



SCOTTISH COMMUNITY RE:INVESTMENT TRUST

# **Crowdfunding and the Third Sector in Scotland July 2014**

*Re:Investing in Scottish communities.*

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## 1. Introduction and Methodology:

Senscot, the Social Entrepreneurs Network Scotland, in conjunction with the Scottish Community Reinvestment Trust (SCRT) are aware that Crowdfunding might be an innovative way of attracting more funding into the Third Sector, particularly for those organisations wishing to secure relatively small sums of money.

Senscot commissioned this Report to provide an overview of the Crowdfunding opportunities, including, its scope, key characteristics, levels of awareness, and the attitudes towards Crowdfunding in the Scottish Third Sector. It provides informational overview of Crowdfunding in addition to Scottish Third Sector specifics as well as any concerns about Crowdfunding that the sector might have.

This follows on from earlier *Investing in Ideas* research which established that there is a need for an alternative approach to the provision of finance for the sector, one that is based on harnessing the collective assets and expertise of the Third Sector in Scotland and which will provide a suite of financial services relevant to the needs of the sector.

The methodology employed for this work involved the distribution a short Survey Monkey to 140 organisations which elicited a 36% response rate from 50 organisations. Coupled with that a series of one-to-one telephone interviews were held with 10 organisations from across Scotland all of whom had previously undertaken a Crowdfunding campaign. The Consultant also met with 2 network meetings, consisting of 23 Third Sector organisations.

Together with a literature review and an internet search, the report draws upon the findings of the survey monkey questionnaire; the one to one telephone interviews, in addition to articles and research on Crowdfunding from other sources.

## 2. Executive Summary:

Crowdfunding is part of an alternative digitally oriented financial sector that is witnessing significant development and growth since the banking crisis of 2007-8. At a time when commercial banks have markedly reduced their appetite for lending, particularly to social enterprises and the broader third sector, Crowdfunding is emerging as a new democratic form of participative finance that is steadily growing in influence and popularity across the world economy.

Senscot and the SCRT are interested in the alternative financing sector as it allows for other agents to provide finance to the Third Sector in a cost efficient manner. Crowdfunding in particular has the potential to ensure that investment into the Third Sector is appropriate, affordable and aligned to the values and ethos of the Sector. It offers an alternative way of securing micro finance, soft loans and riskier finance for organisations by potentially reaching out to interested constituencies, be they the communities they are part of, the customers that they serve or the partners that they work with. By harnessing the interest of existing or new beneficiaries and supporters as potential investors for services or products, Crowdfunding could be a new way of bringing additional money into the Third Sector in Scotland.

According to the 2013 Crowdfunding Industry Report, there are currently at least 800 different Crowdfunding platforms operating around the world - a figure which grew by 50% in 2013. NESTA's December 13 '*Rise of Future Finance*' Report indicated however that only 50 platforms accounted for 95% of all crowdfunding monies raised in the UK – something which perhaps indicates the difficulty for newer start up platforms to be successful. Of this total there are currently only four Scottish based Crowdfunding platforms- BloomVC; Squareknot; Crowd Racing and ShareIn.

The NESTA Report calculates that for the period 2011-2013 there was an annual 20% average increase in the money raised for UK charities and social enterprises via crowdfunding platforms resulting in a total of £785m. In 2013 alone, £310m was raised from donation based crowdfunding; £20.5m in reward based crowdfunding and a further £0.8m in community shares and microfinance. These figures clearly demonstrate that crowdfunding does work as a fundraising method for Third Sector organisations.

Recent research for the Glasgow Chambers of Commerce indicates that Scotland is lagging behind in accessing all types of finance via Crowdfunding - including donation and reward platforms. The research proposes two principle reasons for this –

- The lack of Scottish-based crowdfunding platforms.
- The lack of a sophisticated understanding of crowdfunding: although general knowledge of Crowdfunding is similar to the UK level.

The Survey data for this Senscot report would appear to confirm this scenario with a very high awareness of Crowdfunding (90%) amongst respondents, matched by relatively low activity levels at 19% of respondents. However, the results also indicate that this low activity level may be masking a time lag between awareness of, and actual engagement in Crowdfunding campaigns with 19% currently considering using it as a potential income stream, and 58% considering using it in the future.

All of the interviewees had previous experience of Crowdfunding campaigns and had reached their financial targets, although the sums of money sought were relatively small from £500 to £15,000. This range reflects the broader views of the Survey respondents with two thirds of those organisations considering Crowdfunding (62.5%), looking to secure £20k. Although, nearly one quarter (22.5%) would consider using it for sums up to £50k.

As the research is primarily concerned with the non-regulated Crowdfunding models i.e. Donation and Reward, our research indicates that about half of the respondents (51%) would be willing to offer a gift or reward in exchange for an investment, but a third were either not willing or able to do so.

What did stand out was that nearly (45%) of respondents indicated that they would be willing to consider all different types of rewards/returns including financial returns for the right project and the right amount of investment.

