Equity Crowdfunding: positioning and inquiry from an entrepreneurial perspective

Authors: Kevin De Moortel[a], Promotor: Marc Goldchstein[b],
[a] Vrije Universiteit Brussel, Pleinlaan 2, B.2.06.B, Elsene, Belgium
[b] Vrije Universiteit Brussel, Pleinlaan 2, B.2.14, Elsene, Belgium
Corresponding author: Kevin De Moortel. Tel.: +32 488 27 69 06.
E-mail address: kdemoort@gmail.com (K. De Moortel)

Abstract

Equity crowdfunding has recently risen as an alternative equity crowdfunding method for funding a start-up company. With banks being less eager to providing a loan to the entrepreneur and traditional equity funding methods being rather inaccessible or too demanding, the entrepreneur is in need of this new type of capital resource. However, a general overview of the positioning and the practices of this method, which would support the entrepreneur, is lacking. This thesis will elaborate on these two aspects via a critical literature review and a study on twenty popular and global equity crowdfunding platforms. Three interviews were deducted to support following findings. Firstly, this thesis concludes that equity crowdfunding complementary positions itself on the funding market between angel investors and venture capitalists, but that overlaps are present as well. This shows that the techniques are also competing with each other. Secondly, this thesis provides a set of considerations that indicate common practices on today's equity crowdfunding platforms. This thesis shows that these practices may sometimes contradict previous literature, indicating fast evolutions of the platforms. Therefor, developments of equity crowdfunding need tracking in the future.

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Chapter 1 - Introduction

Although start-up companies are frequently little more than an innovative idea, these initiatives contributed their fair amount in technological and scientific advances and in job creation and economic prosperity (Ibrahim, 2008). However, at the beginning of their entrepreneurial adventure, entrepreneurs often lack the ability to attract outside capital (Schweinbacher & Larralde, 2010). Indeed, a considerable amount of information asymmetry, high level risk and uncertainty leaves the investors in these projects somehow reserved and cautious of opportunistic behavior on behalf of the entrepreneur (Wilson & Testoni, 2014; Lerner, 1998; Agrawal, Catalini, & Goldfarb, 2013). In addition, the lack of assets, collateral and track record, and the risky nature of the business wipes out the possibility of traditional bank loans for a great deal (Wilson & Testoni, 2014; Schweinbacher & Larralde, 2010; Collins & Pierrakis, 2012). This is a clear indication of the impact of the recent (2009) financial crisis and, consequently, the stricter financial environment. And it does not end there. Banks want to have certainty; they want to know every aspect and detail on the start-up company (R. Peels, personal communication, April 23, 2016). This is information that entrepreneurs generally cannot provide yet in a start-up phase. In spite of these issues, capital choices have shown to be of crucial importance for the operations of the business, risk of failure, firm performance, and the potential of the business to expand (Cassar, 2004). Luckily for the entrepreneur several other financing methods are available to overcome these barriers. Keeping in mind that a proportion of the capital structure of a start-up firm could be based upon debt financing, equity financing provides support to the entrepreneur in ways debt financing does not. For example, equity finance distributes the actual risk between the manager and the stakeholders, whereas debt financing makes the entrepreneur bear the risk alone: the bank requires a mortgage. Of course, this has to do with the nature of equity financing, where the entrepreneur sells shares of his firm, and thus part of an ownership interest, to willing investors. This paper will merely focus on equity financing.

Traditionally entrepreneurs of young firms find themselves confronted with financing via family and friends, angel investors, and venture capitalists. But venture capital and business angels are getting a lot of criticism for a lack of regional, gender, and ethnic inclusiveness (Estrin & Khavul, 2016). With the emergence of crowdfunding, a fourth method has taken its place in the row. Ahlers, Cumming, Guenther and Schweizer (2012) define crowdfunding as “an umbrella term used to describe an increasingly widespread form of fundraising whereby groups of people pool money, typically small contributions, to support a particular goal” (p. 1). Different forms of crowdfunding exist, yet equity crowdfunding, on which this paper will focus, tends to be the most complex (Wilson & Testoni, 2014) one and tends to be less studied, compared to donation and reward-type crowdfunding (Estrin & Khavul, 2016).

Equity crowdfunding, also referred to as *crowdinvesting*, deals with “the way entrepreneurs sell equity or equity-like shares to a group of (small) investors through an open call for funding on Internet-based platforms” (Ahlers et al., 2012, p. 1). Some authors (e.g. Hagedorn & Pinkwart, 2013) argue that this new form of equity financing is in particular addressed to start-up companies. This is then reflected in their definition of the concept: “Crowdinvesting is a financing method for young ventures and other commercial projects that supports the acquisition of equity by coordinating the submission of different forms of shares to an undefined group of possible investors through social virtual communities” (Hagedorn & Pinkwart, 2013, p. 17). These social virtual communities, typically in the form of Internet-based platforms, play a vital role in crowdinvesting as they connect the entrepreneurial demand with the financial supply of the investors. In fact, they often provide financial contracts to the issuer, marketing and business guidance to the entrepreneur, and an investor network by advertising the available securities (Hornuf & Schwienbacher, 2014a). Frequently a previously determined success fee is asked in return.

This paper tends to analyze this setting from an entrepreneurial perspective and will focus on the role of equity crowdfunding, compared to other equity financing methods in the entrepreneurial start-up market. Indeed, the first part of this paper consists of an extensive study and comparison of the different forms of equity financing: family and friends, angel investors, venture capitalist and equity crowdfunding. As equity crowdfunding is less studied in literature, due to the recent nature of the matter, the second part of this paper focuses on a particular component of crowdinvesting, namely the equity crowdfunding platforms. The performed comparison of the financing methods and the study of the equity crowdfunding platforms will, as a whole, contribute to answering substantial questions for every entrepreneur willing to start his own business. Thus, the main research topic of this thesis will be to, firstly, *position equity crowdfunding next to the alternative equity financing methods*. For the entrepreneur this could provide a good overview to select the proper equity capital source for his/her start-up company. Secondly, this thesis will focus on the equity crowdfunding platforms in particular and will try to *answer a set of entrepreneurial questions related to the equity crowdfunding platforms*. This will give the entrepreneur actual insights in how to deal with these platforms and what to expect when they choose the path of equity crowdfunding.

Chapter 2 - Literature Study on Equity Financing Methods

This literature review will contain two main parts. First this chapter will look at the different forms of equity financing individually: family and friend, angel investors, venture capital, and equity crowdfunding. Then, on several levels, equity crowdfunding will be compared to the other financing methods. Thus this thesis will compare key characteristics of an investment, investor's characteristics, entrepreneurial characteristics, and contracting between the traditional financing methods and equity crowdfunding. Hereafter, equity crowdfunding will be positioned between the other financing methods. This chapter will conclude with indicating clear interrelation between all financing forms.

Different forms of equity financing

A comparison between four different equity financing methods will firstly be provided in this section. Respectively, financing via family and friends, angel investors, venture capital and equity crowdfunding will be discussed. Afterwards, a clear overview of the differences and resemblances between those forms will be given, primarily based upon the key characteristics of equity financing. The goal of this section is for a new entrepreneur to dispose over a clear image of the different forms of financing available.

In order to fully understand the following sections, it is important to introduce a few concepts. First of all, the reader should be aware of the fact that financing a start-up firm typically consists of three stages of financing. The first stage is the *seed stage*. At this point, the business of the entrepreneur is merely an idea or a concept (Manchandra & Muralidharan, 2014). In this stage, initial capital is required to transform this idea into a successful commercial enterprise. The second stage is the *early stage*. Here, the actual production and distribution of a product or service is being handled (Ramadani, 2009). Financing is necessary to develop this product or service properly. The third stage is the *later stage*, where the enterprise takes on a mature level and hopes to expand itself as much as possible. In this paper it will become clear that each of the different equity financing methods prefer a certain stage of financing. Also this paper will refer to *staged financing*. This consists of the investors providing their committed money in pieces. Typically this is some form of risk reducing by the investors, as they will monitor the company and the established goals along the way of their financing.

Secondly, different types of equity shares will be used through the comparison of the different financing forms. A *common share* refers to the ownership in a company by an investor (Weston, n.d.). With this ownership, typically comes a claim on a portion of the profits of that company. A *pro-rata share* indicates that investors will get a proportion of the profits of a company, determined by the amount of investment. *Preferred share* can be seen as an elite form of common share. Where common shares provide uncertain and variable dividends, preferred share commonly provide certain and fixed dividends. Preferred shares are *convertible* when the investor has the right to turn them into a set of common shares on a predetermined date or after a predetermined period of time. In contrast to shares, bonds are debt securities, instead of equity securities. Negative bonds give the investors rights to accept or decline a certain decision of the company. *Convertible bonds* give the investors the right to turn the bonds into a predetermined amount of equity of the company (Stein, 1992). Lastly, *participation notes and cooperative certificates* refer to the acknowledgment of a certain deposit by the investors. These two terms will in particular be used in the context of equity crowdfunding.

Thirdly the concepts moral hazard, information asymmetry and due diligence might need proper explanation. Moral hazard consists of “the risk that the existence of a contract will change the behavior of one or both parties to the contract” (Brealey, Myers & Allen, 2007, G-10). Due diligence refers to the performance of an (extensive) investigation of a certain person or company. Information asymmetry simply refers to one party having more information over the other one in a given situation.

Lastly, when considering the exit strategy of a firm, the term IPO will be used several times. IPO, or initial public offering, refers to “a company’s first public issue of common shares” (Brealey et al., 2007, G-8). This consists thus of a private company turning public by selling shares, and thereby ownership, to the public.

Financing via Family and Friends

When own capital of the entrepreneur is virtually nonexistent, family and friends can provide finance to the entrepreneur to start up the company (Wilson & Testoni, 2014; Agrawal et al., 2013; Lee & Persson, 2012). Typically this form of financing takes place in the first phases of development of the start-up; also known as the seed stage.

Agrawal et al. (2013) also mention that the amount of investment on behalf of family and friends is of a disproportional kind, yet until a certain limit is reached (Lee & Persson, 2012). In addition, a mix of selfishness and altruism on behalf of the entrepreneur drives the proportion of the required funds by family members (Basu & Parker, 2001).

Not only can family and friends get involved in the entrepreneur’s start-up activities, they can interact with the entrepreneur on different levels. Dyer & Handler (1994) identified three other “career nexuses”, next to the start-up phase, where family and the entrepreneur can intersect: early experiences in the family of origin, employment of family members, and involvement of family members in ownership and management succession. Although this study did not mention any participation of friends, it can be argued that the relationship between the entrepreneur and friends is similar to that between the entrepreneur and his family.

In addition to the financial and labor aspects, family and friends can provide contacts and other resources (Dyer & Handler, 1994). Also, in the alternating positive and negative experiences and entrepreneurial endeavors, which come with starting a business, they can provide a refuge.

Despite the costless offer of these family members and friends, also commonly referred to as *informal* investors, many entrepreneurs seem to prefer some form of *formal* finance (Lee & Persson, 2012). This can have several reasons. Weinberg (n.d.) indicates that several friends and family members may demand their money back or, in a worse scenario, may cause a lawsuit against the entrepreneur. Also, they can be time consuming by trying to help, getting intensively involved or over-visiting the firm of the entrepreneur. Lee & Persson (2012) studied the social preferences through a model of external finance and found that family finance even constrains entrepreneurial risk taking and growth of the firm. All this, could resolve into the social loss of valued friendships or family members (Weinberg, n.d.). Also, family and friend may require preferred stocks when financing the entrepreneur. However, this can leave them diluted afterwards, as the issuing of new shares in a time when the business is growing will typically leave them with less value in hands than possible via these new issues. Previously mentioned advantages also hold the assumption that there is a good form of social interaction between the entrepreneur and his family and friends. In case of absence of this, family and friends can prove to be a real obstacle to starting a new firm, by providing few material or financial resources and/or no social support (Dyer & Handler, 1994).

When an entrepreneur chooses to neglect the possible downsides of financing via family and friends, his mind might be driven by two important factors. Firstly, Basu and Parker (2001) recognize that participation in family finance is dominantly driven by selfish motives on behalf of the entrepreneur. Secondly, Agrawal et al. (2013) argue that financing from family and friends can trigger later investors trough accumulated capital, and thus ensuring future financial investments (typically by other parties). Independently from the will of the entrepreneur, he needs to be aware of the fact that financing via informal investors may or may not be suitable for a given start-up venture. Lee and Persson (2012) suggest that it is suitable for mitigating endogenous risks, like moral hazard. Indeed, when family or friends of the entrepreneur bear or share the risks of the entrepreneur's actions, the latter may be more cautious and prudent in taking those risks, due to social convention. In contrast, financing via family and friends tends to be unsuitable for ventures with significant exogenous risks, like uncertainty. For example, it is quite common that in order to protect his close ones, the entrepreneur will not accept decisions that bear too much uncertainty or tend to be uncontrollable, due to exogenous factors.

In cases where involvement of the family gets high, the whole system of the firm can be referred to as a family system instead of a common business system (Dyer, 1992). In such systems the goal is rather the development and the support of family members instead of profits, growth and revenues. Also, written and formal rules can get replaced with informal expectations. Relationships are rather deeply personal. In family systems, succession will be determined by death of divorce, and not by retirement or promotion.

In conclusion, financing via family and friends typically occurs in the seed phase of a start-up company, yet can be seen as the most important equity financing method available for entrepreneurs (Basu & Parker, 2001). The invested amount is disproportional, yet limited. Some social aspects, like the avoidance of moral hazard, support in endeavors and provision of labor, may benefit the start-up and development of the enterprise. Other aspects, like the possible loss of contact, restricted growth of the company and consumption of time, may hinder the start-up venture. This is why Lee and Parsson (2012) suggest combining informal family and friend's capital with some form of formal capital. Nevertheless, they indicate that impersonal financial relations may be critical to certain types of entrepreneurial activity.

Financing via Angel Investors

Angel investors typically are high net-worth individuals investing in small, private, and often innovative firms on their own account (Wong, Bhatia, & Freeman, 2009). They have a lot of business experience and entrepreneurial and managerial background. This is why, next to their money, they also provide their time, expertise, skills, knowledge, participation in operations, and relationships. This all, in the hope of getting a financial gain (Ramadani, 2009; Mason, 2006), altruistically give back by helping other entrepreneurs (Wilson & Testoni, 2014), or simply for fun and pleasure (Ramadani, 2009). As a result of their experience, angel investors are known to invest in the seed, start-up and early stage of enterprises and thus, in particular, being important for small and medium-sized enterprises (Ramadani, 2009; Freear, Sohl, & Wetzel, 1994; Wilson & Testoni, 2014; Aernoudt, 1999). In terms of geographic activity, the angel market tends to be heterogeneous and localized (Prowse, 1998; Freeat et al., 1994). The venture they invest in can vary a lot, yet it is not uncommon that they typically invest in ventures that are familiar to them (Wong et al., 2009).

Some authors went further and even investigated the typical profile of an angel investor (e.g.: Ramandi, 2009; Mason, 2006; Aernoudt, 1999). The typical angel investor is a 40/45 – 65 year old man, with high qualifications and education, and a wealthy established living environment, due to the advantageous selling of their own enterprise. He makes risky decisions by nature, which has led him to success in managing companies.

Wilson and Testoni (2014) value the amounts invested by angels between $25.000 and $500.000. Prowse (1998) mentioned ranges between $50.000 and one million dollars. Some authors are rather cautious in pasting a value on the amount of funding. Weinberg (n.d.), for example, speaks of a 'larger' amount of capital compared to family and friends finance, Ramadandi (2009) of a 'significant 'amount and Mason (2006) of an amount that is beyond the ability of resources from family and friends, but below the minimum investment threshold of venture capitalist funds. Ibrahim (2008) shares this last description as well. Additionally, Aernoudt (1999) argues that an angel investor generally invests 25% of his total assets in informal ventures. In return for this the angel seeks a return on his investment with an internal rate of return of around 20%.

Several activities tend to be linked to the behavior of angel investors. It is notable that these activities are closely related to the fact that angel investors provide their capital in the early, risky start-up stages of the firm. A key characteristic is the performance of due diligence. To assess the potential value of the firm, angel investors will often perform this on a regular basis (Wilson & Testoni, 2014). This can be time and resource consuming for the angel, but evidence shows that it is an important determinant in achieving proper return on investment. To additionally ensure proper returns Wong et al. (2009) found three control mechanisms to manage the risks, like expropriation by the entrepreneur, that go along with the early investments. The first one is the amount of funding, which typically is smaller than that of venture capitalists. Also the amount of funding is reflected in the uncertainty that the angel investors has. This uncertainty can be alleviated with the creation of manager teams in the firm, the correspondence of enough information, history of the entrepreneur, and so on. The second one is the use of syndication. This basically consists of the angel investing in a portfolio of companies and thereby diversifying the risk. And the third one is geographic proximity. Indeed, geographic proximity between angel investors and their investments may influence the amount of funding, control, and degree of post-investment assistance by the angels.

