Economic Development Practitioners (EDP)

Guide to Investment
CROWDFUNDING
Through MNVest Legislation
Why “MNVest Legislation Investment Crowdfunding” matters to Minnesota-based businesses and what does it mean for an Economic Development Practitioner (EDP)?

Crowdfunding is by definition, “the practice of funding a project or venture by raising many small amounts of money from a large number of people, typically via the Internet.” Small businesses struggle to stay afloat and entrepreneurs face even greater odds when searching for startup capital. Investment Crowdfunding offers these individuals a chance at success by showcasing their businesses and projects to the entire State of Minnesota.

The role of the Economic Development Practitioner (EDP) is critical to the success of many crowdfunding offerings and creating an entrepreneurial friendly region. Economic development can be defined as efforts that seek to improve the economic well-being and quality of life for a community by creating and/or retaining jobs and supporting or growing personal incomes and the tax base.

Job creation, economic output, and increase in taxable basis are the most common measurement tools used by economic development organizations. When considering measurement, too much emphasis has been placed on economic developers for “not creating jobs.” However, the reality is that economic developers do not typically create jobs, but facilitate the process for existing businesses and entrepreneurial start-ups to do so. Therefore, the economic development professional must make sure that there are sufficient economic development programs in place to assist the business achieve their goals. Assistance and support throughout the process of developing a successful investment crowdfunding campaign is just one tool the economic development professional may use.

Investment Crowdfunding in Minnesota, developed with the recently passed MNVest Legislation, allows for equity-type investments in Minnesota businesses by non-accredited\(^1\) Minnesota residents. Non-accredited investors can provide up to $10,000 per investment with no limit for accredited investors\(^2\). Companies are subject to maximum investments per offering. Caps on funds raised via MNVest Legislation are $2 million per 12 months with audited or reviewed financial statements and $1 million with internally prepared financial statements.

Companies must provide detailed disclosure documents that comply with statutory requirements and funds must be held in escrow until minimum funding targets are reached. All MNVest Legislation offerings must be conducted through an approved portal. “MNVest Portals” are subject to stringent recordkeeping requirements and general oversight by the Minnesota Department of Commerce. MNVest Portals
do not need to be registered broker-dealers. Issuers may create their own MNvest portal or work with a third-party host platform.

Project creators typically develop a short video as an introduction to their project and graphics/images to elaborate. The idea is to create a compelling message that readers will be drawn towards.

The idea of “it’s not what you do, but why you do it,” really hits home here. By focusing on a bigger purpose project creators will be able to create a unique community of likeminded individuals. Leveraging existing customers can be key to a successful offering. Each offering has a set goal amount of money and a fixed number of days. Once the project is launched, each day will be counted down and the money raised will be tallied up for visitors to follow its success.

Instead of traditional investors, crowdfunding campaigns are funded by the general public. Typically, most successful crowdfunding efforts receive about 25-40% of their revenue from their first, second and third degree of connections. This could include friends, family, work acquaintances, or anyone that the business is connected to, including their second and third degree connections. Once a project has seen some traction unrelated consumers start coming out of the woodwork to support campaigns they believe in.

There is a huge misconception that creating a successful crowdfunding offering is as simple as hitting the submit button and waiting for it to go viral. While this has happened, the vast majority of projects will require a decent amount of energy, effort and resources on the part of the project creator and their team of technical assistance providers. Seek professional advice since another type of exempt offering may be more appropriate for the business. There will be costs associated with any type of MNVest Legislation offering. Each project’s cost will vary depending on the business and offering!
Utilizing social media, creating email distribution lists before the project launches and contacting local media are all necessary steps prior to the launch of the offering. Remember, this is not a platform to ask for a handout. If the business expects people to invest they must be prepared to prove the potential return on investment. Each offering must contain the deal structure identifying what you are offering and at what price—debt, equity, convertible debentures, distributions, etc. Each offering must contain disclosure documents that summarizes the offering and discloses material risks to investing in the offering. It’s important to build the right team of management and advisors to create the path to a successful offering.

Businesses also need a solid understanding of what they can legally say and do under the MNVest Legislation exemption. The business’ success (and or failure) in raising capital will be in the public eye.