There was a very mixed response to the question on whether a specific Scottish Third Sector platform would be used, with nearly 70% of survey monkey respondents to the survey indicating that they would use it, provided other support was made available (such as social media advice or assistance with a video production). However, more than half of the interviewees did not see the need for it, citing the current platform availability.

There are clearly some main obstacles and concerns regarding the use of Crowdfunding amongst Third Sector organisations. These issues can be categorised under four broad headings:

- The support needed to make Crowdfunding work for organisations.
- The perception that Crowdfunding is not suitable for all organisations.
- The lack of real understanding about Crowdfunding and how it works.
- The disincentives of Crowdfunding.

These issues would need to be addressed if the sector was to take full advantage of the financial returns offered by Crowdfunding.

It is apparent from those with experience of Crowdfunding that whilst all of them had undertaken Crowdfunding with a view to securing additional monies they were surprised by the non- financial benefits to it - primarily in the area of PR; publicity and additional traffic to websites or additional followers on social media. Most did not anticipate these before the Crowdfunding campaign as they were unforeseen prior to the commencement of the campaign. Strategies to maximise these benefits need to be considered before any campaigns commence on the platforms chosen.

If additional support measures were available and the fee structure was competitive many respondents (70%) indicated they would consider using a new Scottish Third Sector Crowdfunding platform. As such, a new platform would need to recognise its role in up-skilling the sector and the impact that this would have upon the timescale for achieving financial sustainability.

Another determining factor in the success of such a platform would be the extent to which it could reach the Scottish diaspora as most experienced organisations felt this wider reach is crucial to successfully securing the required investment.

In conclusion, it is clear that Crowdfunding is a financial option that the third sector cannot afford to ignore if it is to keep up with contemporary trends in finance which involve the digital economy, and to maintain and develop its services during the current period of fiscal austerity. Crowdfunding finance is predicted to grow at the same rapid pace as the last three years.

Given the small number of Scottish platforms and the current lack of any specific Scottish Third Sector one, there is a strong likelihood that a platform would be successful. Nevertheless, Crowdfunding requires a whole new skillset and expertise that are currently lacking in the Third Sector, in particular engaging potential donors or investors via social media. As such, providing just a platform and driving potential investors/donors to it would not be enough and the following issues will need to be considered:

- A new sector specific platform would need to recognise its role in up-skilling the sector to order to maximise potential financial success.
- Additional support measures would need to be present such as support with making an interesting pitch and/or assistance with social media.
- This approach would have an impact upon the timescale required for the platform to achieve financial sustainability.

As such the cost of providing this 'added value' platform would be significant. It will require at least 2 'creative' staff skilled in social media and an administrator with a potential cost of £80k. There is also the cost of developing a highly technical sophisticated Crowdfunding platform with sufficient interactiveness and accessibility to compete with existing platforms. The cost of designing such a platform is likely to be significant.

Options to keep costs low would be to consider 'white labelling' an existing platform such as Buzzbnk rather than establish a whole new platform. White labelling is where an organisation leases or purchases a fully supported product or service from another source, applies its own brand and identity to it and then markets it as its own. This option could offset the cost of designing a whole new platform.

Another option might be to contract out An alternative might be to contract out the social media support to another organisation with that expertise in house, thereby reducing the core staffing costs to 1 administrator.

### 3. Background Overview:

Crowdfunding is part of an alternative digitally oriented financial sector that is witnessing unprecedented development and growth since the banking crisis of 2007-8. At a time when commercial banks have reduced their appetite for lending, particularly to social enterprises and the broader third sector, crowd-funding is emerging as a democratic form of participative finance that is growing in popularity across the world economy. The alternative finance sector is capitalising on the reluctance of the mainstream banks to provide loans to people and businesses. Utilising the internet as the basis for customer engagement, not only results in a more cost effective way of providing finance, but potentially also in the democratisation of the whole financial sector model.

From equity crowd funding, to peer-to-peer (P2P) lending, from invoice trading to reward crowd funding, these alternative financing activities are supplying early stage investments to start ups, fostering innovation and supporting local activity. According to the Berkeley-Nesta-Cambridge's *UK Alternative Finance Benchmarking Report (2013)*, this marketplace (excluding donation-based crowd-funding) grew in the UK by an average of 75% a year in the last three years to reach £939m of investment in 2013. In addition the report records up to 9.4m active investors and donors in the UK, an average growth rate of 22% (although there is a proviso that this may include double counting as people invest across multiple platforms).

According to the 2012 Breedon Report, since the financial crash, the projected gap between the supply of money and the demand for money amongst UK SME's is estimated to be between £26billion and £59billion in the five years to 2017. This is the gap that alternative finance is increasingly coming to occupy.