Procedures of the interaction between the entrepreneur and the angel are fairly straightforward. Mason (2006) elaborated the different stages that occur. In the deal origination, angel investors and the entrepreneur meet each other in some kind of way. Secondly, the initial screening (first impressions) and a detailed evaluation are performed in the deal evaluation stage. Thirdly, terms are negotiated and the contract in fixed with a focus on pricing. Fourthly, the investor gets involved in a hands-on manner with the business in the post-investment stage. Finally, the angel investor exits the enterprise, either by the failing of the enterprise or by selling his shares.

An interesting stage in terms of literature and ongoing investigation is the contracting stage. Indeed, in many cases the interaction between the angel investor and the entrepreneur is sealed with a contract. This contract often includes anti-dilution provisions that protect against the risks of failure of the firm, rights that facilitate the exit opportunities of the angel, and liquidation preferences with higher priority in the distribution of the firm's value (Hornuf & Schwienbacher, 2014a). Higher priority may be achieved by opting for securities such as preferred shares. In addition, angel investors are known to stage their provision of capital, to reduce risk exposure. With respect to the contracts, Ibrahim (2008) broke the conventional wisdom that these contracts are rather simple and entrepreneurial-friendly for angel investors despite the extreme risks that in practice occur. He proofed that upon closer examination, these contracts are often rationally designed with clear financial and nonfinancial goals in mind. In fact, the author mentions the professionalization of angel investing as a trend; the evolution of contracting herein is a clear illustration of this.

Nevertheless, the closer involvement of the angel investors may have rather negative side effects as well. Weinberg (n.d.) describes some of these drawbacks. In terms of the amount of financing, angel investors may have their limits, just like friends and family. Because of the due diligence, these investors might ask the entrepreneur to produce better business plans or create a management team. Also, angel investors might demand a seat in the board of directors and voting rights or might demand preferred shares, which can leave the entrepreneur with minor priority and less control or decision power. Also, as angel investors are seeking profit, they might control the exit or sell of the firm differently than the entrepreneur would. Often the company is sold quite soon and thus no longer private. Wilson & Testoni (2014) even argue that achieving a positive exit is a long and scare process. Another known issue is the double trust dilemma, where on the one hand no angel investor is willing to finance a firm without knowing the exact value of the firm (Hornuf & Schwienbacher, 2014a). On the other hand investors might use the innovative information without giving compensation, which leaves the entrepreneur cautious to reach out for the funds. This dilemma, however, can be solved via the creation of non-disclosure agreements.

In conclusion, entrepreneurs are rather fond of angel investors' capital as it provides them not only the money, but also the knowledge, expertise, support and so on (Mason, 2006). This might give the entrepreneur a reason to prefer the 'empathic' angel financing method instead of other financing methods (Fairchild, 2011). However, the choice of financing method needn't be exclusive. It can be said (Ramadani, 2009; Wilson & Testoni, 2014) that they fill the gap between family and friends' capital and venture capitalist, which will be discussed in the next section. Indeed, angels invest at a critical time, after friend or family money has reached its limit, yet before venture capitalists will start to invest (Ibrahim, 2008). As a result it can be said that angel investors fulfill a complementary role, between, friends and family, and the venture capitalists in the financing of new ventures (Wong et al., 2009; Aernoudt, 1999). In any case, all this tends to be the case for the typical angel investor. Participation, the venture they invest in, the funding process, contractual terms, formal or informal attitude and so on, can vary among angels (Wong et al., 2009) or as Prowse (1998) puts it: “Angels appear to be extremely diverse” (p. 787).

Financing via Venture Capitalists

Venture capital can be seen as the professional form of equity financing (Wilson & Testoni, 2014). The form exists thanks to the collaboration of institutional partners; in which each of them contribute an amount of funding. These funds are then assembled to typically finance new technology-based start-up firms. Indeed, Hellmann and Puri (2000) approve that venture capital financing is of great influence for new innovative firms. Financing in these firms can occur in different stages of the firm’s evolution and in several rounds. However, venture capitalists generally focus on those enterprises that are in a more evolved stage of their existence. This can lead to the appearance of a funding gap between the early investments of more informal investors (family, friends, and angels) and the later-stage investments of formal investors of venture capitalists.

A well-known goal of venture capitalists is to make the company grow quickly to get their return on investments as soon as possible (Weinberg, n.d.; Davila, Foster, & Gupta, 2000). Evidence from Davila et al. (2000) shows that the growth factor of the firms is significantly higher than that of firms that are financed via non-venture-capital methods. Nevertheless, venture capitalists are aware of the fact that actual payout may only be likely in about five to ten years (Macmillan, Siegel, & Narasimha, 1985; Tyebjee & Bruno, 1984). Bergemann and Hege (1998) and Tyebjee and Bruno (1984) even mention that short term financing of these types of ventures can never be optimal and remains illiquid. In return, venture capitalists expect a good return on investments, as will be discussed in one of the next paragraphs. They will try to achieve this growth of the firm through extensive follow up and periodically monitoring of the firm's evolution. Also, not only financial contributions, in the form of follow-on capital, but also social ones, in the form of relationships and networks, are added to the business (Fairchild, 2011; Davila et al., 2000). Thus, venture capitalists also provide managerial and value-adding support to the entrepreneur. This skill augmentation and reputation signaling can get the enterprise the advantage of high quality employees, new customers, alliances, and joint ventures (Davila et al., 2000). The success of this lays in the hands of the venture capitalists themselves, who devote a lot of time and effort in the understanding of new technologies and markets.

The intensive way venture capitalists study their environment is also reflected in the way they approach potential ventures for investment. Indeed, just like angel investors, venture capitalists perform some form of due diligence to reduce the risk of failure (Wilson & Testoni, 2014). It can be noted that this due diligence takes on a more extensive form in the case of venture capitalists. This can be illustrated by the amount of studies that seek the motives of venture capitalists to finance a certain entrepreneur and his firm. Macmillan et al. (1985) found that above all, the quality of the entrepreneur, in terms of experience and personality, is the ultimate determinant for the funding decision. The authors continue that the business plan of the entrepreneur should reflect the potential of the entrepreneur in terms of staying power, reacting to risks and so on. When the entrepreneur lacks these characteristics, he should pull together a team that does possess them and the entrepreneur should show that he is able to lead this team towards success. It appears that without a good management team or entrepreneur, good financials are meaningless, as they will never be achieved (Muzyka, Birley & Leleux, n.d.). An older study of Tyebjee & Bruno (1984) suggests that venture capitalists actually consider five main elements: market attractiveness, product differentiation, managerial capabilities, environmental threat and resistance, and cash-out potential. In sum, Salomon (2014) indicates that the due diligence procedure is indeed based upon several decision-making criteria and is concluded by a standard financial ratio analysis, as the financial side can certainly not be neglected.

In contrast to angel investors, venture capitalists do not invest their own money in firms (Wong et al., 2009). They raise money from other funders and invest that money into chosen enterprises. The amount of money tends to be twice the amount that angels provide; this is around three million and five million dollars (Wilson & Testoni, 2014) or even more (Weinberg, n.d.). In addition, as mentioned before, venture capitalists typically invest several times (rounds) in an enterprise, with the amount invested increasing each time (Sahlman, 1990). This leads to amounts of investments typically higher than other forms of financing for start-up firms. Of course, these big investments need to generate income for the venture capitalists. The choice for technology-based firms makes their investments generally more risky, which of course means that they may require higher excepted return on their investments, compared to angel investors. Similarly to angel investors they will invest in a portfolio of firms to diversify these high risks.

The procedures and steps that venture capitalists follow are similar to those of angel investors. Tyebjee and Bruno (1984) summed up these different steps in their study. The first step is the deal origination, where venture capitalists consider several possible ventures for investment. Next, deal screening is performed. Here, venture capitalists consider several variables, like size of investment, policy of the venture, the market, stage of financing, and location, to look at the potentials of a certain venture. Third, risks and expected returns of a venture are considered in the deal evaluation phase. In the deal structuring phase the arrangement is then set up and a specific contract closes the deal. The last phase concerns the post-investment activities of venture capitalists. These include the previously described assistance, planning, financing and so on. At the end of the collaboration between the entrepreneur and the venture capitalists the exit form, being a merger, acquisition or public offering, is planned out as well.

As already mentioned before, start-up firms tend to be risky business, filled with uncertainty, information asymmetry and potential opportunism by the entrepreneurs (Ibrahim, 2008). Davila et al. (2000) argue that venture capitalists are best placed, in comparison with other financing methods, to deal with these issues. Indeed, these problems can easily be leveraged by the dependence of entrepreneurs on the financing of venture capitalists. Even more than in the case of angel investors, a contract will be set up, which allows the venture capitalists to screen, monitor and control the investments they made. In many cases, the exit strategy is already predetermined between the entrepreneur and the venture capitalists (Wilson & Testoni, 2014; Ibrahim, 2008). They then will work together and try to make this profitable exit happen. Similar to angel financing, this exit is commonly in the form of a trade sale. Other exit possibilities are via an IPO, which is known to be relatively hard to accomplish, or simply by failing of the enterprise. The contracts will also refer to a form of staged financing, and board seats (Wong et al., 2009; Ibrahim, 2008). Ibrahim (2008) also adds the appearance of (convertible) preferred stock and negative covenants in these contracts.

In spite of all the advantages, venture capital has its downsides as well. As venture capitalists invest significant amounts of money, they may want the main control of the enterprise in return. Weinberg (n.d.) assumes that it will not be uncommon that the entrepreneur needs to give up 50% or more of his shares. He continues that in addition to this, auditing of the financial statements and other forms of control might be urged upon the entrepreneurs. This might be a great burden of the entrepreneur's time, as every detail will need to be agreed upon. This loss of control and uprising of additional efforts might not happen in the case of the somehow more informal angel investors. In addition, the advantages that venture capitalists bring along may only be of relevance to new innovator firms, and not to imitator firms. Indeed, Hellmann & Puri (2000) prove that the latter are less likely to obtain venture capital. And even with the support of venture capitalists the risk of failure of a project of innovative kind is significant (Bergemann & Hege, 1998).

To conclude, it is notable for the entrepreneur that not all venture capitalists necessarily are the same or have the same preferences and goals. Macmillan et al. (1985) divided three types of capital investors. The first type assesses the competitive and implementation risks very carefully. The second type is only searching for easy bail out options. And the third type keeps all options open at all times. Muzyka et al. (n.d.) also found that not all venture capitalist are the same. They divided them in three other groups: those concentrating only on national investments, those focusing only upon the deal, and those consistently evaluating specific management criteria. Also, differences between venture capitalists can be viewed in the amount of investment and involvement in the enterprise. As a result, an entrepreneur should not merely be focused on the typical venture capitalist, but realize that each of them may have other characteristics. This can be of relief for the entrepreneur, as the changes of acceptance to finance may thus be much greater.

Financing via Equity Crowdfunding

The principle of equity crowdfunding is fairly straightforward. The entrepreneur will choose to raise money over an online platform. Consequently he determines the amount of capital he is willing to raise. A (large) set of individuals then chooses to finance the entrepreneur; they become the funders of his new venture. In return for this funding, they will receive some form of equity-based revenue or profit share arrangements (Wilson & Testoni, 2014). Each crowdfunder typically receives a pro-rata share of the starting company, depending on the amount invested by the individual crowdfunder. In summary, crowdinvesting can be defined as the offering of securities by a new privately start-up business to the general public, generally through the medium of an online crowdfunding platform (Collins & Pierrakis, 2012). According to Wilson & Testoni (2014) this last characteristic is what departs equity crowdfunding from the traditional equity financing methods.

It is clear that this form of financing concerns three main parties: the entrepreneur, seeking cash, the crowd, individual investors willing to invest in certain ventures, and online crowdfunding platforms, connecting the two prior parties. Each party has its own vision on the whole financing process. Agrawal et al. (2013) mentions that the entrepreneur is mainly driven by a lower cost of capital. Indeed equity crowdfunding provides the entrepreneur of easily found funders, and additional information from parties that otherwise would be left unknown. In contrast the entrepreneur faces some real disadvantages; their business idea will be exposed publically, property protection may be rare, investors are less eager to helping (in comparison with angel investors and venture capitalists), and also follow-on financing may be a real challenge. The individual investors commonly referred to as the crowd(funders), form the second party. Typically, these invest small amount of money and receive a small stake of the company in return for this money (Ahlers et al., 2012). In contrast to angel investors or venture capitalists, these investors generally lack the financial sophistication, experience, and wealth to provide support or augmented value to the entrepreneur's firm. Also, in contrast with angel investors, these investors needn't be accredited (Hornuf & Schwienbacher, 2014a). The crowdfunders have other incentives to participate in the crowdfunding process (Agrawal et al., 2013): early access to investment opportunities and new products, participation in some sort of community, supporting a certain venture and the idea behind it, and formalized contracts (which will be elaborated later on). Indeed, financial return is not per se a sole motive for the crowdinvestors, e.g. emotional motives may occur as well (Wilson & Testoni, 2014). Their will to invest may however be countered by possible incompetence of the entrepreneur, as everyone can start up a venture. Also, fraud and risks of failure are fairly common. The third party, the crowdfunding platforms, takes on a particular role. These platforms link the investors with the entrepreneurs. In addition, according to Wilson & Testoni (2014), some play an active role in the screening and evaluation of the companies.

In spite of the hype crowdinvesting is currently the smallest part of the whole crowdfunding market (Wilson & Testoni, 2014). Globally, Europe seems to embrace the concept most of all, probably due to the setup of its legal framework. In the United States for example, crowdinvesting is present in the form of only accredited investors financing a venture; thus without the participation of the regular crowd (Hornuf & Schwienbacher, 2014a). Also, not all types of markets are being supported by the recent (started in 2007) financing concept. In fact, crowdfunding developed itself solely in the arts and the more creative industries, like music, film, and video games (Agrawal et al., 2013). The reason for this may be the appearance of indirect network effects or the similarity with other online markets. However, through the recent years the crowdfunding market evolved and thus it can now be said that equity crowdfunding targets particularly all different start-ups, which tend to be young and innovative (Wilson & Testoni, 2014). In addition, crowdfunding becomes a global phenomenon: as online platforms are handled via the Internet, investors are no longer bounded by the location of the venture. Next to this, it might be said that, because of the diverse motives of the crowd, the investment spectrum can even be broader than that of angel investors or venture capitalists. Still, the preference of the crowd for creative ventures seems to remain. Nevertheless it is clear that there is a place on the market for equity crowdfunding. This place seems to entail the seed and early-stage financing of start-up ventures, thus operating in the same financial segment of the more informal financing methods, family and friends, and angel investors.

Typical to equity crowdfunding is that the minimum tickets size to participate for the investors is small so that more crowd investors can participate (Hornuf & Schwienbacher, 2014b). Salomon (2014) speaks in her work of a minimal amount ranging from \$113 to \$282. In theory this means that it should be easier for entrepreneurs to achieve their target. Additionally, Hornuf & Schwienbacher (2014b) indicate that the addition of contractual arrangements that enable more participation from the crowd tends to work best to achieve high targets easier. Wilson & Testoni (2014) argue that for crowdinvesting, as for angel investment, the way to a positive exit can be longer and perhaps less likely to happen.

The equity crowdfunding process may perhaps be less straightforward than that of other financing methods, due to the different characteristics of the different online platforms. However, Collins & Pierrakis (2012) mention that usually the same steps are followed. First platforms receive the applications for venture from the entrepreneurs; they decide which ventures to allow. Second, the funds are being raised. Typically a target amount and a time limit to achieve this amount are determined. Third, the fundraising closes: if the target is reached within time the venture is continued, if not investments are returned to the investors. And fourth, some post-investment activities, interaction between and the crowd, may occur. Wilson & Testoni (2014) describe a similar process. They however include an important last step in this process: the exit phase. In this stage, the entrepreneur finds new sources of capital, whereas the crowdinvestors sell their shares to new investors. In contrast to venture capitalists and angel investors, entrepreneurial firms financed via crowdinvesting are often too small for an IPO on the stock market, which leaves exit opportunities somewhat restricted (Hornuf & Schwienbacher, 2014b). Also, in comparison with the other financing methods, it is in particular the investment process that needs more time, due to a two-step start-up selection process: first by the platform founders, and then by the crowd investors (Salomon, 2014).

