMENT-BASED CROWDFUNDING

General awareness of websites such as Kickstarter, Go-Fund-Me, and Indigogo are much more commonplace than they were five years ago. These websites serve as examples of what donation-based crowdfunding is. Donation-based crowdfunding raises money through individual donations for a specific project or initiative. A small business could utilize donation-based crowdfunding to raise capital, but the major difference is that the person donating understands there is zero financial return on their contribution.

> **Accredited Investor:**
> Meets the requirements as defined by the U.S. Securities and Exchange Commission (SEC), generally refers to an investor with a net worth over $1 million.
>
> **Non-Accredited Investors**
> An investor with a net worth under $1 million and has an income under $200,000 individually (or $300,000 with a spouse).

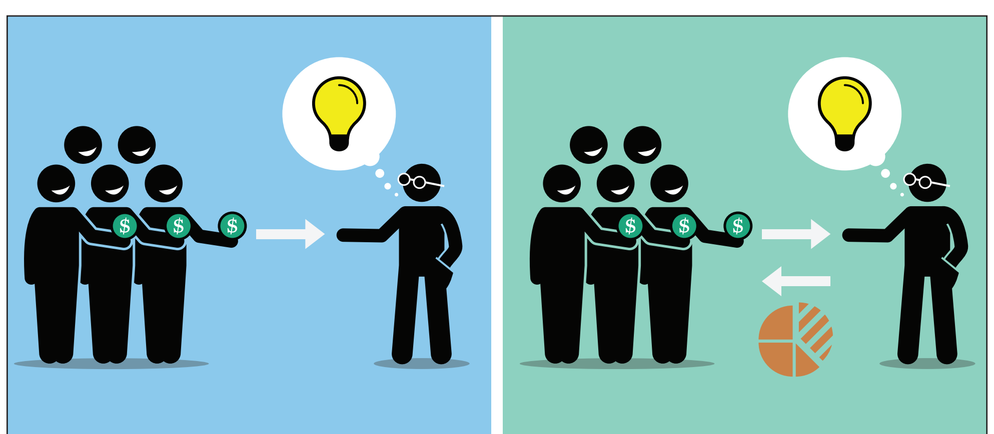
In Michigan, the MEDC's Public Spaces, Community Places program is an example of donation-based crowdfunding. That program has utilized donation-based crowdfunding to support public community projects that need additional capital. In addition to dollars raised from the community, the MEDC provides a grant up to $50,000 as matching funds. Investment-based crowdfunding allows residents, not just accredited investors, to invest in local businesses. The individual investor anticipates receiving a financial return on their investment.

MORE INFORMATION ON THE EVOLUTION OF CROWDFUNDING IN MICHIGAN

In a partnership between the MEDC and the Michigan Municipal League as well as a team of community capital activists across the state, a storytelling booklet, called "Community Investment, Community Growth: A Retrospective in Michigan Crowdfunding," was produced in 2019. MEDC highly recommends reading the guide to learn more about the differences between donation-based and investment-based crowdfunding and read case studies about both kinds from around Michigan.

MECHANISMS THAT ALLOW FOR INVESTMENT-BASED CROWDFUNDING

Jumpstart Our Business Startups Act (JOBS Act 2012): In 2012, President Barack Obama signed into law the Jumpstart Our Business Startups Act,



DONATION-BASED CROWDFUNDING

INVESTMENT-BASED CROWDFUNDING

> **Intrastate Securities Exemption**
> An exemption to certain federal rules when an offering only includes persons within a single state.

or JOBS Act, a bi-partisan bill that made investment-based crowdfunding possible. The JOBS Act set out to change five different laws, one of which, Title III, allowed anyone, regardless of wealth or income status, to invest in a private-owned business. The maximum a company can raise is $1.07 million annually, and the maximum a nonaccredited investor can invest is a formula based on income and net worth. Companies must offer the security through an online platform registered with the Securities and Exchange Commission (SEC).

Michigan Invests Locally Exception (MILE Act 2013): Meanwhile, in Michigan, former Governor Rick Snyder signed the Michigan Invests Locally Exception, or MILE Act, into law in 2013. The MILE Act, which leverages the intrastate securities exemption, allows a company to raise a maximum of $1 million annually, or $2 million if they have audited financials. Nonaccredited investors can invest a maximum of $10,000 per company under this registration. The company must be based in Michigan and solicit the raise only to Michigan investors. An online platform is not required, so a company can register their raise and host events in their community to share information about the offering. However, they do need to verify that everyone they are speaking with is a Michigan resident.

> **U.S. Securities and Exchange Commission (SEC)**
> The federal agency responsible for protecting investors, maintaining fair and efficient markets and facilitating capital formation.

THE VALUE OF INVESTMENT-BASED CROWDFUNDING

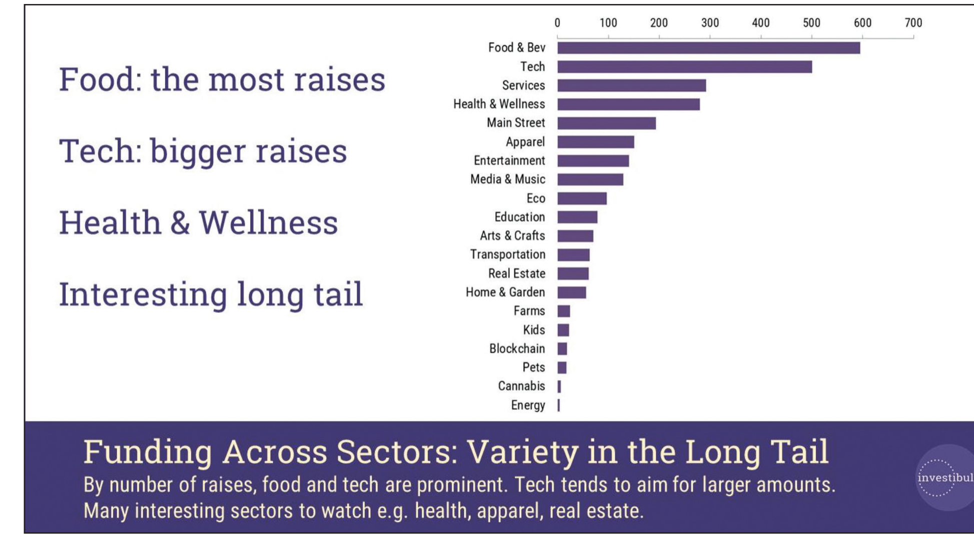
Why might a company be interested in raising capital from its community?
Investor-return crowdfunding serves two primary purposes for businesses:

1. Provides access to capital that may otherwise be difficult for them to acquire
2. Helps strengthen their customer base—turns customers into raving fans and brings in new customers through investing in their company

Companies sometimes pursue investor-return crowdfunding in addition to traditional funding. They see the value proposition of combining growth capital with marketing and sales efforts as a win-win for everyone. When company and customer interests are tied together, it can instigate an increase in the lifetime value of the company's customer base. Revenue-sharing agreements (one form of an investment offering where investors are paid back through a share of the revenues) makes this especially true.