Growth across the various forms of crowd-funding and Peer2Peer lending, over the three years to 2013, was high:

- donation-based crowd-funding grew by 20%, *per year on average* to £310m;
- reward based crowd-funding, by 382% to £20.5m;
- microfinance and community shares grew 166% to £0.8m;
- Peer2Peer(P2P) generic lending, by 107% to £287m;
- Peer2Business (P2B) lending, by 200% to £193m;
- invoice trading, by 487% to £97m;
- equity-based crowd-funding, by 371% to £28m;
- debt-based securities, by 170% to £2.7m;
- revenue and profit sharing crowd-funding, by 1400% to £1.5m.

Senscot and the emerging Scottish Community Reinvestment Trust (SCRT) are interested in the alternative financing sector as it allows for other agents to provide finance to the Third Sector in a cost efficient manner. Crowdfunding in particular has the potential to ensure that investment into the Third Sector is appropriate, affordable and aligned to the values and ethos of the Sector. It offers an alternative way of securing micro finance, soft loans and riskier finance for organisations by potentially reaching out to interested constituencies, be they the communities they are part of, the customers that they serve or the partners that they work with. By harnessing the interest of existing or new beneficiaries and supporters as potential investors for services or products, Crowdfunding is an ideal way of bringing new money into the Third Sector in Scotland.

With the support of the BIG Lottery *Investing in Ideas* programme Senscot has commissioned this report to provide an overview of the crowdfunding opportunity, its scope, its key characteristics, and the levels of awareness, appetite for and attitude towards Crowdfunding in the Scottish Third Sector.

Senscot and the SCRT intend to development the unregulated Crowdfund models, which are primarily 'donation' and 'reward' based. It is hoped that this report will determine if there is a need to develop a Scottish wide online platform for the sector.

#### 4. Brief History of Crowdfunding:

The concept of crowdfunding is one where lots of people (the crowd) come together and make small financial contributions (the funding) to ensure a particular project or enterprise happens. Crowdfunding is a very recent development made possible by the networking opportunities afforded by digital media and the internet, with the earliest platforms dating back only to 2000/01. The financial crisis of 2007-8 and the resultant withdrawal of lending has assisted its development as businesses in general, but SME's in particular, were cut off from much needed traditional sources of working capital and investment from banks.

The role of the Internet has been essential to the growth of crowdfunding as it allows quick and relatively easy access to the widest variety of potential investors. In addition the emergence of social media is propelling the development of crowdfunding as it allows organisations and entrepreneurs to pitch their project or enterprise to their social media networks and beyond.

The emergence of 'Open Source' data handling systems such as Apache Hadoop & Cassandra and MongoDB in 2007/08, have given a vital boost to the growth of Crowdfunding. These systems are able to handle; process and structure vast amounts of data from a huge range of sources including social media. This has resulted in the ability of online Crowdfunding platforms to assess the investor or borrowers' creditworthiness to a very high degree of accuracy in superfast time, which in turn has impacted upon due diligence processes and allowed crowdfunding to minimise failure and default levels, thus reassuring investors and those willing to lend or borrow via this source.

Over time Crowdfunding has developed into 4 broad categories of operating platform:

- Donation based
- Rewards based
- Peer2 Peer (P2P) and Peer to Business (P2B) Loans; and □ Securities or Equity based loans.

The first two platform types are more akin to charitable giving as investors do not expect to receive a monetary return for their contribution or investment, although they may receive an inkind reward or gift product. The latter two types are increasing called Investment Geared Crowdfunding (IGCF) because they channel finance to businesses and returns to investors, although in almost all cases equity investments assets are non-transferable. (See Figure 1)

According to the 2013 Crowdfunding Industry Report, there are now at least 800 platforms currently operating around the world, of which approximately 75 are UK based crowdfunding platforms, and at least a further 14 overseas based ones are open to UK citizens offering all four Crowdfunding models ([www.crowdingin.com](http://www.crowdingin.com)). However, NESTA's December 13 'Rise of Future Finance' reported that only 50 platforms account for 95% of all monies raised in the UK. This perhaps indicates something of the difficulty for start-up platforms to be successful and make an impact.

In April 2014, new rules governing Crowdfunding in the UK were introduced by the Financial Conduct Agency (FCA). Crowdfunding platforms of the donations or rewards type will not be regulated under the new rules but Loan based and Equity or Securitised platforms will become FCA authorised with the intention of limiting these particular models to sophisticated investors.

Figure 1 - CROWDFUNDING CATEGORIES:

	<b>FORM OF CONTRIBUTION</b>	<b>FORM OF RETURN</b>	<b>MOTIVATION OF FUNDER</b>
<b>DONATION CROWDFUNDING</b>	Donation	Social returns only	Wholly societal benefits.
<b>REWARD CROWDFUNDING</b>	Donation or Pre-purchase of product or services	Non-monetary reward in form of in-kind services or gift product samples.	Primarily societal benefits in addition to non financial gift.
<b>P2P/P2B CROWDFUNDING</b>	Loan	Repayment of loan capital only OR loan capital with interest.	Partially societal and partially financial.
<b>SECURITIES or EQUITY CROWDFUNDING</b>	Investment	Return on Investment in form of shares or profit over time.	Primarily financial motivation.