Contracting in crowdinvesting is mainly based upon standardized contracts (Hornuf & Schwienbacher, 2014a), provided by the crowdfunding portal (Wilson & Testoni, 2014). With hundreds of parties at stake it might be difficult for the firm to anticipate stage financing via contracting. Hornuf & Schwienbacher (2014b) prove that in contrast of what many may believe, the funding crowd rarely purchases common share. Moreover the use of participation notes, cooperative certificates and convertible bonds gets the main attention. In their other work, Hornuf & Schwienbacher (2014a) argue that the crowd often leaves with profit participating certificates, which ranks them lasts in case of bankruptcy and leaves them with little protection form fraudulent behavior on behalf of the entrepreneur.

On the upside, equity crowdfunding may generate the creations of jobs and economic growth (Wilson & Testoni, 2014; Agrawal et al., 2013). In addition, Agrawal et al. (2013) add that through the new financing form, good ideas, which would otherwise be undercapitalized, now may be funded and that the total capital allocated to innovation may be given a boost. Another advantage of equity crowdfunding in general, pointed out by Manchandra & Muralidharan (2014), is that for a start-up firm this financing mechanism can create brand awareness among the general public, and thus serve as a marketing tool. Indeed, it enables entrepreneurs to test and prove their idea and receive feedback on it.

On the downside, crowdinvesting brings along potential for fraud, unrealistic expectations of investors, the loss of expert advice, and inexperienced creators (Agrawal et al., 2013). Also, crowdinvesting offers little opportunity for a proper form of due diligence. Indeed, the absence of face-to-face interaction and 'trusted' intermediaries generates an asymmetry problem; not only in terms of the feasibility and ability of the creator to deliver a product, but also the ability of the creator to generate real equity value and a running company. Geographic distance between the funders and the entrepreneurs also increases this information asymmetry (Wilson & Testoni, 2014). This all leaves the crowd, the individual investors, with a high risk, which is not directly compensated for via governance, reporting, accounting or other common tools in security trading markets. Often the crowd tries to avoid this proper due diligence through discussion forums available on the crowdfunding platforms (Salomon, 2014). However, the high risk and necessity to perform due diligence, is also countered by the fact that the investments of the crowd are relatively small and they can thus also diversify their risk by investing in more ventures (Wilson & Testoni, 2014). Nevertheless, trust building between the entrepreneur and the crowd becomes imperative. Another common issue, in particular related to the behavior of the funders is the free-rider problem. A lot of investors tend to simply wait and see what others do. Related to this issue, a lot of investors tend to trust the ‘wisdom of the crowd’, which at the end can translate in foolish investment decisions that a single investor would not have taken on his own (Hornuf & Schwienbacher (2014a). Agrawal et al. (2013) argue thus that reputation signaling, rules and regulations and crowd due diligence are necessary to the reduction of information asymmetry and moral hazard, and prevention of market failure. It can even be said (Ahlers et al., 2012) some of these elements determine the success factor of a given venture. Dealing with financial roadmaps (e.g. exit strategy per-planned in the contract), risk factors (e.g. amount of equity offered by the entrepreneur) and internal governance (e.g. board structure) may enhance value creation of the firm. For the entrepreneur additional disadvantages may raise: limited capacity for raising money, the loss of confidentiality as the idea gets publicly shared and the time and effort that is required to promote the idea (Manchandra & Marulidharan, 2014)

And so, it can be argued (e.g. Manchandra & Marulidharan, 2014; Hornuf & Schwienbacher, 2014a; Wilson & Testoni, 2014) that equity crowdfunding can have its place between other equity financing methods. It can even be argued that equity crowdfunding complements the financing market, as it takes its place between financing via angel investors and venture capitalists (Hornuf & Schwienbacher, 2014a). On one hand, funding gaps at the lower end of the market can be filled. On the other hand, it creates the possibility for co-investment with professional investors. For example, crowdinvesting complements venture capitalists by maintaining a suitable control process over the valuation of the firms held by the venture capitalists (Manchandra & Marulidharan, 2014). Nevertheless, crowdinvestors may also compete as a substitute with business angels since average funding volumes can be similar (Hornuf & Schwienbacher, 2014a).

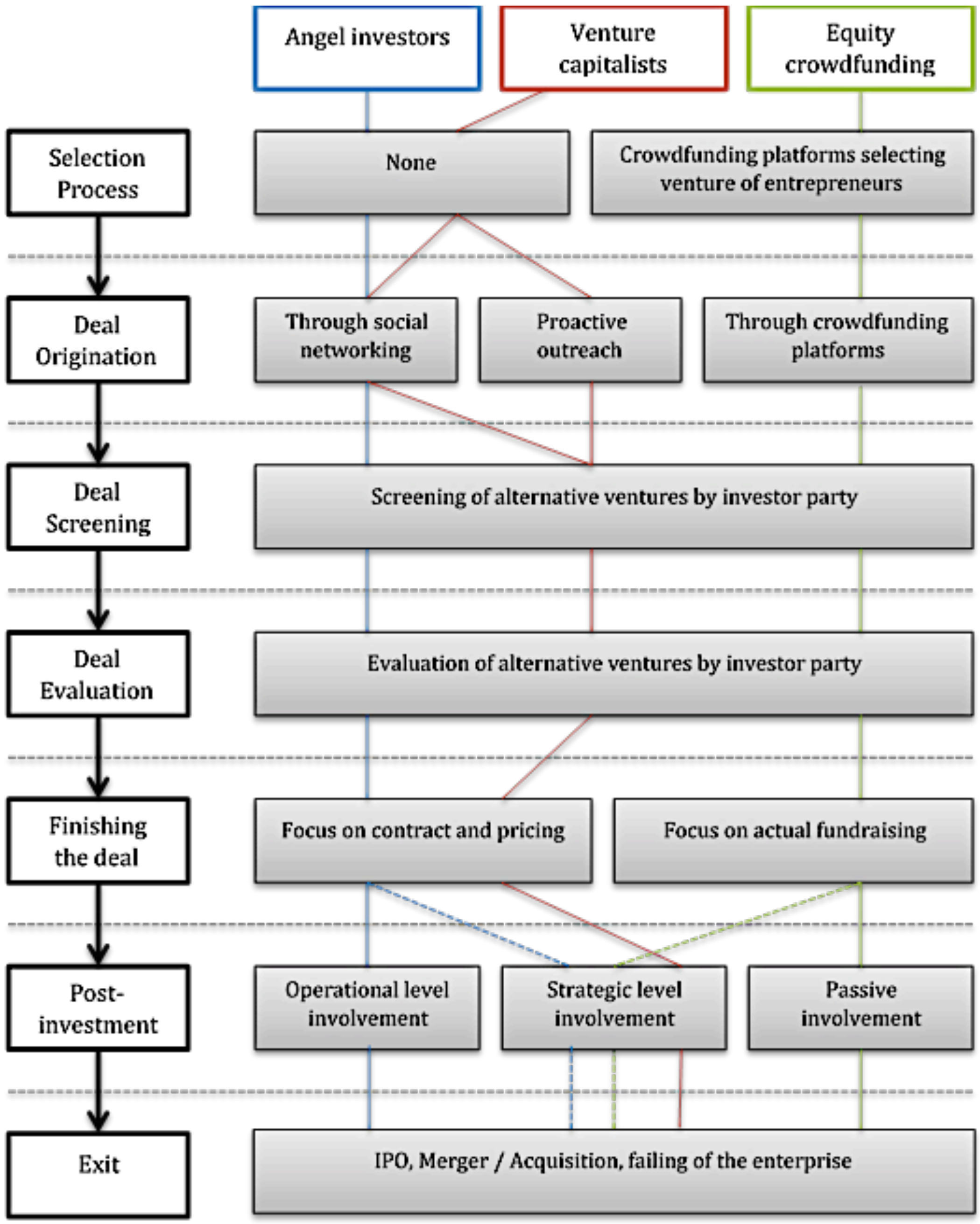
Positioning Equity Crowdfunding

This section will bring together the four previously described equity financing methods. As a result, a comparison of the four types will be constructed and a clear view on the differences and similarities between them will rise. The comparison of the different methods will be done on several levels: the key characteristics of equity financing (including main and financial characteristics, and a risk section), investor characteristics, entrepreneur characteristics and contracting.

Before getting to this, a comparison of the typical procedure steps is performed, which is shown in **figure 2.1**. The family and friends method is not incorporated in this figure, as the typical procedures of this method is not defined, nor does literature indicate that specific steps in this form of financing are actually performed. In this figure, the dotted lines suggest alterative pathways of the typical process. These pathways, however, are less likely to happen. The figure shows how different the process of equity crowdfunding is from the conventional financing methods. This has to with the equity crowdfunding platforms driving this kind of financing. They get involved in all the steps as they are hosting the possibility for investment. However, we can still say that all steps that are completed with venture capital or angel investors remain the same. The way these steps are filled in changes.

Following sections will now go into detail about the comparison of the four financing methods. In every section the reader will be presented with a written summary of the differences and a more detailed table of individual features. These tables are based on all the information derived from previous sections on family and friend, angel investors, venture capitalists, and equity crowdfunding.

Figure 2-1 Comparison of the typical procedure steps of angel investors, venture capitalists and equity crowdfunding



Note: Content based on Collins & Pierrakis (2012), Tyebjee and Bruno (1984) and Mason (2006).

Key characteristics of investment

The comparison between the financing methods will start on a more global level with some key characteristics of investment. This includes main characteristics, financial characteristics, risks, and differences and similarities on firm growth and the overall importance of the market.

Main characteristics

The informal equity financing methods (family and friend, and angel investors) tend to take on mainly local ventures compared to the formal financing methods (venture capitalists and equity crowdfunding), where the geographic activity gets much broader. Venture capitalist prefer investing in secure and innovative startups, which are in a more developed stage of their existence. The other methods may take on more uncertainty and invest in rather early-stage start-up ventures. A detailed comparison is given in **table 2.1**.

Table 2-1 Comparison of main investment characteristics between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Individual investors or partnership	Individual	Individual, (sometimes angel groups)	Partnership	Individuals investing together
Third party	None	None	None	Equity crowdfunding platforms
Social link: entrepreneur vs. investors	Informal band; extremely close, provide refuge	Informal and formal band; depending on AI	Formal band	Formal band
Financing Stage	Seed stage	Seed, early stage	More later stage; also sometimes seed stage	Seed, early stage
Type of industry / firms where financing method occurs	All kinds of firms	Small- or medium-sized, private, innovative, technological firms; AI often familiar with industry	Innovative, technology-based, start-up firms	At first: creative industries; trend: all types of young and innovative firms

Geographic activity	Extremely local	Heterogeneous, localized	Regional, national (and international via partners)	Global

Financial characteristics

Venture capitalists provide the largest amount of money, using accumulated capital. The other financing methods invest their own money, which limits their investment for a great deal, depending on the level of uncertainty they percept. Success seems most likely achieved via venture capital. In other cases the process for a positive outcome for investors may be long and rare. A detailed comparison is given in **table 2.2**.

Table 2-2 Comparison of financial characteristics between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	**Angel investors**	**Venture capitalists**	**Equity crowdfunding**
Monetary approach	Own money	Own money	Accumulated capital	Own money
Amount invested	Disproportional, yet limited	\$25.000 - \$ 1 million, still limited; between F&F and VC, depending on level of uncertainty; staged	Typically, twice the amount that angels tend to provide, around \$3 to \$5 million or more, staged	(Very) small amounts per individual investor; \$113-\$282 or smaller / larger; target amount set up by the entrepreneur (accompanied by a time limit)
Success for positive payout / exit	Undefined	Via long and rare process	LT: only likely in 5 – 10 years ST: unlikely and illiquid	Via long and rare process

Risk

Risk management and due diligence of family and friends financing and equity crowdfunding depends strongly on trust-worthy relationships between the entrepreneur and the investors. Angel investors and venture capitalists typically have a set of protection mechanisms. In case of venture capitalists this tends to be even more extensive. A detailed comparison is given in **table 2.3**.

Table 2-3 Comparison of risk between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Risk management by investors: avoiding moral hazard and uncertainty	Depending on attitude of F&F; trust-based	Amount of funding (staged), syndication, geographic proximity	Mainly syndication & contracting, staged financing	Overall little protection against fraud and bankruptcy; syndication might appear; trust-based
Due diligence	Based on trust	Performed on regular basis; based on own experience	Performed extensively by VC firm, in particular decision-making criteria and financial ratio analysis; in some cases by outside firms	In some cases by equity platforms (screening and evaluation); in other cases by crowd via discussion forums; In general little opportunity / incentive to perform this

Firm growth and overall importance

Growth of a firm is mostly encouraged in the case of angel investors and venture capitalists. Respectively, relative and significant fast growth is achieved in these financing methods. Data on equity crowdfunding is yet to be found. However, the most important sources for entrepreneurs seem to be family and friend and angel investors. The share that equity crowdfunding is taking on simply to small. A detailed comparison is given in **table 2.4**.

Table 2-4 Comparison of firm growth and overall importance between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Firm growth	Constrained	Relative fast growth	Significant fast growth	Undefined
Overall importance of market	High	High and often preferred by entrepreneurs	Medium	Small

Investor characteristics

Typically family and friends and crowd investors tend to be less experienced than angel investors and venture capitalists. However, they all want to provide themselves with financial gain of some sorts. Family and friends, angel investors and equity crowdfunding investors may have additional incentives, of social and emotional kind, to invest in certain ventures. Each of the financing methods provides additional direct or indirect value to the firm. A detailed comparison is given in **table 2.5**.

Table 2-5 Comparison of investor characteristics between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Profile	Undefined	High net-worth, wealthy, experienced, qualified, educated, background, risk taking; former entrepreneurs	Collaboration of institutional partners, different types: risk averse and evaluation-based, easy bail-out options first, only national, all options open; often financial or consulting background	Lack financial sophistication, experience, wealth; many different backgrounds

Drivers	Often social convention and support; constructing family business	Financial gain important (20% IRR); altruism (helping); pleasure	High financial gain (IRR a.s.a.p.) is critical	Financial gain (Revenue, profit share arrangements when company does well), early access to opportunities and products, participation in community, altruism, formalized contracts
Non-financial value to the firm	Labor, networking	Time, expertise, skills, knowledge, operations, networking	Extensive follow-up, periodically monitoring, skills, networking, managerial value reputation signaling, quality employees, customers, joint ventures	Create brand awareness among public, marketing tool, test and prove idea, feedback (also equity crowdfunding as a whole contributes to job creation & economic growth)

Entrepreneurial characteristics

A large set of prerequisites is required for the entrepreneur when seeking venture capital financing. In case of angel investors a business plan (and a management team) will do in many cases. In both cases the choice of the entrepreneur to choose one of them is driven by the investors being supportive and experienced. In the case of family and friends financing the incentive is more related to selfishness and risk aversion, and in the case of equity crowdfunding the incentive is more a lower cost of capital one. Each of the financing method seems to have their drawbacks given an entrepreneurial perspective. A detailed comparison is given in **table 2.6**.

Table 2-6 Comparison of entrepreneurial characteristics between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Necessary prerequisites	Strong social bands	Business plan, in some cases a management team	High level entrepreneur (qualified, experienced, personality, staying power, risk reacting…) or presence of and ability to lead a management team; innovative business plan	Little or none (in fact the entrepreneur himself might be incompetent)
Entrepreneurial behavior	Driven by risk averse, selfish motives	Driven by supportive, experienced investors	Driven by supportive, experienced investors	Driven by lower cost of capital
Possible negative consequences / drawbacks	Time-consuming, intensively involved, over-visiting, request money back, lawsuit, loss of friends/family	In some cases: give a seat in board, voting rights, preferred shares, loss of decision power, selling company soon (public)	Loss main control, give up 50% shares, high level auditing & control, time-consuming	Exposure of business idea, low property protection, non-helping investors, challenging follow-up capital, limited amount capital, time-consuming promotion

Contracting

Contracts via venture capital finance are the most complex and professional ones. The standardized contract of equity crowdfunding commonly contains pro-rate shares in the form of convertible bonds, participation notes and cooperative certificates. The other financing forms tend to use preferred shares, although angel investors will also work with common bonds. A detailed comparison is given in **table 2.7**.