Each offering should contain a powerful reason behind the idea, exciting and unique rewards in addition to the offering and an eye-catching display. Videos definitely play a huge role in this last point, and novice film makers might want to consider taking the time to ask for assistance from an educated friend or seeking a crowdfunding platform that assists with the video editing. In this age of digital sophistication many investors will stop if they don’t connect to the video so this is really the gateway to the proposal.

“Investment Crowdfunding” creates a funding opportunity that certain smaller businesses may not have received in the traditional way and offer a great outlet for more established companies that may be interested in expanding their product range. Reverse engineering the investment could be a good idea, not to mention
the excitement they can generate before the launch. Crowdfunding, in general, has proven itself as a great asset in sourcing potential customers and growing an audience.

Additional benefits to crowdfunding can be its “locally sourced helping hand” and has proven to be a powerful force. Not only is it providing small businesses with needed capital but it is also encouraging entrepreneurs to continue creating and promoting innovation of existing ideas while aiding the local, regional and state economy.

In addition to the upcoming “MNVest Portals” for investments, there are numerous social crowdfunding platforms where consumers can ask for and/or donate money such as Kickstarter, Indiegogo, RocketHub, and Onevest co-founded by Tanya Prive, to name a few. While each site offers their unique spin and related fees the general concept of social crowdfunding is the same across the board.


1Non-accredited investors- investors who do not meet certain net worth or income thresholds to be deemed sufficiently sophisticated and/or financially stable to understand and navigate investment risks.

2Accredited investors are: An individual with a net worth of at least $1 million, not including the value of his or her primary residence; An individual with income exceeding $200,000 in each of the two most recent calendar years or joint income with a spouse exceeding $300,000 for those years and a reasonable expectation of the same income level in the current year.
What is Crowdfunding through “MNvest Legislation” Securities Regulations?

Crowdfunding is a potential new source of capital for rural small businesses in Minnesota utilizing the MNvest Legislation Registration Exemption. The growing interest in communities to invest locally presents an opportunity for a new type of investor for small businesses: Minnesota “non-accredited” residents willing to invest in Minnesota businesses.

Smaller investment amounts from several individuals contributed into a funding pool to assist local businesses also known as “equity or investment crowdfunding”, this internet-based approach helps small businesses raise capital from individuals interested in backing the business and seeing a return on their investment at some point in the future. Equity or investment crowdfunding is an outgrowth of donation/social crowdfunding where investors received token gifts or perks versus equity, shares or stock ownership in the business they supported.

The Securities Exchange Commission (SEC) was created to protect investors, this means the burden of compliance is on the business owners who are seeking capital. Individual investors are responsible for performing their own Due Diligence.

The MNvest Registration Exemption allows Minnesota businesses and entrepreneurs to offer and sell intrastate securities through a registered Internet portal in order to raise capital through local investment. So long as issuers of MNvest offerings comply with notice filing requirements and other conditional requirements included in section 80A.461, such offerings will be exempt from Minnesota’s securities registration requirements.

Entities controlling the Internet portals through which MNvest offerings are sold are required to register with the MN Department of Commerce as MNVest Portal operators.

Minnesota investors particularly “non-accredited”, who work through MNVest Portal operators to purchase MNvest issuers’ securities are beneficiaries of the MNvest Registration Exemption. Federal and state securities laws have long precluded issuers from selling or marketing certain securities to non-accredited investors (investors who do not meet certain net worth or income thresholds to be deemed sufficiently sophisticated and/or financially stable to understand and navigate investment risks).
Accredited investors are:

1. An individual with a net worth of at least $1 million, not including the value of his or her primary residence;

2. An individual with income exceeding $200,000 in each of the two most recent calendar years or joint income with a spouse exceeding $300,000 for those years and a reasonable expectation of the same income level in the current year

In the years since the JOBS Act 2012 was passed, and in response to the SEC’s delay in implementing rules, several states passed legislation allowing for intrastate equity crowdfunding offerings to be exempt from state securities registration requirements within their own state’s borders. Minnesota is one of those states, with the adoption of section 80A.46. The SEC’s recent amendments to Rule 147, create a federal securities registration exemption for issuers of securities that comply with state regulations, such as MNvest Legislation, pertaining to intrastate offerings.