## 5. Crowdfunding Basics:

There are a number of basic rules that operate across Crowdfunding platforms. As a democratic form of finance, platforms allow the 'crowd' to make its own decisions as to what or who should or should not get funding, with the platforms acting only as the intermediary between the crowd and those that seek funds. This principle of **platform objectivity** is crucial in ensuring that the crowd acts as investors, advocates, contributors and supporters of what it wants to see happening and this is not mediated by financial 'professionals'.

Another basic principle is that of either the '**All or Nothing**' or the '**Keep it All**' approach. These relate specifically to the money raised. The former requires the project to meet its full target before getting access to the monies pledged. If that does not happen, usually within an agreed time period, the money goes back to the funders. In the latter case, the project gets access to the money pledged irrespective of whether it achieved the target or not.

When it comes to the cost of using a crowdfunding platform, there are only two or three fee structures in operation. At its simplest, platforms charge a **percentage fee** of the money raised. However there are additional costs to be paid by the organisations using the platforms e.g. Paypal costs or Credit/Debit card costs. As crowdfunding platforms develop so do the charging models. Increasingly there is flexible funding, especially in the 'Keep it All' platforms. Flexible fees kick in if a target is not hit; all money raised is kept but consequently the fee increases. So a platform might operate a range of different fees determined by the success or otherwise of achieving the agreed fundraising target. Most 'All of Nothing' platforms levy no fee if the fund raising target is not met and consequently all monies are returned to givers. (See Figure 2)

In the case of P2P, there is the usually a '**return of loan capital only**' or a '**return of loan capital plus interest**' approach adopted. In addition P2P is increasingly split into Peer2Peer lending and Peer2Business lending, with the latter a vehicle for the crowd to fund businesses and the former matching the crowd with individuals e.g. artists or inventors. In the case of P2P lending platforms fees are levied for their use. In addition borrowers pay interest rates directly to lenders. Since 2014, Investment Geared Crowdfunding (IGCF) (i.e. lending and equity models) operates within the UK financial regulatory environment (FCA) with the UK leading the way in developing the regulation for these types of platform.

The four different models appear to have consistent characteristics. IGCF platforms tend to be used to secure larger funds, with donation and rewards platforms used for raising smaller sums of money. Reward based platforms tend to get used by those in the creative industries be they film making, publishing or the arts and also by those organisations with products they can gift or use to reward financial backers. The donation based platforms are used predominately by charities or civic organisations looking for philanthropic givers.

Figure 2 – CROWDFUNDING FEES (Sample):

NAME of Platform	Type of Funding	Charges	Gift Aid Reclaimable
Buzzbnk	Fixed & Flexible Fees (Milestone System)	5% ( + 2% credit card fee or £0.37 debit card fee)	YES
		0% if target or 1 <sup>st</sup> milestone not reached & money returned to funders.	
Sponseme	Fixed & Flexible Fees	Fixed - 4% (+ reduced Paypal fees of 2.9% + 0.20 GBP)	NO
		Flexible - 9% if you reach target, 4% if not, (+ reduced Paypal fees of 2.9% + 0.20)	
Crowdfunder	Fixed Fees	8% (5% Crowd Funder, 3% Go Cardless). Paypal Fees paid by funder.	NO
		0% if target not reached & money returned to funders	
Indiegogo	Fixed & Flexible Fees	Fixed - 4% if you reach your target,	NO
		0% if you don't (+ 3% credit card processing fee)  Flexible - 4% if you reach your target, 9% if you don't (+ 3% credit card processing fee)	

## 6. Crowdfunding in Scotland:

There is very little research into Crowdfunding within the specifically Scottish context. However, looking at the UK context it is possible to extrapolate for a Scottish perspective. Although the UK is recognised as having the most developed market to date in alternative finance models, it is becoming clear that Scotland is lagging behind the UK in accessing crowdfunding opportunities. Despite the fact that the niche Scottish beer company Brewdog is recognised as a highly successful early adopter of Equity crowdfunding, there are still only four Scottish based crowdfunding platforms with at least two of them highly specialised in what they offer:

- ❖ ShareIn – Edinburgh-based only equity-based crowdfunding platform designed exclusively for UK technology and healthcare ventures.
- ❖ BloomVC – First Crowdfunding platform to be launched in Scotland when the majority of its early projects were Scottish owned. It aims to help start-ups, community projects and social enterprises find seed money through the crowdfunding model.
- ❖ Squareknot – Based in Glasgow, the first Scottish Crowdfunding platform to offer investors reward, equity and debt funding on the same platform to all UK companies.
- ❖ Crowd Racing – Based in Edinburgh the first Crowdfunding Platform in the world to offer racehorse ownership to the crowd.