Table 2-7 Comparison of contracting between family and friends, angel investors, venture capitalists, and equity crowdfunding.

	Family and friends	Angel investors	Venture capitalists	Equity crowdfunding
Type shares	Preferred shares	Common shares (Preferred shares)	(Convertible) preferred shares, negative covenants	Pro-rata share; mostly via participation notes, cooperative certificates, convertible bonds; common share in less extend
Characteristics of contract	Undefined	Anti-dilution provision, exit rights, liquidation preferences (higher priority)	Exit strategy, staged financing, board seats	Standardized (provided by platforms), overall little rights for investors
Complexity	Unprofessional	Rational design, but trend of professional behavior	Professional	Standardized for public

Interrelation between financing methods

In addition to this it can be argued that all described forms of equity finance mostly complement each other on the financing market. Indeed, formal and informal financing techniques complement each other through the large set of differences between them. Also, equity crowdfunding provides a complementary channel, by exploiting the full potential of the Internet (Wilson & Testoni, 2014). Next to this complementary essence of the financing forms, it can be said that these different forms tend to merge and overlap with each other. For example, Ibrahim (2008) points out that a certain set of angel investors are becoming more and more professional in their actions, especially in the case of their contract designs. Thereby their resemblance tends to be closer with venture capitalists than with the traditional angel investors. Another example is found in the case of equity crowdfunding. This type of financing typically takes its place between angel investors and venture capitalists, yet on both ends convergence between the parties may be perceived. Of course, when merging activities take place, the complementary approach can switch in some cases to a substitution one. Indeed, angel investors and crowdfunding, or angel investing and venture capital, may then be competing with each other on a market share level.

Chapter 3 - Study on Equity Crowdfunding Platforms

In chapter two of this paper a comparison between four alternative equity financing methods is performed, based on existing literature. Through this comparison it has become clear that equity crowdfunding is substantially less studied than the other three financing methods. This, of course, has to do with the recent nature of the matter. Therefor, in what follows, a study will be introduced, which contributes to solving this issue. Not only will it contribute to improving the knowledge about equity crowdfunding, this study will go one step further. At this point, entrepreneurs are being confronted with mainly these four different equity financing methods, yet no study supports the entrepreneur in some way when he is confronted with the equity financing method in particular. In addition, a lot of questions that the entrepreneur has on equity crowdfunding platforms remain unclear. Therefor, this study will focus on equity crowdfunding and on its platforms. A study on a sample (twenty) of these platforms will give insight about the working of this financing method and will point out important factors that an entrepreneur should consider, when choosing equity crowdfunding as their equity financing method.

This chapter includes an explication on the selection of the equity crowdfunding platforms, the variables or questions to consider in this study, an elaboration on the method of data/information collection, and the results of this study.

Selection of the Equity Crowdfunding Platforms

The obvious first step in the study of equity crowdfunding platforms (ECPs) is the selection of these platforms. Although equity crowdfunding is a recent given, the phenomenon is already a global matter. Western economies, including the United Kingdom, The Netherlands and France, are considered early movers in the adoption of equity crowdfunding, providing laws and regulations to support equity crowdfunding since around 2010 (Estrin & Khavul, 2016). The UK can additionally be considered as a leader in fostering new technologies to support entrepreneurs in raising capital. The United States followed in 2012, but legal matters, including the JOBS (Jumpstart Our business Start-ups) ACT, lost support of the government, only to be reinstated in 2015.

Because of the international presence of equity crowdfunding it seemed only fair to include platforms from all over the world, to clearly capture the differences between countries in the handling and the procedures of these platforms. From all available platforms only the most popular once were selected. A platform was considered popular if it often appeared in the relevant academic literature or if it was presented as a 'top equity crowdfunding platform' on a given website. Top search results in web browsers were additionally considered as an indication of the popularity of a platform. From this list of ECPs a purposive sample of twenty platforms was deducted. In this deduction special attention was given to fair representation of both European and American countries. Reason for this is to also clearly capture the differences in procedures, regulations and laws. Concerning the European countries, the presence of the UK as leader was also considered as a factor. On the basis of theoretical saturation an amount of twenty ECPs was considered sufficient.

This process resulted in the selection of the following equity crowdfunding platforms:

- CrowdCube (UK)
- BankToTheFuture (UK)
- Syndicateroom (UK)
- Seedrs (UK)
- Companisto (Germany)

- Seedmatch (Germany)
- Symbid (The Netherlands)
- MyMicroInvest (Belgium)
- WiSeed (France)
- Invesdor (Finland)
- FundedByMe (Sweden)
- StartUpValley (USA)
- Angellist (USA)
- CircleUp (USA)
- Fundable (USA)
- Crowdfunder (USA)
- EquityNet (USA)
- Wefunder (USA)
- Localstake (USA)
- Seedinvest (USA)

The consideration that these are popular equity crowdfunding platform is also resembled in the amount of capital that already has been raised by them (April, 2016). On average, American platforms assembled around $174.000.000. Platforms from the UK rose around $126.000.000 and other European platforms around $121.000.000 on average.

Variables to consider in the study

The goal of this paper, in addition to positioning equity crowdfunding next to the other main forms of equity financing, is clear: this paper aims to capture the experience that entrepreneurs might have with equity crowdfunding platforms. The overall process of equity crowdfunding is well defined and information is fully available to the entrepreneur, yet a lot of elements that might be crucial to future entrepreneurs seem to disappear on the background. Nevertheless these might be extremely relevant and an entrepreneur ought to know about these before entering the path of equity crowdfunding. In most cases these elements were not displayed on the main web pages of the ECPs' websites. Main topics and elements of interest in this paper are presented below. These topics are more or less ordered by the steps in the funding process.

(1) Concerning general information about the equity crowdfunding platform: does any institution authorize the platform? How is interaction with investors facilitated on the platform? What are the fees applicable to their services or the use of the platform? What services do they offer? What type of contract with this platform is being arranged, covering rights and duties? What are the general procedures / steps in the equity crowdfunding process? How does the platform handle slow-downs in the process or complications? Are there any relevant legal / juridical elements playing a role?

(2) Concerning the application from the entrepreneur / company to the platform: What are the conditions for application? Is application a national or global given on that platform? What are the investment terms? How is investment being facilitated? Who decides on how much equity to offer? Is there any vetting performed by the platform (due diligence) and how does this work?

(3) Concerning the project pitch: what pitch essentials are asked for by the platform? Can only accredited investors fund a project? What kind of interaction between investors and entrepreneurs is established? How much support does the platform provide?

(4) Concerning the closing of the funding: what is the funding window? Is there an all-or-nothing formula applicable? Is there any second stage vetting? How does the completion process generally look like? Is overfunding an option?

(5) Concerning post-investment: what type of shares do investors get? What right do they (not) have with these shares (pre-emptive, voting…)? Does the platform come up as a nominee for the investors? Are investors represented in the board of directors in some way? Is follow-on capital an option? What are the post-investment general steps? What type of interaction with investors needs to be maintained in the future and how is this facilitated? Is a potential exit strategy already co-determined by the platform?

Method for information collection

All platforms were studied and analyzed in different ways. Main information was generally found on the website itself. A lot of information was retrieved via the Q&A sections provided by most of the websites. In addition to this the 'terms of use' were often consulted when information could not be deducted from the website directly or when information provided seemed rather vague.

Given the variables of interest al platforms were searched extensively; seeking answers to all the questions posed in previous section. The result of this was the generation of information on each of these questions for each of the platforms.

Additionally three interviews (see **appendix A, B and C**) were conducted as a source of additional and practical information. The goal of these interviews was to support the information retrieved from the platforms. The interviewed parties were all part of a successful entrepreneurial start-up company. All companies used an equity crowdfunding platform to raise funds. These start-ups are:

- Domobios
- Only Once
- Opinum

Following section aims to structure and present all this generated information in such a way that a future entrepreneur, be it American or European, has a clear vision of what to expect when financing their venture via equity crowdfunding platforms.

Results of the study

The results of this study on equity crowdfunding platforms will be presented in different sections. These results are aimed at the interest that entrepreneurs might have on the different topics. Firstly, financial considerations for the entrepreneur will be discussed. Next, the pitch drivers will be analyzed. A pitch is a launch of a project to the general public, also the potential investors. This section will thus tell the entrepreneur what to expect from this pitching. Then, a section will be devoted to vetting and due diligence. Here, a model will be introduced that captures all vetting and due diligence flows. The difference between these two kinds of flows will also become clear. This will give the entrepreneur insights in who is screening whom. Hereby entrepreneurs will also know how investors or platforms are potentially screening themselves. Fourthly, the results will elaborate more on the equity crowdfunding process; clarifying each individual step for the entrepreneur. Next, investor interaction will be discussed. This section aims at verifying which kind of interaction is expected between the crowd investors and the entrepreneurs. Then, another section is focusing on the interaction between the entrepreneur and the platform itself. This will show the amount of support that an entrepreneur can expect from the platforms. The final section is dedicated to some legal consideration that an entrepreneur should know of when dealing with equity crowdfunding.

Financial Considerations

This section of financial considerations includes potential fees that entrepreneur have to pay to the ECPs, the dilemma on who is in charge of determining the amount of equity offered, the possibility of follow-on capital and overfunding for a given venture, and the all-or-nothing formula, a condition that may or may not be present in order to complete a project.

Fees

First let us examine the fees that entrepreneurs could expect when raising funds via an equity crowdfunding platform. It is clear that there is no standardized pricing applicable to all the platforms: every platform has a unique pricing system, including or not including a success fee, a registration fee, an administration fee, a legal fee, a setup or listing fee, and so on. In most cases however, registration to a platform is free, as this is not a requirement for your project to get selected for funding. Symbid, however, does asks for a €350 registration fee. It is notable how the amount of pricing corresponds to the support given to the entrepreneur in the funding process, both in the USA as in European countries.

In America some platforms arrange pricing via monthly subscriptions. This is, for example, the case for Fundable, Crowdfunder, EquityNet and Localstake. This kind of structure is not present on European platforms. Based on amount of pricing per month, additional services will be provided by the platforms. For example, Fundable is asking merely $179/month, yet their service only includes the creation and overall management of the entrepreneur's project. Localstake on the other hand offers a lot more services based on the progress of the project: they ask for $199/month during the first phase where the investor market is evaluated, $499/month during the raising of the funds, and $49/month for growing the business after realization of the funding target.

Other American platforms, like StartUpValley and CircleUp, prefer to use only a success fee, which varies around 5% on the total amount raised. This success fee only needs to be paid by the entrepreneur when the funding target is reached. CircleUp calculates their success fee based on what companies would pay a bank for investing in their company. Seedinvest seems to be the only platform asking for a placement fee, instead of a success fee. This would mean that a even though the project may not be a success, the company would have to pay 7,5% on the total amount asked. In addition to this Seedinvest also asks $4.000 for due diligence, escrow management, marketing and legal expenses.

European countries mostly handle by a success fee, ranging between 4% and 12,5%, combined with some additional charges for listing the project, administration or legal expenses. An administration fee commonly includes the issue of digital share certificates and communication with investors, while the legal fee is based on the adoption of the standard articles of association and other forms of assistance with documentation. These fees can also be in the form of monthly payments, like in case with Symbid. Crowdcube, FundedByMe, Invesdor, BankToTheFuture, Seedmatch, Symbid and Syndicateroom.

Important to see for the entrepreneur is that some platforms might ask for additional payments. BankToTheFuture, for example, asks for an addition percentage fee when the company is sold. Syndicateroom asks for £150/month after the money is raised for the management of a nominee structure (see later). And Crowdcube asks for additional money when the entrepreneur relies on their equity services, like financial forecasting.

Like in America some platforms, in this case MyMicroInvest and Seedrs, fully rely on one single success fee, without any other charges. In contrast with the American platforms, however, the percentage is higher and the support given to the entrepreneur is as well.

The French ECP WiSeed presents a special kind of structure. Their pricing is based on the sum of a fixed honorariums scheme and additional administration costs.

This overview of pricing and fees of the ECP's should help to see the entrepreneur that there is a huge range of options and that every platform has its own unique pricing structure. It is up to the entrepreneur to select the right platform, keeping in mind that the higher the fees asked by the platform, the more support will be provided throughout the funding process.

Decision on how much equity to offer

The decision on how much equity to offer is always up to the entrepreneur, independent from which country you are from. However, different platforms are supporting the entrepreneur in making this decision. Platforms that are offering this collaboration include Crowdcube, WiSeed, Localstake and Companisto. Other platforms, like Crowdfunder and FundedByMe, are supporting the entrepreneur in a more indirect way by providing them with an interesting learning section on their website. This section then is filled with the essential information needed to decide upon the amount of equity offered and the (pre)-valuation of a company.

In some cases the ECP encourages the entrepreneur to work together with one or more experienced investors, which are then also backing the project. This is the case for Wefunder, Seedinvest, Syndicateroom and MyMicroInvest. M Turcksin, from Opinum, worked together with MyMicroInvest and told his experience. Indeed, the amount of equity offered to the crowd investors was not only a decision by the entrepreneur, but there was a negotiation period with the relevant investors (M. Turcksin, personal communication, May 3, 2016). In the case of MyMicroInvest this investor is Inventures, the company owning MMI. It was even the case that Inventures would only invest in Opinum if part of the capital were raised via their crowdfunding platform. In that aspect, for Opinum, it was not really a choice to use an equity crowdfunding platform.

In all other cases the decision is fully the responsibility of the entrepreneur. The entrepreneur can however still decide to be supported by an independent third party financial advisor. The start-up company Only Once is a good example on carrying this responsibility about the equity offered. Symbid offered a valuation scale tool to determine the valuation of their company (R. Peels, personal communication, April 23, 2016). However, the CEO, Roel Peels, and the CFO of the company felt that they were experienced and mature enough to make this decision themselves. Therefor, they did not follow the valuation method of Symbid, but proposed their own valuation of the company, along with the equity offered.

Important to know is that the amount of equity offered cannot always be changed during the funding process. In the case of Crowdcube and Symbid, for example, this change is still possible, but in the case of MyMicroInvest it is not.

Follow-on capital

On most platforms, follow-on capital is not being supported directly. This brings along some important disadvantages. R. Peels (personal communication, April 23, 2016) points out some important disadvantages of platforms not supporting follow-up capital rounds. First of all, every new round means the creation of a new project. This means that all documentation and information needs to be uploaded yet again. The second issue comes up when you would like to contact your crowd investors. In staid of just sending one mail to all investors (over all rounds), you will have to send one mail per project/ round. The platform thus actually is not aware of the total amount of investment that is already backing an entrepreneur's project and is not able to provide the entrepreneur with one single list with all crowd investors.

Only in few cases, like in the case of CircleUp or Seedrs, the software of the platform is supporting follow-on capital. An important consideration here, is being clearly mentioned by Seedrs: the company should be aware of the pre-emption rights that were or were not given to the entrepreneurs of the first funding round, as issuing new shares to new investors might of course leave these first investors diluted.

Overfunding

Overfunding is generally possible on the ECPs. Some platforms, like Seedinvest, Seedrs, Syndicateroom, Symbid and Crowdcube, clearly indicate this possibility. It may not seem that surprising that the platforms are supporting overfunding of a project. Generally, the more funding a company captures, the higher their share will be based on the success-fee pricing method. Often, e.g. Seedinvest and Invesdor, it is up to the entrepreneur to decide upon accepting overfunding or not. It is not surprising that the entrepreneur should have the final vote on this issue, as overfunding means that more shares will need to be issued, which will then again have an impact on the valuation of the company. In this study only Wefunder did not support the possibility of overfunding. When overfunding would be the case, priority would be given to one investor over the other one.

All or nothing

The all or nothing formula in equity crowdfunding indicates that the funding amount that is set at the start of the funding process needs to be funded by at least 100%. If this is the case, at the end of the funding period, the total amount, excluding a possible success fee, will be transferred to the entrepreneur. If this is not the case, investors will be returned their full investment individually.

It is clear that on most platforms this formula is present. However, both in America as in European countries exceptions are present. EquityNet allows entrepreneurs to go through with the funding amount that is reached at the end of the funding window. BankToTheFuture, FundedByMe, and Crowdfunder are taking on a more subtle and intermediate path. In these cases a solution will be build. Full support by all three parties, the investors, the platform and the entrepreneur, will be needed.

All platforms are using a third-party escrow company to keep a funding account where all investments are being assembled and kept during the funding process.

Pitch Drivers

This section on pitch drivers actually contains two main elements. First, the pitch essentials will be discussed. Secondly, this section will elaborate on the pitch window. In sum, this section will tell the entrepreneur what to expect from this pitching their project to investors.