As a community development organization and small business supporter, why would you recommend a company explore this path if it was not already familiar with this strategy?
If you are working with an entrepreneur who has a strong customer base already, this form of capital raising may be a great fit. Here are some other considerations that might lead you to identify this strategy for them:

- They have access to traditional resources but do not want to tap them until they need to do so.
- They are already comfortable with digital platforms and have a secure connection with their community online.
- They are looking for less than $1 million in investment.
- They are a "main street" business and will likely not be a target for angel or venture funds.
- They are a startup, and they/you believe they are likely to be turned down for capital elsewhere.



The other big value…
It is important to recognize that entrepreneurs and the companies they are growing need access to capital and resources, but community members also need more access to wealth-building opportunities.

Your town may have already started discussing investment-based crowdfunding not just as an opportunity for small businesses to raise capital but also for citizens to build wealth. This interest could look like greater integration between community development practices and economic development practices, into what is now often termed "community economic development."

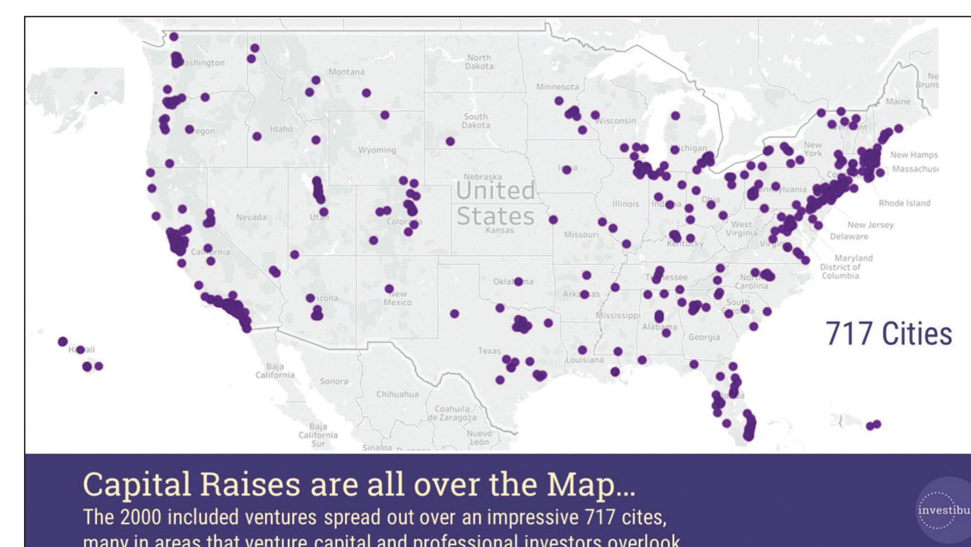
Many local partners are excited about sharing this strategy due to the implications of circulating more capital within communities and the higher social and economic justice goals this addresses.

WHO IS USING INVESTMENT-BASED CROWDFUNDING?

Investment-based crowdfunding tends to work best for businesses that:

- **Have a supportive customer base** or community network, or
- **Are based in a town that has prioritized access to capital** and support for all types of businesses, not just high-growth businesses or the attraction of large businesses from outside the community

Investment-based crowdfunding can work for high-growth, but also slow-growth, no growth, and nonprofit organizations as well. The size or sector of the business is not the determining factor of success—it is the strength of its network or the community support for the method at large. The slide below, produced and compiled by Investibule, shows the number of raises nationally split out by



3 WAYS

your organization can create a culture that leads to successful investment-based crowdfunding in your community

Bring together local stakeholders to build awareness of investment-based crowdfunding opportunities, share stories of raises in Michigan and trends nationally. Many online platforms allow you to search by state. You can also keep an eye on new information coming from the National Coalition of Community Capital.

Leverage other crowdfunding opportunities in your community to utilize the crowd and build familiarity, such as undertaking a Public Spaces Community Places project, hosting a pitch competition or SOUP event, or working with a platform such as KIVA that will provide zero interest small business loans.

Connect with small businesses and entrepreneurs to understand their capital needs, opportunities for growth and pain points in starting up or expanding their businesses. Use the "Step-by-Step Guide to Supporting Businesses Interested in Pursuing Investment-Based Crowdfunding" on page 7 to provide a foundation for investor-return crowdfunding education.

industry sector. As you can see, food and beverage companies, followed by tech, lead the industry breakdown.

Some communities in Michigan have become early adopters of investment-based crowdfunding tools. In Adrian, Michigan, a new company can take a community investment raise public and potentially succeed without a growing customer base or a deep network. The city of Adrian prioritized education and awareness building for this form of capital circulation, creating a friendly environment for aspiring entrepreneurs.

The Adrian community has already supported several successful campaigns, including:

- Three Adrian businesses participated in the MEDC's MI Local Biz donation-based crowdfunding campaign: Encore Dance Studio; Ghidrah's Mind, Body, and Spirit shop; and Advantage Videos raised more than $5,000 each and received a $5,000 MEDC matching grant to support small businesses' Covid-19 recovery efforts.
- The Buzz Café and Marketplace, a new downtown Adrian business, sought community investors to help renovate a historic building and build out its restaurant and candy shop. Thirty-five investors from five states invested $118,000, and after just over two years of deconstruction and renovation, the shop will open in fall 2020.