NESTA estimates that £200million was raised via crowdfunding across the UK in 2012. Given that the Scottish economy represents about 8% of the UK economy, it should be the case that approximately £16million was raised in Scotland. However recent research for the Glasgow Chambers of Commerce indicated that less than £1million in such funding was raised in Scotland. This underutilisation of Crowdfunding as a vehicle for raising monies is common across all 4 models of Crowdfunding, including the donation and reward based ones used largely by the Third Sector. The research highlighted two principle issues:

- The lack of Scottish based crowdfunding platforms.
- The lack of a sophisticated understanding of crowdfunding: although general knowledge of Crowdfunding is similar to the UK level.

The scarcity of Scottish platforms could impact upon the visibility of Crowdfunding as a mechanism for raising monies, which in turn could partially explain the low take up level in Scotland.

## 7. Crowdfunding and the Third Sector:

NESTA's December 13 report calculates that for the period 2011-2013 there was an annual 20% average increase in the amount of money UK charities and social enterprises secured via crowdfunding platforms resulting in a total of £785m monies raised. In 2013 alone £310m was raised from donation based crowdfunding; £20.5m in reward based crowdfunding and a further £0.8m in community shares and microfinance.

These figures would indicate that crowdfunding does work as a way of bringing new monies into the wider Third Sector. The National Council of Voluntary Organisations (NCVO) would however dispute that Crowdfunding results in actual 'new' monies. It has recently expressed concerns about the potential 'Channel Shift' that might be occurring as a result of Crowdfunding which may involve donors moving from traditional methods of donation to Crowdfunding methods instead.

At a UK level there are some platforms that cater specifically for wider third sector organisations, but none of these provide the full range of support that third sector organisations require to maximise their chances of securing funding. Interviewees for this report who have experience in securing such finance were very clear that Crowdfunding is about more than utilising a platform to make a pitch. This is a point also highlighted by NESTA, which argues that it takes as much skill and effort to be successful at Crowdfunding as it does to successfully secure traditional grants and loans.

A few of the larger charities have adapted the Crowdfunding concept for their own use with Cancer Research UK one of the earlier adopters to set up the platform (MyProjects) in 2008. This allows donors to choose the type of projects they specifically want to support e.g. they can specify that their money should go towards funding childhood cancers. In 2012 Leukaemia & Lymphoma Research launched its own platform (Pledgeit). This allows supporters to create an online challenge and to draw in other potential supporters to that online challenge and pledge money to the charity.

Raising money via crowdfunding is very different to other forms of raising finance: a crowdfunding pitch is much more emotive, colourful and visual. It is likely to be based on a 2-3 minute video rather than a 100+ pages business plan and sophisticated use of social media is essential. This report will highlighted that these skills are relatively scarce within Third sector organisations and they will require assistance to master all the forms of communication required.

## 8. The Scottish Third Sector Experience:

### A. Awareness of Crowdfunding

One of the questions that this research wanted to answer was the extent of Crowdfunding awareness within the Scottish Third Sector. The research indicates that there is a high awareness level (90%) within the sector, but this has not translated into action or activity with less than 20% of respondents having actually undertaken a Crowdfunding campaign. This high awareness level may be explained by the fact that some survey respondents were given a brief overview of what Crowdfunding was prior to completing this survey. This was not to skew the results but to ensure that the respondents felt able to complete all the questions in the survey.

Interestingly this more or less mirrors the Glasgow Chambers of Commerce research into Crowdfunding and SME's which again showed high awareness levels at 76% but poor activity levels.

The low levels of actual Crowdfunding activity is not necessarily because people do not believe Crowdfunding is for them, rather it can be explained by the lack of real understanding about the concept and how it can be used by the sector e.g. a typical response was *'I know a little about it but don't know how it works'*.

The evidence would indicate that amongst those who answered 'Yes' to an awareness of Crowdfunding, there is a lot of interest with 19% currently considering using it and 58% considering using it in the future. So the low level of activity may perhaps be masking a time lag between awareness of, and actual engagement in Crowdfunding campaigns.

### B. Potential Income from Crowdfunding

The two largest Donation and Reward Crowdfunding sites are Kickstarter and Indiegogo. The average financial target for users of the Kickstarter site is \$5,000 or £2,940, whilst the average for Indiegogo is \$3,700 or £2,200, although averages, they are relatively small sums of money.

This is mirrored by the experiences of those Scottish organisations that have successfully engaged in Crowdfunding. They all secured their financial targets, although the sums of money sought were relatively small ranging from £500 to £15,000. Although their experiences have been very mixed, they did all indicate that they would consider undertaking another Crowdfunding campaign in the future.

Interestingly, of those organisations who, had not carried out Crowdfunding, but who indicated in the research that they are considering it, two thirds (62.5%) said that they were looking to secure under £20k, but just over a fifth (22.5%) said that they would consider using it to generate up to £50k.