The adopted and proposed rules and federal regulations widen opportunities for businesses and entrepreneurs to raise money while attempting to simultaneously protecting investors in those businesses and endeavors from financial harm.
What financial work is priority for Crowdfunding Offering?

1. All business and personal funds need to be separate

2. Historical financial performance to date and projected financial performance in the next 3-5 years
   a. Realistic estimates of net profit and projected investor returns

3. Financial goals and minimum requirements of total project and crowdfunding offering. What will be done with the money raised? Buy equipment, purchase property, construction, working capital, inventory, etc.
   a. What are the sources of funds? Loans, grants (?), owner equity, other investors, etc.

4. Record ALL Contributions
   a. What are the TAX Requirements? Is this taxable income?

5. Track Expenses
   a. Estimates of all expenses
   b. Receipts of all expenses-RETAIN for potential IRS Tax-related audits

6. Taxes-Investors require
   a. 1099-K form with IRS

7. UNCLE SAM-IRS
   a. Track Receipts and Expenses

8. Seek professional Tax/Accountant Advice!!!
   a. There will be costs associated with any type of MNVest Legislation offering. Each project’s cost will vary depending on the business and offering!
Tips for Developing a Successful Crowdfunding Offering?

1. Detailed business plan that explains the business and financial statements.
2. Start with close connections—Personal/owner network; Founding Team’s friends and family
3. Personalize the message—is it local foods/goods/services, community-based business, solving a problem, e.g.
4. Take fundraising efforts offline
   a. Meet with people and have personal interactions
5. MNVest Legislation crowdfunding doesn’t end with the launch of the offering
   a. A capital raising campaign is hard work and requires time, energy and resources!

What other priorities/concerns for Crowdfunding Offering?

1. Make sure the business DOES THEIR RESEARCH—Borrow ideas from the BEST—KNOW their stuff
2. Is the idea and/or product a good fit for investment crowdfunding?
   a. Consider who are potential investors
   b. (Hint) Typical backers are young males....
   c. Seek professional advice since another type of exempt offering may be more appropriate for the business.
3. Execute with excellence
   a. Professional quality videos, photos, copy and editing
4. Make it happen!
   a. 30% of funding goal usually occurs in first 24 hours
5. Not giving advice, but one thing to always keep in mind, never ever encourage others to invest money they can’t afford to lose!
Additional Resources:

www.northcentraleda.org
www.mnvest.org
www.thedatabank.com
http://www.crowdfundingguides.com/The%20Crowdfunding%20Bible.pdf
http://whatis.techtarget.com/definition/crowdfunding
www.crowdsourcing.com
www.crowdsourcing.org/directory
http://www.smallbusinesssuccess.ca/ebooks/prince_albert/pdfs/2013_CrowdFunding.pdf
http://www.entrepreneur.com/article/228534
www.sec.gov
www.sba.gov/tools
www.buylocaltwincities.com/MNVestWebinarRecording

Preparation – Execution – Will Power

The JOBS Act of 2012 Title III: Regulation Crowdfunding requires these intermediaries to, among other things:

- provide disclosures that the SEC determines appropriate by rule, including regarding the risks of the transaction and investor education materials
- ensure that each investor: (1) reviews investor education materials; (2) positively affirms that the investor understands that the investor is risking the loss of the entire investment, and that the investor could bear such a loss; and (3) answers questions that demonstrate that the investor understands the level of risk generally applicable to investments in startups, emerging businesses, and small issuers and the risk of illiquidity;
- take steps to protect the privacy of information collected from investors;
- take such measures to reduce the risk of fraud with respect to such transactions, as established by the SEC, by rule, including obtaining a background and securities enforcement regulatory history check on each officer, director, and person holding more than 20 percent of the outstanding equity of every issuer whose securities are offered by such person;
- make available to investors and the SEC, at least 21 days before any sale, any disclosures provided by the issuer;
- ensure that all offering proceeds are only provided to the issuer when the aggregate capital raised from all investors is equal to or greater than a target offering amount, and allow all investors to cancel their commitments to invest;
- make efforts to ensure that no investor in a 12-month period has purchased crowdfunded securities that, in the aggregate, from all issuers, exceed the investment limits set forth in section Title III of the JOBS Act; and any other requirements that the SEC determines are appropriate.