In most towns, however, this is still a new and unexplored topic. Investment-based crowdfunding remains a relatively unfamiliar tool to downtown management organizations, small businesses and citizens.

Who has used investment-based crowdfunding so far?

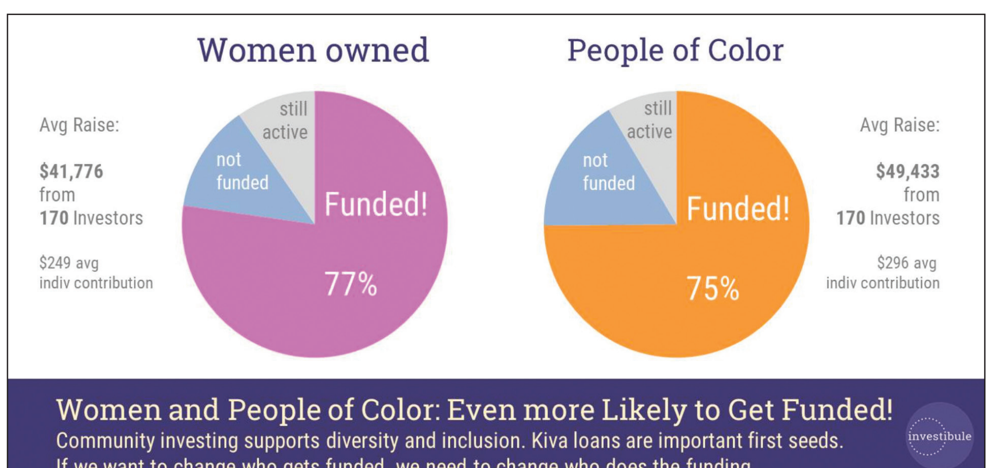
Investibule, the country's only campaign aggregation site, launched when the SEC enacted the JOBS Act rules in 2016. They pull data from all live campaigns across more than 30 crowdfunding platforms.

Since their launch, there have been about 2,000 companies that have raised capital using many different registration mechanisms, not just regulation crowdfunding (commonly called "Reg CF"). Investibule released a report at the National Coalition of Community Capital Conference in June 2019 and now have the report available online.

Regulation Crowdfunding (Reg CF)
Provides an exemption from the registration requirements for securities-based crowdfunding, allowing companies to offer and sell up to $1.07 million of their securities without having to register the offering with the SEC.

One notable finding from the report is that 33 percent of all capital raises were from women-owned companies, and 26 percent of all capital raises were from minority-owned companies. Compare this to 12 percent of venture capital going to women in 2018, which declined 15 percent from 2017.

African American business owners find an even greater uphill battle when trying to access venture funds, with less than 1 percent of venture capital going into their businesses. So far, community investors are proving to be more inclusive in their investment decisions, creating a more welcoming process for those often left on the sidelines.



A STEP-BY-STEP GUIDE TO SUPPORTING BUSINESSES INTERESTED IN PURSUING INVESTMENT-BASED CROWDFUNDING

As a community development organization, you are often the first point of contact to serve small businesses and entrepreneurs who reside in or want to locate to your downtown. Understanding the basics of investment-based crowdfunding is a great way to grow local awareness, build public and private partnerships, increase accessibility to opportunities, and ultimately support business owners on their journey to accessing the needed capital to start or grow their business.

WHERE DO YOU START?

STEP 1: The business needs a solid business plan, backed by realistic financial projects

It may seem overly simplistic to start with the idea that an entrepreneur needs a solid business plan first, but you'd be surprised at how many companies attempt to raise capital from the community only to find investors rejecting their offering or online platforms not approving them to launch at all. Raising capital still hinges on a solid foundation—dollars coming from the crowd doesn't change that requirement.

Small business owners can utilize the Michigan Small Business Development Center or other service providers such as SCORE, in order to develop and refine their business plan. Its crucial for the business to put the effort into this step. It shows potential investors that business owners understand all aspects of their business from management to marketing. It also requires that business owners put pen to paper to address their business model and how investment-based crowdfunding will provide needed capital, how that capital will be used and how investors will be paid back.

Community investors are generally concerned with the following questions, which are slightly different than what a banker or angel investor—those who are accredited and typically invest in high-growth companies—might be looking to answer:

1. How does the business make money?
2. How does the business spend its money?
3. What's the long-term vision for the business?
4. How does the business serve the community's broader interests?
5. How will I get my money back?

Community investors may utilize a due diligence checklist to vet the business' offering. It is a great idea to have the business become familiar with what types of questions a potential investor may ask. Nearly every question you might find on a due diligence checklist can be traced back to one of these five questions.

In many examples of successful raises, having a plan in mind and being able to communicate the broader points by delivering this information through a short video, an executive summary, or a pitch deck versus the traditional 50-page business plan is the aim today. The building of this plan and realistic financials is the most important thing you can do to prepare a business for local investment.

STEP 2: Identify the business's existing sphere of influence

Gathering investment from the community requires access to a community. You want to help the business determine if they could potentially gather 80 percent of their funding goal from within their network. Why 80 percent? Because generally speaking, that's the amount that comes from within an entrepreneur's direct and extended network, with the remaining 20 percent coming from investors who are on the online platform, heard about it from far away, or who are interested in supporting an attribute the entrepreneur hits (sector, LGBTQ, minority- or women-owned, etc.).

For entrepreneurs, the idea of connecting with potential investors may seem overwhelming. Oftentimes, they may not have a wide network of family and friends to lean on to raise capital. Therefore, entrepreneurs may be inclined to skip over this step, and then they launch a campaign only for it to sit and languish for six months. Once an entrepreneur has launched a campaign and it's languished, it makes it harder for them to raise capital in the future.