Pitch Essentials

The pitch essentials include all forms of information that the entrepreneur provides to the investors via the equity crowdfunding platform. These essentials ought to capture the attention of the investors and convince them to invest in the project of the entrepreneur. Every platform is putting other pitch essentials in front. Nevertheless, it seems that some pitch essentials are needed, independently from the ECP you are using as an entrepreneur.

All platforms seem to be requesting at least a business plan and a financial forecast. Story telling is another pitch essential that all platforms are sharing. R. Peels, CEO of Only Once, agrees to this (personal communication, April 23, 2016). He states that a crowdfunding project is an opportunity to tell your story to the world via a marketing campaign. Each platform is also using a pitch deck where a summary of the entrepreneur’s project is given. Therefore, the entrepreneur should be able to capture the essence of their project into some kind of summary, including also the valuation of the company and the equity offered. Based on this, the investors should be able to make an investment decision, as the goal is to provide them with enough evidence of the strength of the project. Another pith essential that a lot of international platforms share is some kind of visual representation of the company, in the form of a video, pictures, or PowerPoint slides. Seedinvest, WiSeed, Crowdcube, Seedrs, Symbid and MyMicroInvest are amongst those platforms that are expecting a high quality video. BankToTheFuture, WiSeed and Invesdor, for example, are also requesting an investor presentation.

On European platforms one pitch essential is emerging, which is not (yet) or less relevant on American platforms: a team. Syndicateroom, MyMicroInvest, FundedByMe and Companisto are clearly indicating that the company team needs to be presented in the pitch deck. None of the American platforms are requesting this representation of the team.

Like I mentioned before, each platform has slightly other expectations of the pitch deck and thus can have a different focus. Crowdcube and FundedByMe, for example, are clearly focusing on the marketing of the project, as they are additionally asking for a marketing and a list of upcoming events. Crowdcube even stimulates the entrepreneur to consider other kind of rewards towards investors. BankToTheFuture and Fundable, on the other hand, are focusing more on the legal side of the picture by asking for clear communication towards investors about the investor terms, articles of association and shareholders agreements.

In addition to all these pitch elements the entrepreneur is often stimulated to add additional relevant information like property rights, designs, memorandums, market information, KPI’s and other closing documentation.

In any case, the entrepreneur should make sure that his product adds value to the lives of people. Therefor, the product or service itself may not be forgotten as a pitch essential (R. Peels, personal communication, April 23, 2016). Having an attractive product simply makes the raise of capital less of a hurdle.

Pitch Window

The pitch window or funding window determines the period in which the entrepreneur can raise capital. The determination of the pitch window is of course an important factor for the entrepreneur. Eventually it could determine the success of a project. In most cases, if a company is unable to raise the target funds in time, none of the funds will be transferred and all investments will be returned to the investors.

In most cases this length is predetermined and unchangeable. This seems to be especially the case on the European platforms, which are stating a standard duration of a funding campaign. This standard duration varies between 30 days, like in the case of CrowdCube, and three months, like in the case of WiSeed and MyMicroInvest.

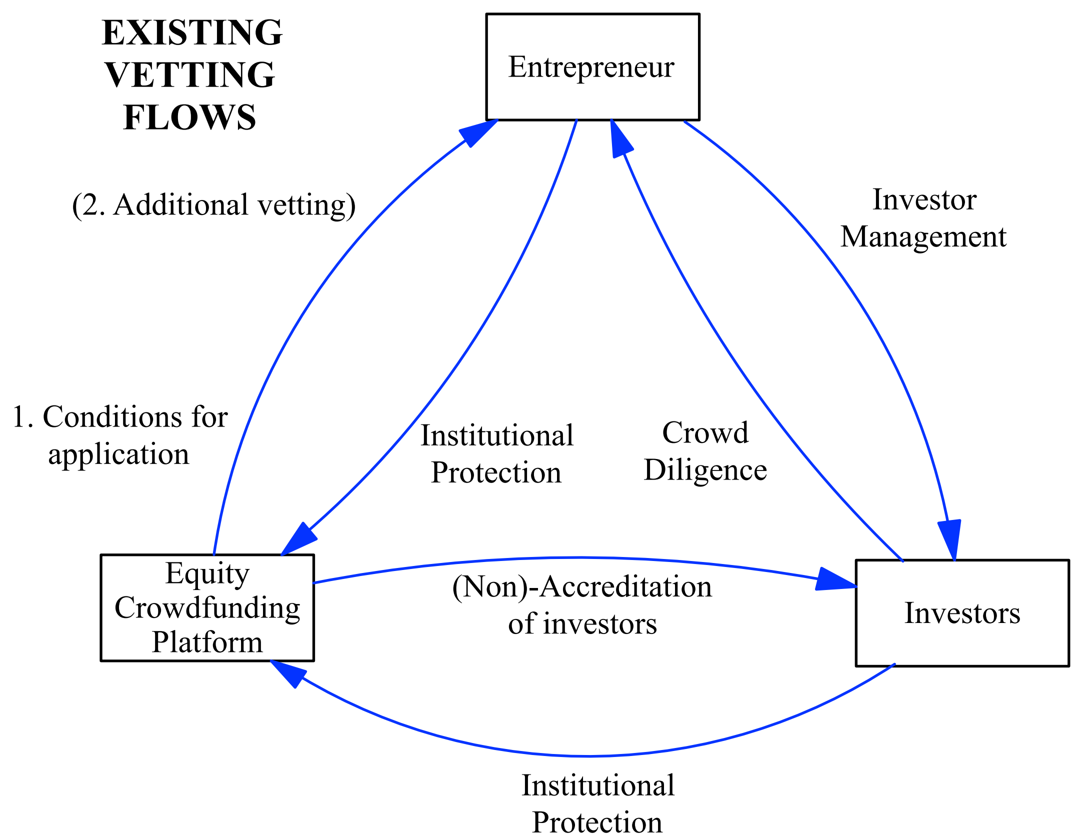
In other cases, especially on American platforms, the duration of the pitch window is negotiable or flexible. EquityNet, Localstake, Fundable and Seedinvest, for example, are stating that the funding window will be determined in negotiation with the entrepreneur. Crowdfunder and CircleUp are proposing an interval of two to three months and respectively 60 to 90 days. The final decision of the exact duration will then again be in negotiation with the entrepreneur.

Vetting and Due Diligence

Equity crowdfunding entails three parties: the entrepreneur (company), the investors (crowd) and the equity crowdfunding platform. An important an interesting issue in crowdfunding is how these parties are performing due diligence on or vetting each other. As mentioned before, due diligence refers to the performance of an (extensive) investigation of a certain person or company. The term due diligence is mostly used in the context of investors going trough the process of researching a potential investment (Investopedia, 2016a). A more global term can be used to describe how the three parties are reviewing each other: vetting. Collins English Dictionary (2016) defines vetting as “the act of making a prior examination and critical appraisal of a person, document, scheme, etc.”. In following sections vetting between the entrepreneurs, the investors and the platform will be described in greater detail.

These sections will elaborate on a model of all existing vetting flows in the equity crowdfunding process (**figure 3.1**). The entrepreneur performs vetting, in the form of investor management, on the investors (the crowd). In some cases the entrepreneur might even accept or deny investors himself. The investors on their turn are investing in these projects that seem to have the most potential. Therefor, they are performing some crowd diligence, as collectively this decision is also made. Investors and entrepreneurs want to have enough protection against potential misuses of the equity crowdfunding platforms. They are seeking this protection that via third party institutions. Of course, the platforms themselves need to make sure that they are dealing with proper entrepreneurs and investors. Vetting on the entrepreneur generally can be done via two steps, where the first one lays in the conditions for application and the second one is a variable kind of additional vetting. Vetting the investors is generally done via accrediting of the investors, which could of course also be relevant for the entrepreneurs.

Figure 3-1 Vetting flows present in equity crowdfunding.



The equity crowdfunding platform vetting the entrepreneur

This section will show how ECPs are vetting the entrepreneur. This will give entrepreneurs a view on what to look out for and what to expect. Vetting of platforms mainly consists of two parts, in which the second one is optional: basic conditions for application and additional vetting.

Conditions for application

Conditions to apply for equity crowdfunding are largely depending on the type of platforms we are dealing with and where this platform is located. First of all, it is clear that there is a different approach from platform as to which types of industries they are focusing on. This will then of course influence the fact if an entrepreneur can apply or not. **Table 3.1** shows all the studied platforms, along with their location and the industry they are focusing on. The table shows that American platforms seem to be more precise in what applications they would like to receive from entrepreneurs. Entrepreneur will be more restricted in the sence that most platforms clearly state which industries they will accept or not. In Europe it seems that this restriction is subtler. Most of the platforms are allowing all types of industries in the application for funding.

Table 3-1 Industries that international equity crowdfunding platforms are focusing on.

ECP	Location	Industry
StartUpValley (1)	USA	Technology
Angellist (2)	USA	Technology
CircleUp (3)	USA	Customer products & Retail
Fundable (4)	USA	All
Crowdfunder (5)	USA	Technology, Social, Film & Entertainment
EquityNet (6)	USA	Any type of private business
Wefunder (7)	USA	All
Localstake (8)	USA	All*
Seedinvest (9)	USA	All
CrowdCube (10)	UK	All**
BankToTheFuture (11)	UK	Finance
Seedrs (12)	UK	All
Syndicateroom (13)	UK	All
WiSeed (14)	FR	Health, environment, finance, industrial and services
Symbid (15)	NL	All
MyMicroInvest (16)	BE	All
Seedmatch (17)	GE	All
Invesdor (18)	FIN	All
FundedByMe (19)	SWE	All

Companisto (20)	GE	All

Note: (*) Except for biopharma, gambling, drugs, insurance, non-for-profit, politics and weapons. (**) Except for gambling, betting, e-cigarettes, sexual applications, filmmaking and property.

In general, R. Peels states that platforms that are allowing all kind of projects will not be that strict on accepting projects (R. Peels, personal communication, April 23, 2016). These projects are in fact their income. Symbid, for example, does not seem to be strict at all. There is no good selection procedure, simply because cannot afford this yet.

Of course, the type of industry is not the only condition for application of a project on an equity crowdfunding platform. Following **tables 3.2, 3.3 and 3.4** give an indication of all other elements platforms are (not) requiring of the entrepreneur's projects. These requirements are forming the basis for the platforms to accept or reject a given project. Note that the numbers (from 1 to 20) in these tables correspond to the numbers related to the platforms in **table 3.1**.

Table 3-2 Conditions for applications on American equity crowdfunding platforms.

Requirements/platform	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**
(Clarity of) vision and concept		X							
(Proven) customer traction/momentum		X					X		X
Fast growing market		X						X	X
Financial performance			X					X	
Large market		X							
Leading investor							X		
Management team			X						X
Series A or series B funding					X				
Technical founders		X							
Top marketing materials								X	
Working product							X		
No specific requirements	X			X		X			

Table 3-3 Conditions for applications on UK equity crowdfunding platforms.

Requirements/platform	**10**	**11**	**12**	**13**
(Clarity of) vision and concept	X		X	
(Proven) customer traction/momentum	X			
Ambitious exit strategy in mind	X	X		
Fast growing market	X		X	
Leading investor				X
Management team	X		X	
Valuation	X			
Working product		X		

Table 3-4 Conditions for applications on European (non-UK) equity crowdfunding platforms.

Requirements/platform	**14**	**15**	**16**	**17**	**18**	**19**	**20**
(Clarity of) vision and concept	X				X		X
(Proven) customer traction/momentum	X			X			
Fast growing market	X			X	X		X
Financial Performance					X		X
Innovative	X			X			
Management team				X	X		X
Quality			X				
Reliable			X				
Top marketing materials		X			X		
No specific requirements						X	

This study shows that some requirements for applying for equity crowdfunding are globally shared. An important requirement is the story-telling one. Project need to show a clear vision and concept, that not only captures the imagination, but can be perceived as a real need in people’s lives. That is why a lot of platforms also require having some proof of customer traction, showing that a momentum can be created around a product or service. A third common requirement is that the project should be connected to a fast growing market. Also, the management team can be a criterion for allowing a project. Other globally shared requirements are top marketing materials, financial performance, having a working product, and already having captured a leading investor. Of course, beside these requirements every platform is requesting the necessary documents, as mentioned before.

Interestingly, innovation is less perceived as a true criterion in contrast of what a lot of literature is saying. Merely two European platforms (non-UK) are indicating an innovative product as a condition for application. This point can be related to another interesting side-study. Before, based on literature, we have argued that equity crowdfunding is focusing on seed and early stage companies. But is this really the case in practice? Well, we can certainly say that the focus in on these type of start-ups. Some platforms, like StartUpValley, Crowdfunder and Seedinvest, are literally stating this. On other platforms it is simply visible by browsing through the projects that are being accepted. However, few platforms, including MyMicroInvest, Wefunder, and CircleUp, are also allowing grown companies to use equity crowdfunding for a certain project within the company. In any case, important to know for the entrepreneur, is that your company already needs to be legally created in almost all cases.

A last point in considering the conditions for application is the location of the company that applies for equity crowdfunding. In most cases, the company needs to be domiciled in the land of the equity crowdfunding platform. BankToTheFuture, Crowdfunder and EquityNet are exceptions on this rule; you literally can apply for a project form everywhere in the world. Invesdor is also an exception: they allow companies from the whole Nordic Region.

Additional vetting after application

The platform needs to make a selection of which projects to accept and which ones to reject. The first step in this decision-making is based upon the fulfillment of the conditions, mentioned in previous section. In most cases, a second vetting step is performed by the platform. In some cases, like in the case of Fundable and Symbid, the review of the application is the only vetting procedure. The second step can take on different shapes and forms:

- A simple background check via Internet (e.g. StartUpValley).
- Answering how fundable the project is (e.g. EquityNet).
- A full vetting procedure before any funds can be raised (e.g. CircleUp, Seedinvest, Companisto).
- Focusing on fraud prevention (e.g. Wefunder).
- Focusing on anti-money laundering (e.g. BankToTheFuture).
- Focusing on legal vetting procedure; form and structure of the company (e.g. Seedrs).
- Focusing on financial and legal information (e.g. MyMicroInvest).
- In form of an interview (e.g. Seedmatch).
- In collaboration with leading investors a hidden due diligence process is performed (e.g. Invesdor).

As a result, we can argue that some platforms are performing a lot of additional vetting, like Angellist, Seedinvest, MyMicroInvest and Companisto. This vetting procedure would then include legal and confirmatory evidences, organizational and structural checks, review of ownership and the team, study on the terms if agreement, review of the transaction documents, review of the investee committee, business and campaign review, contract negotiations, and so on. As a result of this strong vetting procedure only 1% of the application are allowed to pass to the funding stage, like in the case of Companisto and Angellist. Others platforms, like Crowdfunder, Fundable and Symbid, are not going trough all this additional vetting.

In two cases, MyMicroInvest and Invesdor, this step of the vetting is bounced back to the investors. Before raising funds, companies first need to get enough support by potential investors, without the need for investment. The platforms use this information then to see how much backing the project is getting and how appealing it would be to the general public. M. Turcksin, which has experience with MyMicroInvest, argues that it is indeed the investor party that is performing additional due diligence, in their case Inventures (M. Turcksin, personal communication, May 3, 2016). But he states that this is typical when the equity crowdfunding part is only a small part in the total capital raise amongst other investment parties. In this case, due diligence is outsourced to one of those parties. The platform merely becomes a marketing tool. Dorian Penninckx, business developer of Acar'Up (Domobios), also agrees upon this statement. He argues that beyond the financial tool, crowdfunding is a great marketing tool (D. Penninckx, personal communication, May 2, 2016). Nevertheless, MyMicroInvest can be very strict on which project to accept as they often invest too in those project via Inventures, their professional investment fund.

Investors vetting the entrepreneur

In those cases that not a lot of vetting of the entrepreneur is being performed by the equity crowdfunding platform, the investors (the crowd) are expected to do their own due diligence. Platforms that are clearly indicating this are StartUpValley, Wefunder, Seedinvest, Syndicateroom, MyMicroInvest and FundedByMe. Syndicateroom, for example, promotes this by having a specific Q&A section on their platform between investors and entrepreneurs to facilitate due diligence procedures.

In the case of MyMicroInvest and Invesdor, due diligence takes on a special form. Here a project first need to get enough backing by a group of known investors, before it is presented to the crowd.