Interestingly the French social Bank La Nef has recently launched a Crowdfunding platform *'Pret De Chez Moi'* to provide loans of between €3k and €25k. La Nef is very clear that it has taken this step because it is unable to provide these loans efficiently via the normal banking process. This reflects the lack of interest in the provision of micro loans by either mainstream banks or social banks and as such it would appear that Crowdfunding does have the potential

to work for micro finance loans and that most survey respondents have a preconception that it is at this level that Crowdfunding works best.

### ***C. Crowdfunding Returns to Donors/Investors:***

Senscot is particularly interested in the concept of Donations and Rewards based platforms as the principle of these Crowdfunding models is to have no financial return to the investors. In addition, since April 2014 they are also the unregulated parts of the Crowdfunding sector. However it is now common to offer a non-financial reward in the form of a product or service or experience to investors. It is also normal to offer different rewards for different sums invested.

Research for this Report indicates that about half of the respondents (51%) would be willing to offer a gift or reward in exchange for an investment. In some cases the organisations either already produce a product or have access to gifts that they can offer. Others, who do not fit this category, have to be more creative and innovative in their rewards e.g. one respondent would offer advertising space on their website if a local company give them some finance.

Interviewees of this study had all offered non-financial rewards to investors, these ranged from postcards to shelf space in a library. All felt that it is very important to offer a reward in order to attract finance. Although it is clear that it was easier for the creative based organisations to offer rewards, others engaged in more difficult issues such as homelessness struggled to offer a reward.

This was reflected in the survey responses where around a third of organisations (30%) felt unwilling or unable to offer anything in return for an investment. It is unclear if this is because they are ethically or morally opposed to it, or if they perceive themselves to have little to offer in tangible rewards because of the nature of their work.

What did stand out was that nearly half (45%) of respondents indicated that they would be willing to consider all different types of rewards/returns including financial returns for the right project and the right amount of investment.

## Scottish Case Study: Impact Arts



### D. A Scottish Third Sector Platform

The issue of whether or not there is a need for a specific Crowdfunding platform for the Scottish Third Sector is at the centre of this research. As stated above, there are a plethora of Crowdfunding platforms: some are run as social enterprises e.g. [www.Buzzbnk.org](http://www.Buzzbnk.org) and some are specific Donation and Reward platforms such as BloomVC and Kickstarter. Conversely, there are only four Scottish based platforms and the general level of Scottish engagement in Crowdfunding is low.

Survey respondents were very positive about such a platform with nearly 70% indicating they would use this platform to raise funds for their organisation. Just over a third (35%) of respondents would use a specific Scottish 3<sup>rd</sup> Sector platform to invest in other 3<sup>rd</sup> sector organisations either in an individual capacity or a Business to Business capacity.

The survey findings indicate that offering only a digital platform on its own would not be enough. Many organisations indicated that they would be more inclined to use a crowdfunding platform if it was offered with social media support and with support for developing a pitch and producing an effective video. If a complete crowdfunding package like this could be put together it and provided, it would be quite unique in the Crowdfunding sector where platforms generally offer little support. It would however be likely to have implications for the cost of using such a platform and may be viewed negatively by the just under half (43%) of survey respondents who indicated that if used they would be looking for the platform fee structure to be competitive with others.

The research interviewees had very mixed responses to this issue, with more than half indicating that were unlikely to use such a platform. Most felt where the platform is based is irrelevant in comparison to the social reach it had and a Scottish one might limit the audience. They did feel there could be merit in a 'Scottish' platform if it was able and willing to engage with the Scottish diaspora across the world and felt this could be a strong market for the platform.

These interviewees were also least enthusiastic about a sector specific platform arguing that this would limit the audience for the platform and therefore undermine its success. In addition some are clear that using the bigger more well-known platforms gave their pitch credibility and their investors' confidence. For a few interviewees, a Third Sector platform was too wide and they saw a need for a more narrowly defined sector platform e.g. a platform just for the arts and creative sector. However, the viability of a platform with such a narrow focus would be a concern.

### **E. *Obstacles and Concerns***

Despite the positive answers by the interviewees and respondents this study also sought to establish what are the main obstacles and concerns regarding the use of Crowdfunding by the Scottish Third Sector (See chart 1 below). These issues fit into four broad areas:

➤ **The support needed to make Crowdfunding work for Third Sector organisations.** Many organisations had concerns about their capacity to undertake Crowdfunding campaigns. This included a lack social media expertise: the need for assistance in the production of an effective video: making the pitch stand out from the competition and general support to get the campaign off the ground. This links to the point above that those potential users of a sector specific platform would expect to see additional support measures being offered whilst the fee structure remain competitive.