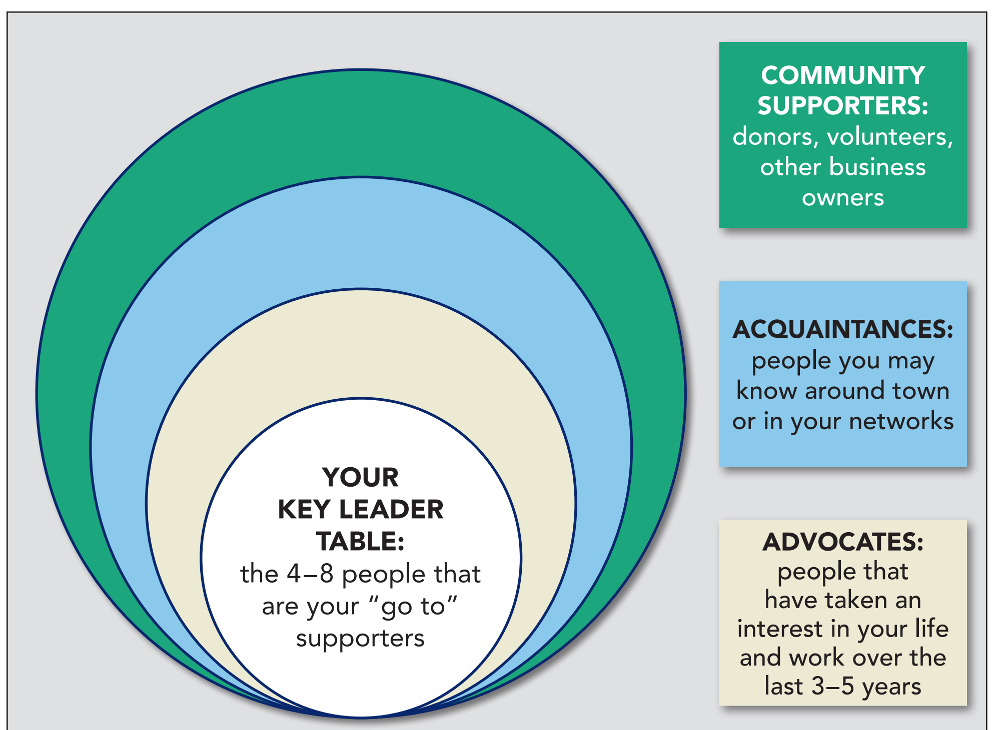
Help your small businesses walk through their spheres of influence using the concentric circles method from Jeff Aronoff, a Detroit, Michigan, attorney who helped entrepreneurs in the early days of the MILE Act:

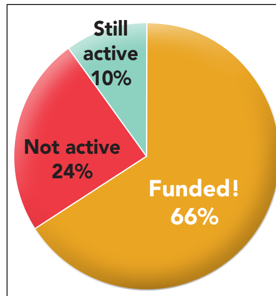
As the small business owner goes through each of these rings, have them make a list of specific people and networks of people that would fit into each ring. You may be wondering how many people the entrepreneur needs to identify? Investibule has some data to help gage how many investors may be needed.

As an average, consider one community investor being worth a potential $1,000. If the business wants to raise $200,000, then they're likely looking for 200 people to invest. If we know that, on average, 80 percent of the investors come from their own immediate or extended network, that is 160 people. If you assume at least half of the people pitched say no, then in this scenario, the entrepreneur needs to identify 320 people.

Indeed, some investors come in for more than the average, and in many cases, that is the goal of this exercise altogether—figure out how to raise the $200,000 with 50 investors instead of 200. There are many case studies about companies that planned to do a community investment raise, only to register the security and hit their fundraising goal without ever having to take the raise public.

If after reviewing these averages with the business owner they are immediately overwhelmed by the thought of finding 320 people to talk to, that is a signal that community investment may not be the best route for them, or they could lower their investment target and consider it part of a diversified capital stack. It is still worth going through this exercise with them. Start with their inner circle, while they dictate the names, you may want to write them down in a spreadsheet for use later in the business's marketing work. Note that at this stage, there is no need to restrict the list to Michigan residents only—you can note in the spreadsheet if the individual or network lives outside of Michigan.





Successful raises

$134,000 (avg)
range: $5K–$12M

131 investors (avg)
range: 1–3,515

And yes, businesses are getting funded. *66% of offerings reach or surpass their minimum target. While ranging widely, typical raises attract 100–200 community investors.*

STEP 3: Understand how to register a capital raise

Once the small business owner has a robust business model with sound financials and a potential investor target list, it is worth directing them to legal counsel.

A business that wants to solicit funds from community investors and is offering a return on that investment must register their offering (or "security") under the JOBS Act (federal) or MILE Act (Michigan). There are many things to keep in mind and pitfalls to avoid prior to using investment-based crowdfunding as a mechanism to access capital. If the business owner violates either the federal or state regulations, there may be serious consequences (See the chart in Appendix B on page 15 for the various types of registrations.) Having general legal counsel on the business's side of the table is the ideal situation.

There are three ways the business can do this:

1. **Pay out of pocket for an initial consult to fact find:** determine what the attorney fees will be from start to finish, what registrations they are most comfortable with given the makeup of the company (its legal status, ownership interests, existing debt), and what types of registrations they would recommend.
2. **Access legal guidance as a client of an incubator or accelerator**: if a business incubator or accelerator serves your community, the business owner may be able to take advantage of technical assistance offered, including legal guidance. It is possible that not all legal networks are familiar with investment-based crowdfunding through the MILE Act or JOBS Act.
3. **Call the platforms:** Online platforms that facilitate investment-based crowdfunding typically make their money through fees on capital raises that hit their target. Some also charge upfront flat fees to evaluate a company and onboard them to their platform. This upfront fee covers the legal costs for putting their term sheets in order and registering their capital raise.

   If the entrepreneur already knows what registration or platform they want to use, then they could go directly to the platform to get the legal work done. The downside to this is that the platform is incentivized to onboard them according to their preferences, not what's necessarily best for the business. If the platform doesn't specialize in Reg A+, for instance, then they're less likely to suggest it even if it may be in the best interest of the business.

Remember, it is important to follow state and/or federal requirements for securities registrations.

1 REGISTER THE SECURITY:
Do not violate securities laws and go renegade with raising capital. It is harmful to the company, to investors, and to the ecosystem when businesses cut corners and try to raise capital without running it through the proper channels.