An important question to ask is if the investors on the equity crowdfunding platforms are capable of conducting a proper due diligence procedure. It is reasonable to argue that due diligence by investors, in the context of equity crowdfunding, is not the same as due diligence preformed by venture capitalist, for example. Can we really still speak of due diligence? BankToTheFuture actually acknowledges this statement by indicating that investors must basically rely on the wisdom of the crowd, they therefor introduce the term Crowd Diligence.

Even if platforms are performing a great amount of vetting on the entrepreneur, investors still have full responsibility of their own investment. Every platform is clearly stating this in their terms of agreement.

And still, there is one other dimension that helps the investors in vetting the project and the entrepreneur: the fact that entrepreneurs need to already provide a lot of details on their company. R. Peels (personal communication, April 23, 2016) affirms that a platform, in their case Symbid, asks for a lot of information on the company. This gives investor a larger amount of certainty and transparency.

Platform vetting the investors

Investors need to register onto the ECP's. The question then of course remains on who can register as an investor. In Europe (non-UK) the rule seems to be fairly clear: everyone willing to invest can invest (except for, on some platforms, investors from the US). All these platforms are accepting both accredited and non-accredited investors. As a result, institutional investors are investing alongside the regular public. This however raises questions on the knowledge of these investors. R. Peels, CEO from Only Once, shares this concern (personal communication, April 23, 2016). He states that, on the Symbid platform, the general knowledge of investors is really poor. They notice this from the type of questions they were getting from these investors. Most of them are just looking at the video or the global idea. Symbid does not at all check the background of investors, so everyone can invest.

In the UK, the Financial Conduct Authority (FCA) is stating the profile of investors. The FCA (2015) argues that only those can invest who take regulated advice, those who qualify as high net worth or sophisticated investors, or those who confirm they will invest less then 10% of their net assets. Their rules also require checking whether investors understand the risks involved when they do not take regulated advice. Crowdcube, for example, is following the FCA rules. However, in many cases in the UK, investors are able to self-certify themselves. This means that, under less restricted rules; they can become a sophisticated or high net worth investor, which can invest in a firm that does not necessarily follow the FCA rules. Of course in this case, they will loose all the protection that the FCA could provide them. Seedrs and BankToTheFuture, for example, allow self-certification via their platform. As a result, in the UK investors are certainly more accredited as in other European, but their true capacity for performing due diligence can be questioned, as self-certification and firms not following the FCA rules remain present. Some UK platforms are having additional procedures to know the state of the investor: Syndicateroom is offering an additional form of certainty, as al investments need to be led by top investors, BankToTheFuture is performing a AML and customer due diligence procedure, and Seedrs is doing an extra check on each investor that is investing for the first time.

In America non-accredited investors will be allowed to invest in companies via equity crowdfunding. The Jumpstart Our Business Startups Act (JOBS-Act), title III, regulated by the

SEC will be effective May 16, 2016. This means that both accredited and non-accredited investors will invest together on future projects. Localstake, Seedinvest, Wefunder, EquityNet and StartUpValley are already anticipating upon the non-accredited investors. Accredited investors in USA include business angels, institutional investors (venture capitalists), and self-certified individuals. Some platform, like CircleUp, Fundable and Crowdfunder, were focusing on accredited investors, including venture capitalists and business angels. Fundable even performs a high level of vetting on their investors. The question remains if these platforms will keep their focus, as the entrance of non-accredited investors opens the doors to a lot more capital generation, and thus more potential profit for the platforms.

Entrepreneur vetting the investors

The fact of dealing with (self)-accredited or non-accredited investors could be of interest for the entrepreneur. It is up to the personal opinion of the entrepreneur to consider the positive and negative effects that regulations might have upon this selection. But in most cases, the entrepreneur will not do trough extra vetting towards investors (D. Penninckx, personal communication, May 2, 2016).

Nevertheless, in some cases the entrepreneur gets to control and manage the investors that are investing in his project. On Angellist, Crowdcube, BankToTheFuture and FundedByMe the entrepreneur has the choice to personally reject an investor. On other platforms, like on CircleUp, the entrepreneur does not have this power and investors get treated on the first-come-first-served principle.

Vetting the equity crowdfunding platforms

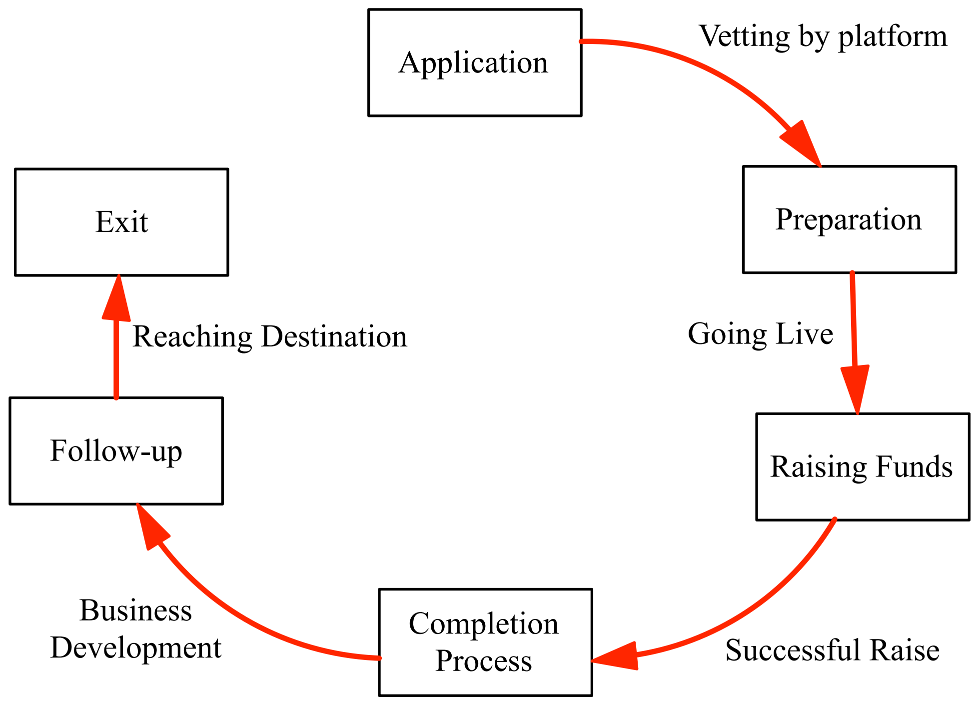
Platforms want to get the support of both entrepreneurs and investors. Thus, they need to earn the trust of both groups. On of the ways to do this is to register at an institution that protects the rights of all parties involved in equity crowdfunding. That is why most platforms appear to be authorized or registered by national institutions, like the FCA (UK), FINRA/SIPC (USA), FSA (Sweden), AFM (The Netherlands), and so on.

The Equity Crowdfunding Process

In chapter two we already compared the overall process of equity crowdfunding to the process of venture capitalist and business angels. In this section we will elaborate on the equity crowdfunding process. It is important for an entrepreneur to be prepared about what to expect in each step of the funding process. The following process and its drivers are derived from the procedures and steps throughout all the studied equity crowdfunding platforms. Important to note is that every platform goes trough the general flows of the process (figure 3.2), but every platform is dealing with a particular step differently. Therefor, all the following figures are a combination of all the possible elements that an entrepreneur could encounter in the equity crowdfunding process.

Figure 3.2 depicts the overall process of equity crowdfunding. The process takes of with the application of the entrepreneur to start raising funds on an ECP. This application is reviewed by the platform, as discussed in one of the previous sections. When all conditions are met, and perhaps additional vetting is performed, the entrepreneur can launch his campaign and start raising funds. When the raise is successful, the completion process of the raise can start. Note that a successful raise does not necessarily mean that the target amount is reached, as discussed before. The completion process is about finishing the deal by going trough the administration and communication towards investors (e.g. issuing of shares). When this task is finalized, the entrepreneur can start growing his business over the following years. A crucial step however is that the entrepreneur still needs to follow-up on his investors via regular updates. In most cases, the platform does not want to stay connected too long to the company. Thus, and exit strategy, that may already been formulated at the beginning of the funding process, will be developed. This then concludes the entrepreneurial adventure of raising funds via equity crowdfunding. In following section we will go deeper into detail on each of these steps.

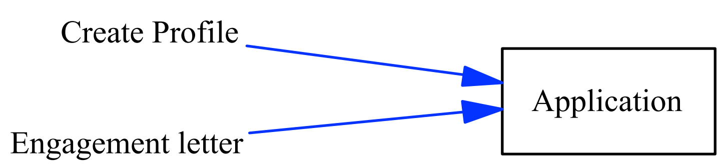
Figure 3-2 The overall Equity Crowdfunding Process.



Throughout this process slowdown or throwback can of course be encountered. These are mostly resolved via the terms of investee and terms of investor that are carefully written down by all equity crowdfunding platforms.

The application step

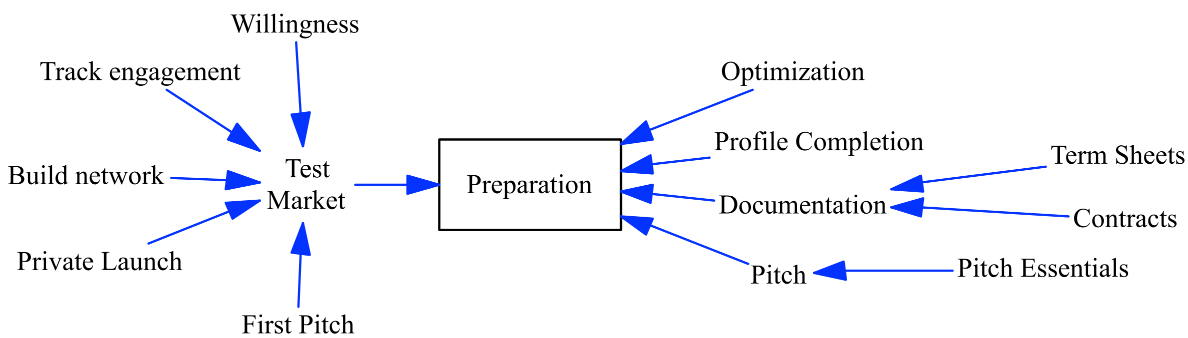
Figure 3-3 Factors influencing the application step in the equity crowdfunding process.



In the application step, the entrepreneur generally needs to create on account on the equity crowdfunding website. Via this account he/she then applies for the funding process to take on. In few cases, like in the case of CircleUp, the entrepreneur also needs to write an engagement letter, to make sure that he is dedicated to his future activity. **Figure 3.3** shows all factors influencing this application step.

The preparation step

Figure 3-4 Factors influencing the preparation step in the equity crowdfunding process.

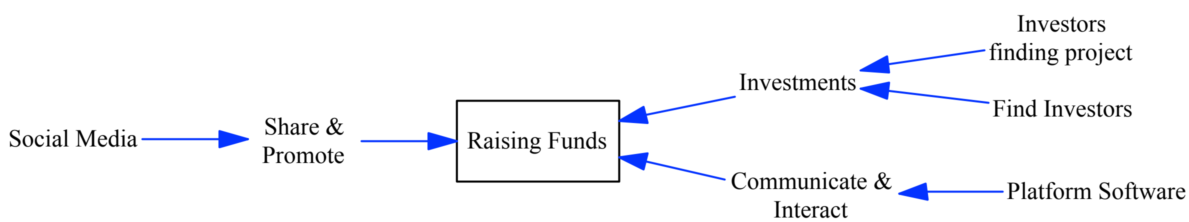


In the preparation step, the application of the entrepreneur has been accepted, after vetting on the entrepreneur has been performed by the platform. Preparation from this point on will be in spite of the launch of the project and raising the funds. It is possible that in this preparation phase the market will be tested first, aka some sort of pre-launch of the project, a first pitch. This is so on Localstake and WiSeed for example. WiSeed is facilitating this via an e-vote in the community of investors. The willingness to invest and engagement of the investors will be evaluated here. In some cases, like in the case of Seedrs, there will even be a private launch organized, where first investors can already commit to the project. This all seems like an ideal opportunity to already build the network of investors for the company. Syndicateroom takes this first pitch even to a next level. They require business angels that are registered as investors onto their platform to invest for already 25% of the business.

The preparation phase is also about optimizing and completing the profile of the entrepreneur. After the vetting, maybe some questions by the platform need some additional explaining. The goal of this is for the entrepreneur and the platform to be on the same line and to make sure that all pitch essentials, as mentioned before, are generating additional value in the pitch. All this needs to be supported by proper documentation like terms sheets and contracts (e.g. between the entrepreneur and the platform). **Figure 3.4** shows all factors influencing this preparation step.

Raising funds

Figure 3-5 Factors influencing raising funds in the equity crowdfunding process.



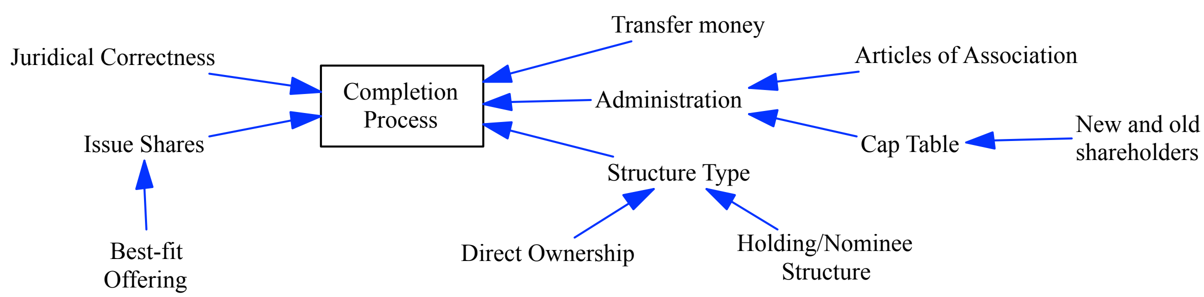
There is a lot more to raising funds via equity crowdfunding than might appear at first sight. If is fair to say that equity crowdfunding is for a large part about marketing. Investors need to be convinced that there is a need for the product or service. This includes a lot of promotion and sharing of the entrepreneur's project to achieve this. Social media form the ideal way to do this. A perfect example for this is the successful story of Domobios (D. Penninckx, personal communication, May 2, 2016). With their first crowdfunding round, they created a team of 100 ambassadors who spoke of Acar'Up (their product) around them. Their action was heavily relayed in the press. Delighted with their first experience, they conducted a second round. Again, the goal was marketing. They decided to undertake the fastest fundraising in Europe yet, with the aim to be seen on TV, and they succeeded. Thus, sharing and promotion indeed is a critical aspect of equity crowdfunding as well.

A second aspect is about communicating and interacting with the (potential) investors. Some of them might have questions that need answering to convince them to invest. Raising funds is thus also a way to show the world and the investors what you are standing for as a company. The communication with investors is often facilitated by the platform via some form of online software, a channel that connects the investors with the entrepreneur.

And thirdly, the entrepreneur needs to raise the necessary funds, of course. Investors may discover the project themselves or the entrepreneur might go on and find the most appropriate investors for his/her project. This second option is often also supported by the platform' software. **Figure 3.5** shows all factors influencing these aspects.

Completion process

Figure 3-6 Factors influencing the completion process in the equity crowdfunding process.



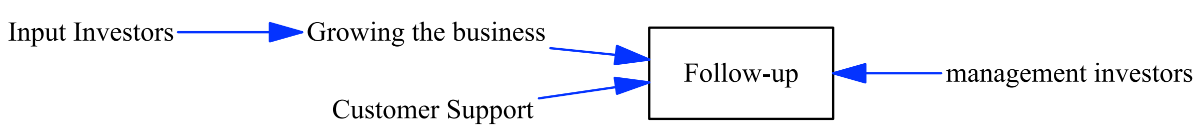
The completion process in equity crowdfunding is mostly handled by the platform itself, like in the case of CircleUp. The raised money that generally is held by an escrow party is transferred to the entrepreneur and the necessary documents are completed by the platform. Generally we speak of the articles of association that are finalized and a cap table that is set up to have a view on the new and old shareholders. All this needs to be taken care of with juridical correctness, related old course to the relevant country. Also, the shares need to be issued to the investors, e.g. via mail; this is also handled by the platform.

A last element that pops up in the completion process of equity crowdfunding is the type of structure that will be dealt with concerning the rights of the investors. One type is direct ownership, where investors have the same rights as any other common investor of the company. Localstake and Crowdcube both act in this way.