➤ **The perception that it is not suitable for all Third Sector organisations.**

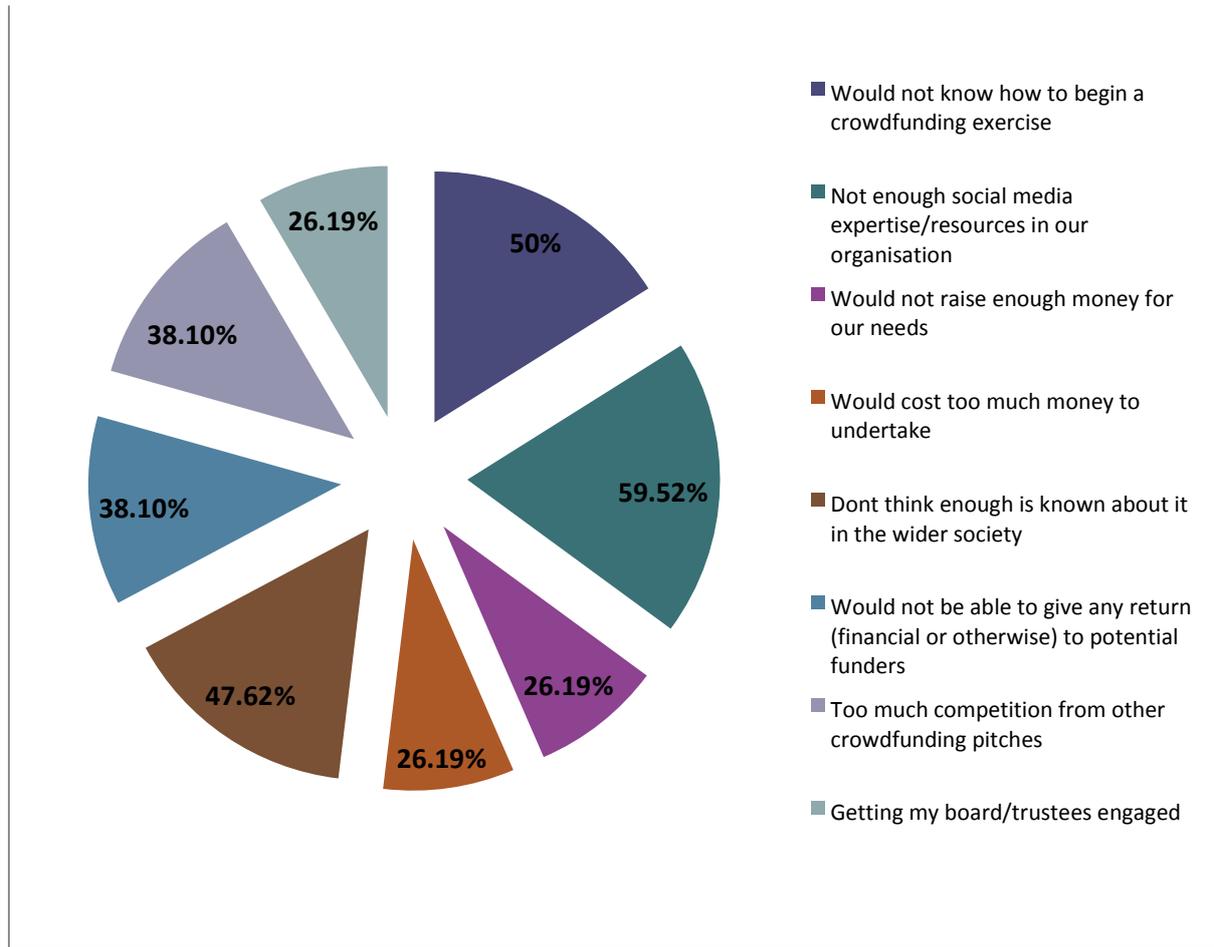
There is a general sense that Crowdfunding is not really suitable for all organisations - indeed the research does indicate that organisations related to the creative arts seem to do particularly well from Crowdfunding while other more mainstream organisations find it more difficult to make it work as a revenue source. Some of the respondents indicated feeling that they are not the type of organisation that could give appropriate rewards, or because they are dealing with quite 'challenging' societal problems that they are not attractive enough to be successful. In some cases, there is a view that Crowdfunding would simply not result in enough money for the project vis-à-vis the effort required to raise it.

The reality however, is that Crowdfunding is ideal for all Third Sector organisations, but there clearly is a lack of understanding on how to engage potential donors in more difficult projects.

Would suggest saying somewhere in the Report that this is very early days for CF – it is very new, very cutting edge, it is constantly changing and developing and innovations are constantly occurring within it – it is however here to stay and it will become an increasingly important

player on the world financial scene – the third sector needs to keep up with these latest developments the new opportunities that they provide – this is 21<sup>st</sup> century finance – you risk being struck in the 20<sup>th</sup> century if you do not engage with it.

**Chart 1 –CROWDFUNDING OBSTACLES AND CONCERNS:**



➤ **The lack of real understanding about Crowdfunding and how it works.**

Although 90% of respondents had heard about Crowdfunding, their level of understanding is very superficial with many organisations seeking clarity and more information on how it could work for them e.g. ‘*what is the difference between Crowdfunding and Community share offers?*’ However the study also showed that organisations felt that Crowdfunding understanding or awareness is low amongst the general public and consequently not enough people would engage with it to make their pitch successful.