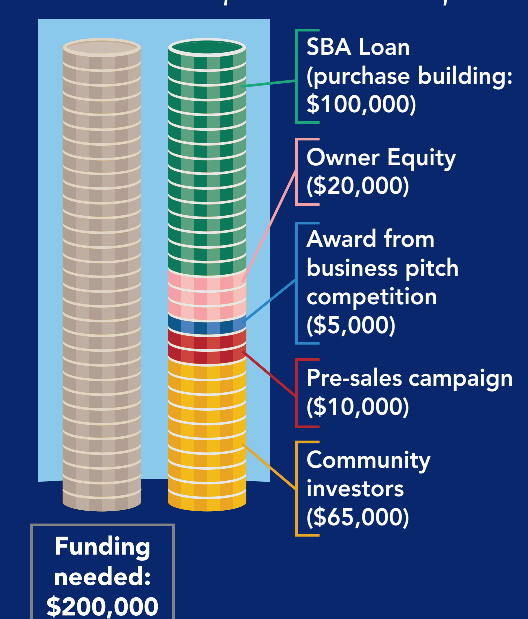
2 DO NOT MAKE GUARANTEES:
As confident as the entrepreneur is about the future, they cannot guarantee that investors will not lose money or that they will receive 10 times their original investment. They must recognize the risks involved and disclose them accordingly.

For further clarification and best practices on how to raise capital in Michigan, visit LARA's MILE page. For further clarification and best practices on how to raise capital using federal registrations, visit the SEC's dedicated web page on the topic.

WHAT IS A CAPITAL STACK?

The small business owner should get comfortable with thinking about the capital they need to start up or grow in a stack. "Stack" is a term often used in the angel investing and venture capital world, and it is becoming even more relevant in the investment-based crowdfunding world also. A stack refers to various types of capital "stacked" upon each other to form the company's total funding needs.

Diversified Capital Stack Example



STEP 4: Decide whether using a platform is the best option

First, what is a platform?

A platform is a website that connects investors with offerings—the amount of money that businesses are trying to raise and what investors are anticipated to receive in return. Businesses, sometimes referred to as the issuer of the offering, will create a profile, input relevant pitch data, and promote their offering. People use many different terms when talking about this aspect of the community investing movement, but for the sake of this field guide, we will use the term "platform." It is essential to know the differences between different versions of what a website can do for an entrepreneur, however.

A platform that does the following is required to register as a broker-dealer:

- Offers investment advice or recommendations
- Finds investors on behalf of the issuer
- Compensates employees, agents, or other persons to solicit the offering or pays them based on a success fee of a successful capital raise (usually a percentage of the raise)
- Holds, manages, possesses, or otherwise handles investor funds or securities
- Engages in any other activities that the SEC determines to be appropriate

The costs of registering and managing a broker-dealer are high, which has pushed many companies to move "upstream" and only work with entrepreneurs who are raising $1 million or more. For this reason, funding portals have found their entry in the marketplace.

Broker-dealer
A brokerage firm that buys and sells securities on its own account as a principal before selling the securities to customers.

If the online platform just lists a company's pitch deck, if it uses a third party to manage the transfer of both cash and stock (including the establishment of escrow accounts for the investors while they wait for the raise to conclude), or if it offers general support services that don't fall into these categories of activities, it can register as a funding portal. These platforms are more likely to accept smaller capital raises. While funding portals do not have to register as broker-dealers, they do still have to register as a portal with the SEC. See this reference book for more information about how to tell the difference between the two.

Regardless of what type of platform a website is, it must abide by the same set of critical requirements, including:

- Conducting background checks on officers, directors, and 20 percent equity holders of each issuer, to reduce the risk of fraud
- Disqualifying an issuer if one of its officers, directors, or "participants" (such as promoters) in the offering is a "bad actor," as defined by the SEC (i.e., a convicted felon; person subject to a finance-related injunction or restraining order; person subject to SEC disciplinary action)
- Being subject to anti-fraud and anti-manipulation provisions of federal securities laws and regulations

If the entrepreneur is unsure if the platform they're thinking of approaching is a broker-dealer by reviewing their "About Us" page, direct them to the Financial Industry Regulatory Authority's (FINRA) BrokerCheck system (incidentally, this is also where consumers can do a background check of any investment professional that they may consider working with.)

How to choose a platform

There are nearly 50 platforms on the market today, making it difficult for entrepreneurs to choose which one is right for them. Fortunately, several organizations have been collecting data on Reg CF campaigns since the rules were issued. Your first resource site to visit is "Crowdfund Capital Advisor's Dashboard on Tableau Public," which covers through the end of 2019. Here are the tabs you will want to review:

- Campaigns/portal: Total campaigns by top 10 portals
- Industry $: Industry appeal by # of campaigns, # of backers, and capital
- Platforms by industry: Industry specialty by portal

The next resource you'll want to check out is the top eight platform comparison article from www.crowdwise.org, which details fee ranges, security types offered, whether a platform is a broker-dealer or not, and whether they perform due diligence or not.

Which platform an entrepreneur chooses to work with depends on several factors:

- Business's industry
- Characteristics of what the business's legal team has charted with them
- How much hand-holding the entrepreneur needs
- How comfortable the entrepreneur feels about the team members they interact with from the company.

Keep in mind that companies planning to use Reg CF are required to use a platform for their raise. If the company is planning to use other registrations, their legal team can inform them of whether a platform is a requirement or only a best practice. The MILE Act does not require a company to use a platform.

For more information about the pros and cons of using a platform, here is a great article that details industry opinions: "Pros and cons of crowdfunding platforms for business owners," *JustCoded*, June 2019.