The other, more common, way is via the creation of a holding or nominee, where generally the platform will act as a representative of the investing crowd. Wefunder, Seedinvest, BankToTheFuture, Seedrs, Syndicateroom, WiSeed, Symbid, MyMicroInvest are all platforms that are working via a nominee structure. This has a huge advantage for the entrepreneur as he is only dealing with one single shareholder. No paperwork for hundreds of investors is needed this way. R. Peels, from Only Once, confirms this advantage (personal communication, April 23, 2016). This type of indirect ownership implies that shares are not in an individual's name but held by a third party. The rights for investors connected to the types of ownership will be discussed later on. Some platforms, like CircleUp and Invesdor, are offering to choose between a nominee structure and direct ownership. **Figure 3.6** gives an overview of all factors influencing this completion process.

Follow-up on investment

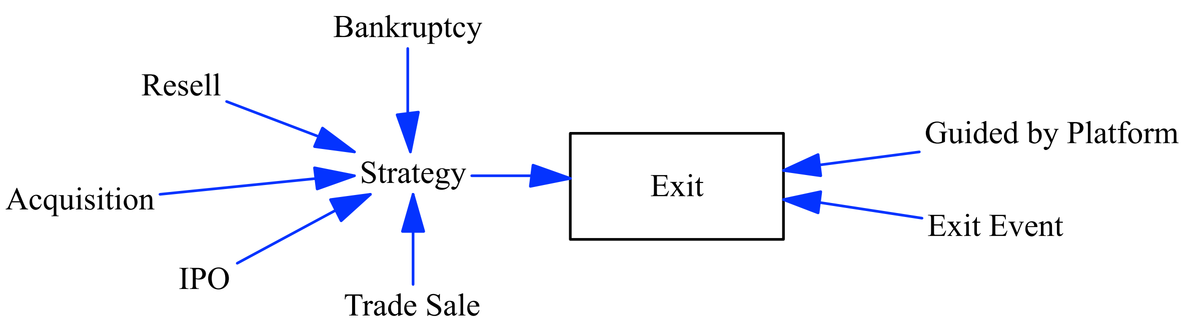
Figure 3-7 Factors influencing the follow-up on investment in the equity crowdfunding process.



Following up on the investments made by the investors is the next step in the process. During the growth of the business enough updates need to be provided towards the investors. In some cases investors might even help the entrepreneur in growing the business (e.g. develop networks). Symbid is one of those platforms that are encouraging this. The follow-up also concerns the support of the first customers that jumped on the product or service provided. The follow-up step is also about the management of all investors, as the crowd investors might not be the only investors. It might be that the percentage of equity that the crowd possesses is merely a fraction of the percentage that, for example, a business angels or a venture capital fund is possessing. This needs to be managed properly. In one of the following sections, we will go into more detail about the interaction with the investors. **Figure 3.7** shows all factors influencing the follow-up on investment step.

The exit step

Figure 3-8 Factors influencing the exit step in the equity crowdfunding process.



The exit step mainly concerns the exit strategy. This strategy, may have be already been agreed on by the entrepreneur and the platform in the contract between the parties. Of course, several exits are possible: resell of (part of) the company, merger or acquisition, an IPO, a trade sale, or, in case of equity crowdfunding a common one, bankruptcy. Some platforms, like, Wefunder, do not allow for a resell of the company. Others, like Syndicateroom, only prefer trade selling or an IPO. In the case of MyMicroInvest and exit strategy is part of the deal (M. Turcksin, personal communication, May 3, 2016). The start-up company Opinum experienced this in real life. As equity crowdfunding was only a small part of their total amount of capital raised, they needed to negotiate the exit strategy with all other investor parties involved. An agreement on the exit strategy was the result. This agreement included several exit conditions and also stated that the entrepreneurs, as shareholders, cannot sell before a specific period of time. Also for other investor parties this is the case.

What is clear however is that the platform will mostly guide the entrepreneur through the exit process. Crowdcube, for example, is stating to “drop a line” and they will guide the entrepreneur trough this process. Platforms are not willing to wait too long for a potential exit. WiSeed for example states that exit possibilities can already be looked at after two or three years. In some cases, e.g. Seedmatch, an exit event is even set up for this final step. **Figure 3.8** shows all factors influencing the exit step in the equity crowdfunding process.

Investor Interaction

All equity crowdfunding platforms are allowing the entrepreneur to interact with the crowd investors in some or another way. The most common way is via the website of the platform or software connected to this platform. Mostly this is in the form of a sort of forum or discussion board or a Q&A section. The CircleUp Hub Platform (CircleUp), The Funded Club (Crowdcube) and The Inner Circle (Symbid) are examples of those kinds of platforms facilitating this kind of interaction. Communication with investors is handled similarly in the US, UK and Europe. In any case “the proximity with the crowd investors is a very interesting aspect” (D. Penninckx, personal communication, May 2, 2016).

Interaction during funding

Generally the amount of interaction between the entrepreneur and the crowd is up to the entrepreneur. However, some platforms are advising how interaction with the investors is optimal. This is then represented in the tools they make available on their website or platform. With interaction mostly communication is meant in the form of updates of information towards investor, contacting current and future investors, answering/posing questions of/to investors, and feedback of investors. As an example of contacting future investors, CircleUp is working with an amount of message credits per week that an entrepreneur can make us of. But, interaction with investors is not merely about communication and answering their questions. Wefunder indicates that investors can also be used as a marketing tool.

The type and amount of interaction provided on these channels can thus be varying over different platforms. There could be a very close and personal connection, like in the case of Angellist, CircleUp, BankToTheFuture or Invesdor. For Angellist, this seems rather normal, as the common investor on there is a business angel, which generally stands closer to the entrepreneur than a common crowd investor. In the case of personalized interaction, often the contact details of the entrepreneur are given to the investors. Localstake states that close interaction with investors is useful for optimizing the investor terms and driving down the cost of capital. Seedinvest also is seeing the potential of the point of view of the investors, but urges to focus on the investors that really add value to the business. FundedByMe is taking on the same view: entrepreneurs should exploit the skills that investors could bring to the table. Symbid also approves of using investors as a think-tank. Invesdor, however, notes that the inverse is possible as well: entrepreneurs supporting investors with their own expertise. In that case investors are involved in the growth of the business and networking events.

In other cases the interaction could be more private and held back, like with Crowdfunder or Wefunder. In the case of Crowdfunder the connection made is only rather a financial one, nothing more. Wefunder tells the investors not to expect too much communication, as the entrepreneur has often other priorities. Investor can provide feedback, but only via the website. No personal contacts will be exchanged between the entrepreneur and the investors. Of course, it is in this case up to the entrepreneur to make a connection if wanted eventually. The start-up company Only Once can approve of this (R. Peels, personal communication, April 23, 2016). In their case, they only communicated with their largest investors, as these are investors they can simply not ignore. Symbid, the ECP that they were using, also did not exchange personal contacts between the investors and the entrepreneur.

Post-investment interaction

The funding is done and the investments of the investors are transferred to the entrepreneur. Now what is next? Where does this leave the (ongoing) interaction between entrepreneurs and their investors? Well, one this is for sure: investors, who have contributed to the successful funding, have the right of knowing what will happen with their money for reasons of transparency. Thus, they have an information right. All platforms are acknowledging this right. However, not all platforms are demanding the same amount of post-investment interaction of the entrepreneur towards investors. CircleUp, Wefunder, Localstake, Crowdcube, Seedmatch and Companisto are platforms demanding for at least an update about the financial and development every quarter of a year. Additionally to this a yearly report should be created. Depending on the close or distant approach of the entrepreneur and the platform towards investors, the entrepreneur could also work together with the investors to grow the business, collect them into private groups for personal updates, do some mentorship, reach for investors for marketing or other skills, arrange networking events, and so on. All this is mostly up to the entrepreneur to decide. Domobios, a start-up company, was very creative in accessing investors as a way of growing their business by some sort of call to actions (D. Penninckx, personal communication, May 2, 2016). When their product was known, they asked each crowd investor to visit two or three pharmacies to ask questions about allergies and Acar'Up (their product). This way they convinced pharmacies that there was a need for the product. There is a benefit linked to these actions for the investors as well: they will help to grow the company and this will have a positive effect on their shares.

An important note is that in the cases where the investors are grouped into a nominee or holding it is common that the entrepreneur is merely in contact with the representative(s) of that holding. Thus, the entrepreneur does not need to inform all investors individually. It will be the representative of the holding that will take on this responsibility. This was also the case for Only Once that used Symbid as an ECP (R. Peels, personal communication, April 23, 2016) and for Opinum that used MyMicroInvest as an ECP (M. Turcksin, personal communication, May 3, 2016). In their case, there is no direct interaction left between the general crowd investors and the entrepreneurs.

Support of the Equity Crowdfunding Platform

This section will sum up all activities in which support for the entrepreneur could be expected from the equity crowdfunding platform. There is no distinction on this level present between any countries: services and support are both available on European and American platforms. One exception perhaps is the collecting of data and analytics on investors' successful deals. It seems that only (some) American platforms are serving this possibility to the entrepreneurs. In Europe, such a service is unseen. Also important to say is that not all supporting activities are provided by every platform. Most platforms are focusing on some of these. A supporting element that all platforms share is of course the availability of their platform that forms the connection between investors and entrepreneurs. Besides this, other possible supporting activities where platforms are focusing on are the following (ordered from seemingly more popular services).

- Legal and administrative help on structure of the investment, articles of association, transferring money, the investor terms, issuing shares and other paperwork (Crowdfunder, Localstake, Seedinvest, Crowdcube, Syndicateroom, Wefunder, Invesdor, BankToTheFuture, Seedrs).
- Marketing tools and engagement tools. This can be present in different forms: sharing of the project, communication. This sharing can take on two forms: to the outside world and to relevant investors (Crowdfunder, Seedinvest, Seedrs, MyMicroInvest, Seedmatch, Invesdor, FundedByMe).
- Expertise sharing in the form of tips and tricks and experience (CircleUp, Seedrs, Seedmatch, FundedByMe).
- Data and analytics on investors and successful deals (CircleUp, Crowdfunder, EquityNet, Localstake).
- Investor Vetting. In section … we showed that equity crowdfunding platforms are performing vetting on investors in the form of (non)-accreditation. This of course is important information for the entrepreneur, especially if a platform is doing this vetting intensively. This way, entrepreneurs have a clearer and more secure view on their investors (CircleUp, Seedinvest). Automation/standardization tool on writing the business plan or contracts (EquityNet, Seedmatch).
- Documentation/Information on equity crowdfunding (as mentioned before).

Some platforms are not stating the support they will be giving upfront. They merely indicate that they will be there each step of the process (e.g. Fundable, Wefunder, MyMicroInvest, Crowdcube, WiSeed, Symbid). In case of Symbid and MyMicroInvest, and perhaps in all these cases, a project manager is assigned that indeed guides the entrepreneur trough the equity crowdfunding process. R. Peels (personal communication, April 23, 2016) worked together with Symbid on his start-up company Only Once. Indeed, a project manager from Symbid was assigned to the company. Nevertheless, the administrative process still took over three months. The reason is simple: as a start-up company you do not have all details about your company on paper yet. However, the platform is requiring this from you. Agreed, they will guide the entrepreneur through all steps and all documents needed, but the actual writing of the documents is all up to the entrepreneur. Every possible question needs to have a decent answer and sometimes you really get tired of answering questions on which you do not know the answers yet. In the case of MyMicroInvest, the platform also provided the entrepreneur with all the necessary forms to fill in (M. Turcksin, personal communication, May 3, 2016), and give a lot of support on the administrative, communication and networking level (D. Penninckx, personal communication, May 2, 2016).

Legal considerations

This section will elaborate on some legal consideration about equity crowdfunding that the entrepreneur should be aware of. First an introduction will be given to some general equity crowdfunding legislation. Then the conducted study will firstly discuss the rights of investors as a part of the funding process and secondly possible exclusiveness of the financing technique.

Equity crowdfunding legislation

The troubled juridical scheme applicable to equity crowdfunding is driving European legislation to find a balance between enough protection for the investors and enough flexibility towards entrepreneurs (Lavens, 2015). However, at this point, European initiatives are focusing on mapping the crowdfunding market. This drives national countries to organize the market themselves and provide the relevant legislation. In Belgium, for example, companies can enjoy an exemption on the *Prospectuswet*, which lowers the financing cost for the entrepreneur and, just like in the American JOBS Act, protects the investors by indicating a maximum amount of investment. The platform themselves seem to be knowing what they are talking about and handle the legal documentations quiet well (M. Turcksin, personal communication, May 3, 2016). However, it is fair to say that they are operating in the grey zones of the juridical system on equity crowdfunding and that they are testing the limits.

But which party, the entrepreneur, the platform, or the investors, carries the largest burden concerning the legislation on equity crowdfunding? Well, let us again take the example of Belgium. In Belgium, the entrepreneur should only be concerned about consumer provisions (Lavens, 2015). The platform, on the other hand, should be dealing with the Prospectuswet, the act on investment companies, the act on payment institutions and consumer rights. Additionally, they will need a license as a brokerage firm (or as a wealth and investment advice firm) and a statute from a payment institution. If we assume that other European countries are following this kind of legislation, this makes the image fairly clear: the platforms will carry a lot of responsibility concerning the crowdfunding legislation. This, of course, explains why a lot of platforms are handling all paperwork for the entrepreneur.

We will see that information right is an important right that all investors are supposed to have: the right to know what’s going on with the business in which they invest. The question remains on how to enforce this right and assure the quality of information provided. Therefor, Lavens (2015) argues, legislation on equity crowdfunding should also rely on rules of conduct, to ensure the creation of a form of trust between all parties.

The USA, in the meantime, the SEC finalized their regulation on crowd funding, which is already effective since January 29, 2016 (Quinlivan, Jenson, Brenckman, & Kuettel, 2015). This regulation is part of the JOBS Act, signed into law by president Obama in 2012 (Securities and exchange commission, 2016). It is an act to encourage funding of the US by supporting some (new) securities regulations. Crowdfunding, including the regulation, is one of the titles/topics in this act. The regulation on crowdfunding defines all requirements for a so-called 'Funding Portal'. This includes a registration requirement, information and financial requirements, some sort of due diligence duty for preventing fraud, a whole set of safe harbor for certain activities (on advertisements, accepting investor commitments, paying for referrals, communication channels, and so on), a compliance act (on privacy and policies) and lots of other provisions. It also includes another major decision: bringing non-accredited investors into the fold for equity crowdfunding (Barnet, 2015), the so-called general solicitation. This will allow everyday ciztizens to invest in startups and thus open up a huge amount of capital for new companies. One thing is for sure: the US legislation is positioning the equity crowdfunding portals as the gatekeepers of the market, as they deicide who will engage in the funding process. This makes that they will certainly have a reputation to defend as a funding portal.

This kind of statute ('funding portal') is only present in a few European countries, like Italy and France (Lavens, 2015). However, it would be a huge stimulator for the further development of equity crowdfunding if the European Union could crate a common European framework: an internal, cross-border and unified market.

Investor rights

At this point in time, the JOBS Act in the US is being executed. This will have an influence on the type of investors the entrepreneur will be dealing with and thus also on what rights these investors will be getting from the entrepreneur or platform.

In general it seems that two main options are possible concerning the right that investors will be getting. The first option is in line with when the crowd is assembled into one legal entity in the form of a holding or nominee party. In this case, as the crowd is already being represented, individual investors do not need to expect too much addition rights, as in most cases the nominee party will act on their behalf. The amount of involvement that investors have is in this case fully up to this newly created third party. It is thus perfectly possible that investors will be getting no rights at all. This is, for example, the case at Wefunder. In other cases, like with Seedrs or MyMicroInvest, investors are getting some rights, like a voting right even though they are represented via a nominee party. Thus, they are still maintaining some economic interest on their own shares. An important aspect comes to play when dealing with a holding or nominee party. In most cases, one person will be representing the crowd in this holding. As a result this one person will also be getting a position in the board of direction of the company. This seems mostly the case on European platforms like WiSeed, Symbid and MyMicroInvest. Invesdor handless the issue of having someone on the board a bit differently: they are sending invitation to investors to occasionally participate in a shareholder meeting.

The second option is that the platform and the entrepreneur will intensively discuss the rights that investors will be getting. Investors could be included in this discussion, like in the case of Crowdcube. These rights will then be included in an investor rights agreement. Important to see is that there is no need for reinventing the wheel. Syndicateroom, for example, argues that the same legal documentation that already exists for angel investors will be used towards investors.