➤ **The disincentives of Crowdfunding.**

Those organisations that had undertaken a Crowdfunding campaign are very honest about the potential drawbacks to using it. Financially as figure 2 above shows is it not a cheap option and claiming GiftAid on donations is difficult. Organisationally it is not an easy option and it takes a lot of organisational resources to be successful as indicated in the Impact Arts case study above. What is obvious is that whilst boards and trustees were broadly support and in some cases individual Trustees pledged some money, there did not seem to be an understanding

that for Crowdfunding to work the networks of everyone associated with the organisation had to be maximised, including the friends, family and networks of all concerned. There are sales and 'pester' power aspects to the process, particularly in relation to close friends and family that some found difficult to manage and that utilises significant staff hours. Data from the Wharton Business School evidenced that 81% of investors or donors are connected to people in the organisations at the first or second degree of separation. Finally, there is considerable competition from other similar projects on the platforms that makes it vital that organisations stand out on the platforms.

➤ ***Non-financial benefits of Crowdfunding***

It is apparent from those with experience of Crowdfunding that while all of them had undertaken Crowdfunding with a view to securing additional monies they were surprised by the non-financial benefits to it. Most did not anticipate these before the Crowdfunding campaign and did not plan for their positive impacts.

These benefits were primarily in the area of PR; publicity and additional traffic to websites or additional followers on social media. The Impact Arts case study is a very typical example of the format these benefits can take. During their campaign they got 100 new Facebook followers; 400 new Twitter followers; 2100 visits to their website and they were featured in 11 publications including a full page article in the London Times.

In order to maximise this type of publicity such benefits have to be anticipated from the outset and strategies put in place to keep these new supporters engaged with the future activities of the organisation concerned. Most of the interviewees recognise now that Crowdfunding is as much, if not more, about raising the profile of the organisation as it is about securing new income.

## 9. Conclusion:

The withdrawal of financial support by mainstream banks due to the financial crisis coupled with the decline of grants resulting from government austerity measures and the increasing presence of private investment agencies is shaping the financial landscape of the Third Sector. Hence this report is particularly timely in relation to the ongoing wider political and organisational discussions on how to finance the Scottish Third Sector into the future.

It is clear that technological advances have made it much easier to secure financial support through the internet and Crowdfunding is one important new way of doing it. It would appear that donation and reward type platforms are particularly useful for raising microloans. There is significant money flowing into the UK Third Sector from Crowdfunding activities. However Scotland would appear to be lagging behind in utilising this method to secure additional resources.

The survey findings indicate that the Scottish Third Sector is aware of the Crowdfunding opportunity and would try it as a means of securing new monies. However, many of the survey respondents felt that within their organisations they did not have adequate information, knowledge and expertise needed to engage successfully with it. The creative/arts based organisations seemed to be more comfortable about their ability to undertake a successful Crowdfunding campaign, but this confidence tailed off when the organisation was addressing 'harder' social issues such as homelessness or drugs. It is clear most would need assistance beyond merely the provision of a platform to be successful in any future campaigns.

Going forward, if the Scottish Third Sector is to catch up with the rest of the UK in terms of Crowdfunding income then it needs support to do so. Crowdfunding requires a whole new skillset and expertise that are currently lacking in the Third Sector, in particular engaging potential donors or investors via social media. As such, just providing a platform and driving potential investors/donors, to it would not be enough and the following points will need to be considered:

- A new sector specific platform would need to recognise its role in up-skilling the sector to order to maximise potential financial success.
- Additional support measures would need to be present such as support with making an interesting pitch and/or assistance with social media.
- This approach would have an impact upon the timescale required for the platform to achieve financial sustainability.

The cost of providing this 'added value' platform would be significant. It will require at least 2 'creative' staff skilled in social media and an administrator with a potential cost of £80k. An alternative might be to contract out the social media support to another organisation with that expertise in house, thereby reducing the core staffing costs to 1 administrator.

Then there is the cost of developing a highly technical sophisticated Crowdfunding platform with sufficient inter-activeness and accessibility to compete with existing platforms. The cost of designing such a platform is likely to be significant. One option of keeping costs low would be to consider 'white labelling' an existing platform such as Buzzbnk rather than establish a whole new platform. White labelling is where an organisation leases or purchases a fully supported product or service from another source, applies its own brand and identity to it and then markets it as its own. This option could offset the cost of designing a whole new platform.

If additional support measures were available and the fee structure was competitive many respondents indicated they would consider using a new Scottish Third Sector Crowdfunding platform. A final determining factor in the success of such a platform would be the extent to which it could reach the Scottish diaspora as the most experienced organisations felt this wider reach is crucial to organisations successfully securing the required investment.