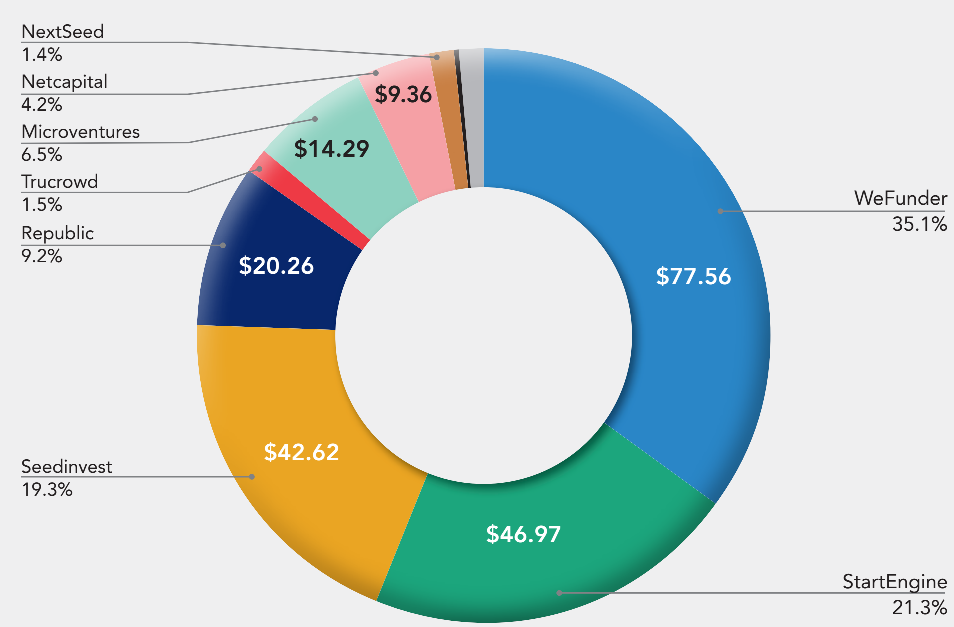
Going old school

Before the days of the Internet and new regulations, businesses might have raised capital only with individual investors (usually angels or friends and family). They would have done it the "old school way," with paper across the table. Today, this takes the shape of investor pitch events, small dinner parties and gatherings, and sending communications out to the company's customer base.

While companies do not have to give up a success fee to a platform when doing it this way, they may not be prepared to take on additional responsibilities, such as:

- Investor relations: gathering interest, converting those to commitments, gathering investment funds into escrow accounts, and managing ongoing questions and answers with the investor base
- Marketing: sending out communications to potential investors, perhaps creating a website or page on their existing site for the offering
- Legal: paying the full legal bill for the registration of the securities, finalization of the investor package, and guidance on the investor relations and marketing responsibilities
- Reporting: this includes the reports required per the registration type(s) chosen by the company, as well as tax statements to the investors if required

Volume of Reg CF capital raised: Inception to date (Aug. 2019)
$ in millions USD



The challenge of keeping track of all these things has created a market niche for platforms to use technology and legal templates as a leverage point in the service of entrepreneurs. Some companies, however, still feel confident about their ability to do it without the help of a platform. When the investor pool is less than 20–30 people, going "old school" could potentially be a wise move.

STEP 5: Chart out the marketing plan and campaign timeline

Just like in a donation-based crowdfunding campaign or a nonprofit capital campaign like Public Spaces Community Places, an investment capital raise follows similar best practices.

With an investment raise, there are three significant considerations that entrepreneurs must keep in mind as they set out their plan:

1. Know what can and cannot be said publicly. An attorney (and the platform the entrepreneur is working with) can guide them.
2. Divide the marketing plan into three tranches: pre-launch, launch, and post-launch. There is a set of critical activities in each of these periods.
3. Plan to make a great video. Most people make decisions about people based on the first 10 seconds of interaction with them. In many cases, the campaign video is their introduction, so entrepreneurs need to be wise about how they present themselves and the story they tell.

Set expectations on the timeline

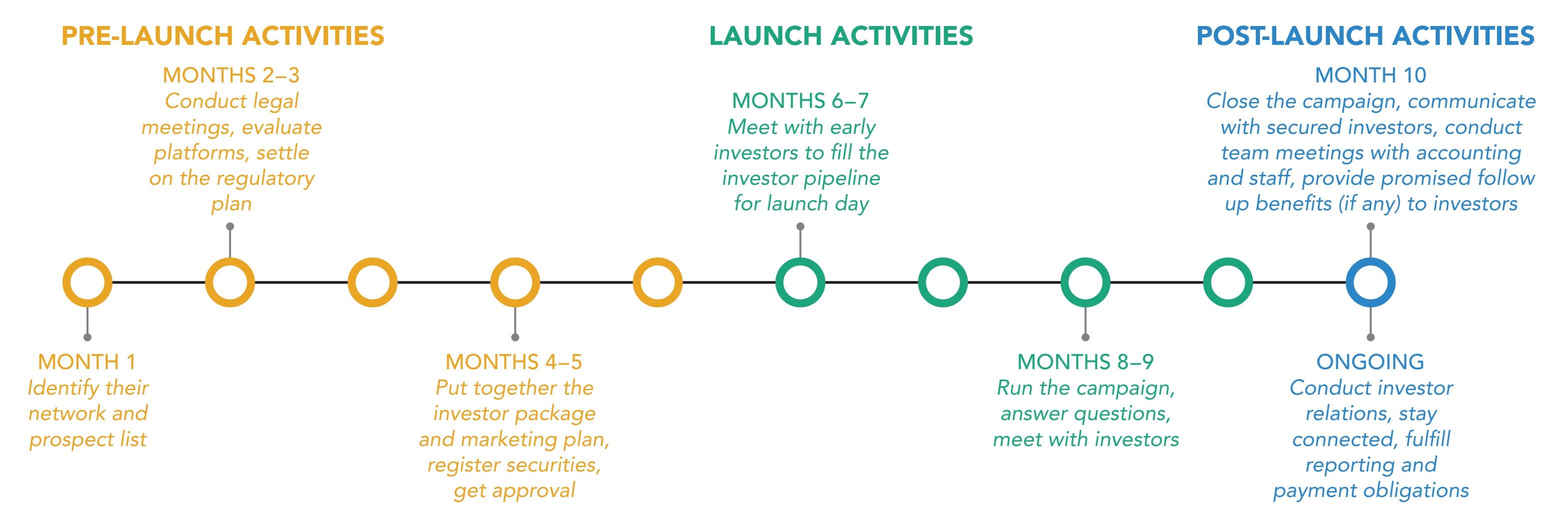
The average successful campaign runs for about 45 days. Some get their investment commitments in 30 days, some in 90 days. Most registrations allow businesses up to 12 months or the end of the calendar year to raise their funds. However, investors often view campaigns that have been live for more than three months as "dying on the vine," which can turn them away. While average campaigns have a relatively short lifespan, the work involved in the campaign is much longer. A lack of understanding has led more than a few entrepreneurs to have unrealistic expectations of when capital will hit their company's financial statements. This misunderstanding can set them up for an eventual cash crunch during or right after the raise. As the saying goes, the best time to look for capital is when you have capital (not after you run out).