Investors will thus, in some cases, be getting investor protection. But two question still need answering: what rights are we then talking about and what types of share are investors having in hand at the end? One right that all investors, among all platforms, are getting is the right on information. This right captures the given that the entrepreneur needs to communicate important developments with the investors and has to periodically provide them with financial and economic reports. Another right that is being discussed on a lot of platforms is voting right. When a holding is created, where the crowd is represented, the voting right will mostly end up with the representative person of that holding. This person can than choose to communicate with the crowd and involve them or completely act on their behalf, without any interaction. Important to see here is that the entrepreneur does not need to care about the potential voting of hundreds of investors. This will then all be managed by the created cooperative, like in the case of WiSeed or Symbid. Some platforms say from the beginning that investors will not be getting any voting rights (e.g. Seedmatch), others (e.g. BankToTheFuture) allow the entrepreneur to set a minimum investment size to qualify for voting rights. When we are not dealing with a holding or cooperative institution arrangements can be made between the entrepreneur, investors and the platform, but in most cases crowd investors do not need to count too much on these.

Other rights that can be given to investors are tag along and drag along rights, like in the case of Syndicateroom. A tag-along right is an obligation to protect a minority shareholder. If a majority shareholder would sell his or her stake, the minority shareholder will have the right to go along with this action and sell the stake in the company as well (Investopedia, 2016b). A drag-along right, the inverse of a tag-along right, enables a majority shareholder to force a minority shareholder to participate in the selling the company (Investopedia, 2016c). On the other hand, Syndicateroom, for example, is not giving another right to investors: an anti-dilution right. This makes that investors may lose their percentage of equity in the company, after follow-up rounds of raising additional capital by the company. Some platforms, like Seedrs, are giving this right to investors. At Companisto liquidation rights are given to investors, meaning that in the case of bankruptcy investors will have the right to claim assets of the company. Thus, investors are threatened equally amongst potential business angels or venture capitalists. Another right that could be given to investors are preemptive rights. This right will then give the crowd investors the possibility to purchase additional shares in the company before the general public would have this opportunity if a seasoned offering would happen (Investopedia, 2016d). In general dividends could also be given to crowd investors (e.g. Invesdor)

The second question that needs answering is what type of share we are dealing with. Well, one thing is for sure: each platform is giving the child another name. In the USA we are dealing with restricted stock (CircleUp), revenue shares or equity securities (Localstake). In Europe, we speak of ordinary shares (Seedrs), (e)-certificates (Symbid and Invesdor), an equity-link-note (MyMicroInvest) or a subordinated profit-participating loan (Companisto). Whatever names the child is carrying, platforms are indicating that in most cases similar characteristic as normal equity investment of a business angel or a venture capitalist will be searched for. In practice, as most platform are using a cooperative or holding to manage investors, the rights will be transferred to the person in charge of this holding, which is a commonly a project manager of the platform itself. As an example, one of the founders behind Opinum, M. Turcksin, does not even know all terms and conditions between the crowd investors and the equity crowdfunding platform, but he knows that they have a type of share that does not offer any additional right, next to the information right (personal communication, May 3, 2016).

As an example, R. Peels (personal communication, April 23, 2016) notes the process of issuing the shares was fully automated by Symbid. Investors merely get a so-called proof of capital, which they can download on the platform. The proof of capital gives investors the right on their economic value. However, this really is their only right.

Exclusiveness of the funding method

An interesting element for the entrepreneur to know is that some equity crowdfunding platforms are requesting exclusivity of the funding method. This means that the entrepreneur cannot use another funding method along with equity crowdfunding. Platforms that are doing this are Crowdcube and Localstake. Other platforms, however, do allow this option. Some allow it, but only under certain conditions. Seedrs, for example, only allow co-investment of a venture capitalist or business angel.

Chapter 4 - Conclusions and Recommendations

Conclusions

This study was set out to explore equity crowdfunding. In particular, two inquiries were derived. The first one was to position equity crowdfunding along alternative equity financing techniques. The second one was to answer a set of questions related to the equity crowdfunding technique. Both questions were approached via the entrepreneurial, start-up side of the funding story. The importance of this study has mainly to do with the rising importance of equity crowdfunding. Today, banks are less eager to give a loan to start-up companies. And even if they would, most of the information that the entrepreneur needs to provide is simply not accessible yet by the entrepreneur. In addition, traditional investors, like venture capitalists and business angels, are being too cautious in the case of start-up companies and they get a lot of criticism on their lack of regional, gender, and ethnic inclusiveness. As a result, the entrepreneur is in need of a good overview of where crowdfunding is standing and what he/she may or may not expect from it.

Empirical findings

This section will provide answers and comments on the two main questions from this thesis. However, in order to do so properly the literature study, performed in chapter two, first needs to be critically reviewed based on the information gathered in the study on the equity crowdfunding platforms.

Critical review on literature

First of all, it is true that equity crowdfunding platforms are focusing on seed and early stage start-up firms. However, it needs to be said that also grown and developed firms can take their shot in equity crowdfunding. In these cases, the company often is working on a particular project within the company and is seeking funding for that project. In addition, we can conclude that equity crowdfunding platforms are looking for a lot of growth potential. This is an element that hasn't been stated throughout literature yet. Thus, it is fair to say that equity crowdfunding is focusing on seed and early stage firms, but that developed companies can also find funding for particular projects. The common element here is the need for a potential significant growth.

Concerning the crowd investors, literature mostly states that investors are investing small amounts into a project. However, a lot of platforms also have a network of venture capitalists and business angels along their crowd investors, which are investing significant amounts of money. This also indicates that the view on a typical investor profile needs to be reviewed. The mass can indeed be considered as inexperienced, yet a significant amount can be experienced and add non-financial value for the entrepreneur. This given also gives new light to the element of due diligence, which can now also take on an extensive form, when for example a venture capitalists is amongst crowd investors. Another element, concerning the investors, is that they are little protected. This is true to a great extent, however it needs to be said that there is a trend of protecting investors in the legislation of individual countries, e.g. maximum amount of investments, accreditation of investors, and so on.

Thirdly, literature states that equity crowdfunding is about innovative firms. This then seems to be a criterion for application on a platform. In practice, this is also not really the case. Most platforms are not even requesting or stating the project to be innovative. More importantly is the vision and the concept as a whole and the possibility to create a momentum around a project. The performed study on the platform also rejects the fact that little or none prerequisites are required to apply for funding on an ECP. The entrepreneur needs to have all necessary documents in place, especially the business plan and a financial forecast. In addition a lot of platforms have their own, more specific, conditions for applying on their platform.

Lastly, stating that equity crowdfunding is a global given seems a little bit to opportunistic at this point in time. In a lot of cases the platform only allows companies that are domiciled in the country of the platform itself. Investors, on the other hand, can indeed invest in the project from all over the world, although also exceptions can be made here. In any case, the fact that legislation is not yet unified over Europe, or over the entire world, makes that equity crowdfunding still has its geographic limits.

Findings on positioning equity crowdfunding

Chapter two covered the first research inquiry via an extensive and structured literature review. The conclusion is fairly straightforward: equity financing takes in a complementary position between angel investment financing and venture capital financing. The reason for this is the set of unique aspects that equity crowdfunding brings along. For starters, a third party, the equity crowdfunding platforms, is driving the whole process. Investors are becoming a crowd, a community, which is often more used as a marketing tool. These investors can invest very little amounts individually. Due diligence also takes on a whole different form: the platforms are mostly deciding the amount of control on entrepreneurs and investors will start to rely on some sort of crowd diligence. Also, contracts that investors are getting are not that typical for an equity financing contract; they are often dealing with pro-rate shares in the form of convertible bonds, participation notes, cooperative certificates, and other forms. And all of these contracts are standardized and often only give information right to individual investors. Lastly, equity crowdfunding can take on a global level. These are all elements that are generally not present in the case of the traditional financing techniques.

However the literature study also showed that equity financing could compete, and thus be a substitute to all three traditional financing techniques. The reason for this is the overlap on some aspects with these three:

- In the case of family and friends, equity financing is also focusing on a trust-based relationship in terms of the risks related to the project. No real standardized mechanisms exist to protect the investors at this point in time. Family and friends financing also is taking place in the seed and early stages of a venture.
- In the case of business angels, equity financing also takes on a more passive involvement from investors and these investors might also be partially driven by an emotional affect for a certain project. Of course a financial gain is still expected as well. Another overlap is the fact that both methods also focus on the seed and early stage markets and that the process of a successful exit is rather long and rare.
- Similarities with venture capital financing can also be found. In a lot of cases with equity crowdfunding, there is no real contact with the investors. The formal role that is being created is also typical about venture capital. Venture capitalists often assist entrepreneurs extensively, but the relationship always remains a rather formal one. Another similarity is that venture capitalists seek significant fast growth. This is also what the equity crowdfunding platforms are looking for, as they do not want to be attached to long to a particular project.

In sum, equity crowdfunding finance certainly has its unique aspects, which makes it take in a complementary place between angel investors on the one hand and venture capitalists on the other hand. However, similarities with both of these methods also make equity crowdfunding a possible substitute to the traditional financing techniques.

Findings on assessing equity crowdfunding platforms

Chapter three covered the second research inquiry via an in-depth study on twenty equity crowdfunding platforms. First of all, the entrepreneur needs to take into account financial considerations. Concerning the fees that an ECP could ask, registration is mostly free. Most popular fee's being asked are success and administration fees. These higher the fees, the more support will generally be given to the entrepreneur. Some American platforms tend to work with monthly subscriptions. The entrepreneur also needs to watch out for additional services that are actually being charged. The entrepreneur is mostly the one in charge of deciding the amount of equity offered. He can of course choose to be supported by the platform, via their tools, people or documentation, or by a third party of choice. In some cases the entrepreneur and important crowd investors sit together to value the company. Important to know is that mostly the amount of equity is generally unchangeable during funding. There is an exception in case of overfunding, which is supported by most platforms. In this case the value of the company might change. The entrepreneur is then in charge to allow overfunding or not. Overfunding can only happen if the company raises enough capital. This is commonly a first condition: raising the target capital. Most platforms work with an all or not formula, which leaves entrepreneurs with no capital if the target is not reached. In some cases, however, an arrangement is made between the entrepreneur and the investors. A last financial consideration is that follow-on capital is not really being supported by platforms. Often a complete new project needs to be created by the entrepreneur, which brings along some disadvantages in terms of communication towards investors. If follow-on capital, on the other hand, is supported, the entrepreneur needs to be aware of the fact that this might dilute previous (crowd) investors.

Secondly, when looking at the pitch drivers, the entrepreneur needs to know that a business plan and a financial forecast are important pitch essentials. Story telling and visual representing your company are important ones as well. In Europe, the management team also is taking on a great role. All pitch essentials are generally summarized in a pitch deck on the platform. All platforms are paying more attention on some elements than on others. The pitch window is in Europe mostly fixed and in America flexible (negotiable). A typical pitch stays on between 30 days and three months.

Thirdly, this study modeled existing vetting and due diligence flows into a model, which also takes into account the entrepreneurial side. The entrepreneur will be responsible for investor management and will seek some kind of protection against the equity crowdfunding platform. He/she also needs to be aware of the fact that investors might be accredited by the platform or not. The investors will generally control the entrepreneur via a form of crowd diligence. The platform will perform some vetting on the entrepreneur in the form of application conditions and some additional diligence that is dependent on the focus of a particular platform. Conditions on American platforms seem to be stricter when looking at the type of industry of the project. European platforms generally accept all types of industries. Other common criteria are the story telling aspect, possibility of creating a momentum, playing in a fast growing market, and having a good management team available.

Fourthly, this study review and modeled the equity crowdfunding process in more detail. This gives the entrepreneur a good overview of all elements that good be involved in creating an equity crowdfunding project. For example, its could be that a private launch or first pitch is being performed before the real pitch as a form of testing the product or service. Another example is that the completion process is mostly performed by the platform, not by the entrepreneur.

Another interesting aspect in the process is that the exit strategy can already be determined in the contract between the parties.

Fifthly, the entrepreneur should recognize that investor interaction could be an important variable in the story. This interaction is arranged via the platform and the amount of interaction is mostly up to the entrepreneur. He/she can choose for a personal approach, and maybe treat some of them as real angels investors that might bring some non-financial added value, or he/she can go for a more private approach. In this second case no contact information is exchanged between investors and entrepreneurs. After the funding investors have information right that allow them to get regular update on performance and developments of the company. In some cases investors might be used to help growing the business. In most cases, after successful funding, investors are assembled into a nominee party that is being represented by one person of the equity crowdfunding platform or a significant investor.

Next, entrepreneurs should be aware of the amount of support that a platform might provide. Mostly platforms are giving support in terms of administration and legalization, and in the form of marketing and engagement tools. American platforms sometimes also provide data and analytics on (potential) crowd investors. Other platforms state that they will support the entrepreneur all the way trough the process, however this does not necessary mean that each step of the process will go fluently. For example, the platform might provide a lot of templates as a form of support, yet filling in these templates might still be completely the task of the entrepreneur.

And lastly, this thesis has studies some legal aspects concerning equity crowdfunding. In case of the creation of a nominee/holding party, investors generally have no additional rights left. In some, fewer, cases the entrepreneur and investors might discuss the rights they get. Rights that could come into play then are voting right, tag- and drag-along rights, anti-dilution rights, liquidation rights, and preemptive rights. Another legal consideration for the entrepreneur is that in some cases the platforms are asking for full exclusiveness on the funding method, meaning that entrepreneurs may not use other financing techniques at the same time.

Implications

This thesis shows that some elements about the equity crowdfunding platforms have changed over recent years. The critical review on the literature in this paper summarized the evolutions in equity crowdfunding. Indeed, the differences between this paper and some previous literature need to be seen as evolutions on the topic of equity crowdfunding, and not as mistakes. These platforms are constantly adapting and adjusting themselves, driven by rules and regulations that are becoming more concrete year after year. Nevertheless it has also become clear that a lot of similarities were found between this study and previous ones. Thus, this paper is certainly also supporting and building on previous literature.

This paper indirectly discussed implications for the entrepreneur as well, as a lot of elements were discussed that play an important lore in the entrepreneurial decision making. At the end, this paper supports equity crowdfunding as an financing option for entrepreneurs as throughout this study a lot of advantages were pointed out like how equity crowdfunding can be an important networking, communication and marketing tool, how it can be less of a burden than, for example, seeking a loan via a bank, and how it is taking its place between alternative equity crowdfunding techniques. Another important advantage is the fact that the entrepreneur is dealing with very flexible investors. Nevertheless the entrepreneur should certainly also consider other financing sources that do not require giving up equity, like subsidies from governments. Also, doing equity crowdfunding implicates to be extremely prepared, which can be a large burden and time-consuming. The entrepreneur needs to be able to answer all possible questions, even detailed ones.

Limitations and Recommendations

The study on the equity crowdfunding platforms encountered a number of limitations, which need to be considered. The main limitation has to do with the selection of the equity crowdfunding platforms. The study was performed on *only* twenty platforms, which could be considered rather small in comparison with the total amount of equity crowdfunding platforms present globally. Thus a sample limitation could be considered in this thesis. However, to counter this aspect it is fair to say that, even though every platform is quite unique, the findings would not be changing that much as a lot of similarities were found between platforms as well. To be sure a validation study needs to be conducted on a much larger international scale.

However, a larger study might become irrelevant in a few years because of the evolution phase that platforms are undergoing at this point in time. This can be seen as a limitation of this study on its own. Therefor it is rather recommended to keep track of the developments on platforms on a more regional level for the upcoming years. When or if platforms converge to a similar state or are becoming more standardized over the world, a global study could show its true value. Of course, to keep on discovering the evolutions in the field of equity crowdfunding, there is a need for more (case) studies to allow further assessment of the subject. Some aspects that are worth exploring are the different approaches and chances of success of different types of projects on the equity crowdfunding platforms, the possibility of unifying platforms over a certain region, and assessing equity crowdfunding next to other financing techniques (e.g. banks). Also loan-based arrangements on platforms are popping up on different platforms. Their potential impact and organization should be studied also. Lastly, studies on the legalization aspects of equity crowdfunding cannot be neglected either.

Ending Note

At the end, this study will contribute to the overall study on equity crowdfunding and on the equity crowdfunding platforms. In addition this thesis took on the side of those who dare to dream without limitations, those who do not fear the unknown unknowns, but embrace their feeling of becoming the next great Henry Ford, Steve Jobs, Walt Disney or Larry Page. May the hopes and visions of these flourish and become reality via the emerging instruments that are equity crowdfunding platforms.

Chapter 5 - References

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