As in nonprofit capital campaigns, the entrepreneur needs to "fill the pipeline," so there is traction on day one of the raise launch. This involves gathering interest, and soft commitments from investors (once they are legally able to do so) before the campaign goes live to the public. The business is asking investors to log in to the site on day one to indicate their commitment. Nonprofits often gather 80 percent of their raise goal quietly before announcing the raise so there is a good chance of getting the rest of the way there once it is public.

Most businesses do not go that far, but they often stack 20–40 percent of the raise into their pipeline before going live to the public. How long this process takes is what ultimately dictates the timeline. Here is an example of a timeline that a business could experience, assuming they have already completed Step 1 (solid plan, realistic financials):

In this ideal scenario, you can see that the capital raise—while only live to the

Sample Business Campaign Timeline



public for 60 days—can be a 10-month endeavor, plus add on the ongoing investor relations and payback work. Most business owners who have attempted to raise angel or venture funds are aware of how time-intensive and long the fundraising process can be, however, most Main Street entrepreneurs have never experienced a capital raise before, so they are more likely to be blindsided by the amount of effort involved.

Engage the network

Now is the time to pull out that investor prospect list from Step 2 and have the business begin activating their network. Here are a few ideas business owners can use to begin communicating the capital raise, using solicitation guidelines provided by legal counsel and the platform:

- Create a series of social media posts on the platforms where the target investor spends their time (for most businesses, the target investor is also their target customer). Plan to intensify the campaign in the last week of the campaign, which is the second most highly trafficked time during the campaign (the first week being the peak traffic period).
- Get marketing help. Some entrepreneurs retain a marketing agency to help with the creation of the pitch video and other investor materials, but it is not required. Any marketing firm with a quality track record can create a compelling video.
- Write a press release and circulate it to local media outlets. Have a media kit ready to go with highlights suitable for the press about the campaign, a picture of the business owners, a couple of pictures of the business, and a bio on the owners.
- Apply to pitch your capital raise at pitch clubs, investor clubs, demo days, or entrepreneur meetups with pitch components, in the area (send in applications three to six months prior to the campaign live date so the entrepreneur is scheduled to pitch during the live campaign).
- Organize a series of investor pitch gatherings, which the entrepreneur uses to engage the inner rings of their network.
    - » It is best to host these gatherings at their business location or collaborate with a strategic partner (could be a supplier or vendor).
    - » Oftentimes businesses host just one investor pitch gathering and do not see success. Plan three to six opportunities in case potential investors cannot make the first couple of dates.
- Have the investor package ready to go, either on a platform or in a Dropbox or Google Drive folder, so the link is easy to access. Many email servers or cybersecurity protocols flag emails with attachments, especially large ones—it is best to have the package hosted in the cloud and send that secure link to potential investors.
- To prepare for investor engagement, the entrepreneur should think through the most common objections or challenges to the business model, deal terms and other materials provided to investors. Write the questions out and have answers prepared for each of them.

STEP 6: Create a post-launch plan

A common issue that technical assistance providers across Michigan have highlighted is that businesses launch their campaigns without a post-launch plan.

Businesses encounter a host of problems in the post-launch days of their campaigns. To avoid these pain points, organizations can help entrepreneurs create a post-launch plan before launching their campaign. Here are the components of a post-launch plan that need attention:

- Establish the business's technical team to help troubleshoot issues as they arise—include business consulting, legal, accounting, tax, strategic advising, marketing and sales.
- If the terms the investors agreed to will no longer work for the company because the prospects have changed after the raise or pivots were required that change the financial projections, have a proactive communications plan with investors to ask for a renegotiation. Legal counsel can guide the negotiations, so the company is staying within the boundaries of the regulations.
- Identify who on the team is responsible for creating the investor reports and handling questions from the investor pool going forward.
- Companies inevitably need more capital as they grow. Identify 10–20 investors from the initial investor pool that may have the capacity for additional growth capital in the future. Cultivate these relationships.
- Determine how involved investors will be. This may mean investors have a silent role in running the business or utilize investor expertise to provide guidance on business operations.

Understanding the community investor climate

What makes individuals want to invest as part of an investment-based crowdfunding raise? There are generally three factors that influence an individual's decision to invest in a business: the investors' values; personal priorities; and expectation of a return.

Values: People who turn their attention to their own backyard for inclusion in their investment portfolio have a common set of values that drive their interest.

Figuring out how a business's mission and vision align with those investor sentiments is the key to compelling them to give attention to the capital raise. Here are some anecdotal responses as to why people choose to invest locally:

- They are interested in businesses that hire locally, spend revenue with local vendors and suppliers and are committed to staying local as they grow.
- They are especially interested in the impact story. Many community investors are motivated by what is now commonly called the social enterprise movement—where a business desires to maximize its benefit to a specific social or environmental objective. The most common areas of impact are:
    - » *Whom the company hires:* disenfranchised populations, returning citizens (formerly incarcerated), veterans, people with disabilities, people who experience homelessness
    - » *Who the company's owners are:* people who have a harder time accessing capital (women, people of color, LGBTQ, those who were formerly incarcerated, people climbing out of intergenerational poverty)
    - » *What the company makes or does:* products or services that solve a problem in the world, or that make the world a genuinely better place; interest is exceptionally high in the following categories:
        - Clean energy: community-owned power, solar installations, woody biomass production
        - Food systems: farmers, makers, organically grown staple crops
        - Health: cannabis, mental health service providers, direct care medical practices, yoga studios, devices that improve safety
        - Environment: reuse products, non-motorized transportation supports
        - Real estate: workforce housing, mixed-income developments, mixed-use developments that have a commitment to energy efficiency or staying affordable for new Main Street businesses
        - Democratization of power and wealth: co-ops, democratically controlled organizations, or those spurring the creation of other similarly minded entrepreneurs

Priorities: Even if an investor's priorities align with the mission and vision of the business, set out to engage them in their capital raise. There are still a number of other factors that investors need to consider before they are willing and able to say yes or no.

The most pressing of those concerns, such as the investors tolerance for risk, can be heard in a four-part short educational series on YouTube specifically for investors, which can be very insightful for businesses looking to court them. These videos are accessible through the MEDC's website here.

Expectations: Individuals that have been investing in businesses in the last five years have come to expect deal terms and return projections based on offerings they have seen in the past. They may be open to considering something that is outside of these parameters, but this is at least what their starting point might be. Note that this list of attributes may not resonate with angel investors.

Furthermore, people in the community who have never invested locally or who have never invested at all may have expectations that are wildly different. These investor differences make it critical for entrepreneurs to know what type of person they are talking with from the onset, so they can help identify whether there may be a mismatch of expectations.

Here are some examples of the kinds of offerings community investors typically consider:

- Five percent monthly revenue share agreements with 1.5 times payback in a maximum of eight years
- Equity investment with an exit of 1.4 times after five years
- Preferred equity with a base dividend of 5 percent, and a vesting schedule of 60 percent, 80 percent, and 100 percent after three, four, and five years, respectively
- Promissory note of three years with 3 percent annual interest, five years with 5 percent interest, or 10 years with 7 percent interest
- Equity investment with no stated exit (usually a small investment, or an investment in their own business)

SUMMARY

Each of the topic areas covered in this "Investment-Based Crowdfunding Field Guide" could easily comprise an entire book. However, this guide is meant to provide community organizations with an overview of investment-based crowdfunding so that you can assist businesses looking for guidance and information.

As the community capital movement gains traction, each of us has a role to play—which carries with it a certain level of responsibility. Community development organizations should share this field guide with their colleagues, inform business owners in their community, and add value to the larger conversation and ecosystem around the state by sharing their expertise, asking thoughtful questions and telling the stories of success and lessons learned.

APPENDIX A: Resource Sites and Citations

Regulation resources

Michigan registered portals
LARA's handout on registration options in Michigan
LARA webinars on raising capital in Michigan
FINRA registered portals

Offering resources

Cutting Edge Capital DPO (direct public offering) field guide
KISS (keep it simple security) template legal documents
SAFE (simple agreement for future equity) template legal documents
Series Seed template legal documents
Explanation of SAFT (simple agreements for future tokens)

Platform information

List of platforms and what registrations they specialize in
JustCoded article: Pros and cons of crowdfunding platforms for business owners
Crowdwise article: Top 8 platform comparison

Sector data

Reg CF deals to date
2017 vs. 2018 Reg CF raise amounts
Reg CF turns 3: What's working, what's not
Investibule: CommunityCapital2000 report
World Bank $93 billion direct investing market estimate report
Crowditz weekly Reg CF activity reports

Community resources

Washington State University local investing field guide (published Sept 2019)
MSU storytelling video on Revalue/Angela Barbash
MML Michigan Crowdfunding Retrospective storytelling report
MML local capital resource site
Michigan Community Resources: Legal guides

Investor resources

TD Ameritrade: DPO vs. IPO
Financial Poise: Articles for investors
Grubstake: Resources for Michigan local investors
FINRA's BrokerCheck system

Other topics for entrepreneurs

Locavesting: How to raise local capital, national news aggregation site
Cutting Edge Capital typical DPO investor guide
SCORE Business plan templates
Entrepreneur Magazine article: What to include in a pitch video
Microventures article: General information about solicitation rules

APPENDIX B: Chart of Registration Types

	P2P Lending	MILE Act	Reg CF	Reg D	Reg A+
Best suited for	Microenterprises, early stage, community-based businesses	Early stage through growth, Michigan-based customer base	Seed through Series A, MVP is out, early customer feedback, passionate fans	Seed through Series A, substantial revenues, top-line, or user growth	Mature companies on a steeper growth curve with a broad active audience
Common names	Microlending	Michigan Crowdfunding, Intrastate Securities Exemption	JOBS Act, Title III, True Crowdfunding	504, 506(b), 506(c)	Mini-IPO, Tier 1, Tier 2
Annual raise limit	Limited by platforms	$1 million (no audit) $2 million (audit)	$1.07 million	$5 million (504) No limit (506)	$20 million (Tier 1) $50 million (Tier 2
Accredited, Nonaccredited, Both	Both	Both	Both	(b) Accredited + 35 Nonaccredited; (c) Accredited only	Both
Investor limits	None	$10,000 Nonaccredited No limit for Accreditation Michigan investors only	Income/NW is below $100K Investment limit is the greater of $2,000 or 5% of annual income/net worth. If the investor's income/NW is above $100K, 10% of income/NW up to $100K.	None	Tier 1: None Tier 2: 10% of the greater of the person's, alone or together with a spouse, annual income or net worth (excluding the value of the person's primary residence and any loans secured by the residence (up to the value of the residence)
Audit required	No	For the higher raise limit	Yes	No	No (Tier 1) Yes (Tier 2)
Filing entity	None	LARA	SEC	SEC	SEC, with LARA review for Tier 2
Cost	0–5%	5–10%	5–10%	5–10%	5–10%
Platform example	Kiva	NextSeed	NetCapital	Localstake	StartEngine
Platform required?	No	No	Yes	No	Yes
Reporting requirements	The platform may have requirements	Quarterly	Annually	None	Tier 1: 30 days after ending an offering Tier 2: Annually, semi-annually, and special events
Resale restrictions	Not available	9 months	1 year	1 year	None
Public Solicitation	Yes	Yes	Yes, but restrictions apply when soliciting outside of the platform	(b) No (c) Yes	Yes

The MEDC is the state's marketing arm and lead advocate for business development, job awareness and community development with the focus on growing Michigan's economy. For more information on the MEDC and its initiatives, visit www.michiganbusiness.org.

About the authors

The "Investment-Based Crowdfunding Field Guide" is published in collaboration with the Michigan Economic Development Corporation and Revalue, a registered investment advisor (RIA), located in Ypsilanti, Michigan.

Revalue is a home for people passionate about cultivating an abundance mindset in service of community resilience and future generations. The company's mission is to be financial navigators, connecting people to their purpose by crafting values-aligned financial plans and creative educational programming in partnership with those they serve. Learn more about Revalue at www.revalueinvesting.com.

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