Project Owner

Risk category: GENERAL

#1 - Limited knowledge on alternative finance

Definition

Alternative finance is an economic dynamic characterized by specific procedures, particular actors, different timing and budget structure. Crowdfunding, in particular, is not a homogeneous practice and the success of a campaign depends on the choice of the most appropriate platform and co-funding type (donation, reward, equity or lending). Making the wrong choice, in these terms, might lead to not reach the funding goal or can prevent from using this precious resource to its full potential.

Mitigation strategy

Awareness creation, training and education about CF and alternative finance is indispensable, as it prevents to be unprepared via à vis the specific funding dynamics. Such training can also empower with further and parallel skills that might be useful in the broader job-market, such as communication and managerial attitude, business planning etc.

Many specialized services and ad hoc coaching sessions are also offered by professional agencies or by the platforms themselves. Always trust service providers with proven reliability, experience and professionalism. The choice of a platform suitable for the business model and product in question is essential. In case of fledging crowdfunding activity, it is always a good practice to opt for a platform that provides support and help all along the process.

In case of multi-national platforms, make sure to have a person or office of reference in the country of activity, with the possibility of scheduling periodic meetings, chats and calls, in order to follow the development of the CF campaign. Administrative and procedural support - and the easiness to find the bureaucratic documents and processes on the platform is key to smooth the launch and the management of any CF campaign.

In case of limited business experience, hiring a risk management consultant is a good investment for most companies. A consultant can analyze a business and determine which risks might be faced and which strategies to apply in order to avoid them or reduce their likelihood.

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Project Owner

Risk category: FINANCIAL

#2 - Underestimation of costs

Definition

Crowdfunding differs from a normal production activity as it requires for diverse unusual extra costs, which are sometimes difficult to spot and calculate, or to take into appropriate account in the budget.

In fact, in addition to fixed production costs related to raw materials, human resources and services providers, there are high costs of initial capitals, in terms of investment in pre-campaign, campaign-maintenance, post-campaign activities. Among these, the delivery-cost of rewards, the social media campaign fees and sponsorships, the changes embodied in small-scale production... Additionally, the platform-related fees largely impact on the final funds collected.

Mitigation strategy

The careful preparation of a thorough business plan - budgeting and expenses forecasting- is indispensable, considering every single phase and aspect of the campaign. A good support by the platform is useful and necessary, as their advice can better define the business strategy and timing of funding completion.

Focus on: Platform's affiliation fees

Choosing for one platform or another can strongly make the difference in terms of final financial goal. In particular, due to the impact of the platform's affiliation fees (flexible/fixed fee option) and on the shares related to the payment provider or extra services...

It is also to consider which approach the platform chooses to refund the project owner of the collected money. It is to differentiate between an "all or nothing" or a "keep it all" approach. In the first case, reaching the total funding goal is binding for the transfer of all the collected money from the supporters, by the platform to the project owner. Such a solution is to be chosen in case of high investments linked to few activities - as it is, for example, with highly-specialized products, whose development implies very large investments in terms of manufacture or technology. The second method allows the project owner to directly get a certain and proportional amount per each and every contribution gathered from the crowd. This is particularly useful when even small amounts can make the project progress and develop.

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Project Owner

Risk category: FINANCIAL

#3 - Unpredictable market factors

Definition

Crowdfunding can be adopted in order to reach different aims, among which gathering feedback on the product, testing the market and proving a brand concept. Nonetheless, it is it is efficient only if anticipated and supported by a **careful market analysis and positioning**.

It is a practice also based on the crowd's emotional affection and attitude - which is not easy to predict. In the case of bad estimations concerning the demand, the appeal and the real value of the product to crowdfund, the campaign is a really missed chance!

In parallel, if the product lacks of brand or identity, it is more exposed to face high competition in the internet's broad and hidden market. Framing potential competitors is also key to better define the offer's success.

Furthermore, during the campaign, some unforeseen and situations can happen. Competing products might emerge, the economy freezes, a crisis occurs... "Murphy's law" and butterfly effects are difficult to predict and even less desired – still, unplanned events might strongly affect the campaign outcome.

Mitigation strategy

Deeply analyzing the market and the surrounding economic context helps frame the competitors, the attractiveness and demand of a certain product. This includess an accurate mapping of the territorial chances and gets hand in hand with a complete outlining of the crowd in terms of affiliation and motivation towards the product/brand.

A careful screening of the firm's potential and internal competencies is also essential, in order to concretely frame the production abilities. It is to remember that "**Intention to produce ≠ Ability to produce**"!
A solid internal structure and a confirmed collaborative attitude is also helpful in order to face contingent changes.

It is nonetheless suggested to not only rely on crowdfunding for the production or the fulfillment of an economic objective, envisaging other scenarios and funding options.

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Project Owner

Risk category: GENERAL

#4 - Reputational damages due to unfulfillment

Definition

There might be many reasons that prevent a campaign to be successful: limitations of technical nature, market- or business-unreadiness, unstable internal management.
Failing to satisfy the initial promises might happen, but it is even worse if the crowd of supporters is not kept informed about the campaign development. This will make the entire firm look non-trustable and hinder the future business initiatives.

Mitigation strategy

Setting **realistic and reachable goals** (in terms of requested amount, timing and production capacity) is essential for a successful crowdfunding campaign.
In parallel, regular exchange information and updates with the crowd about the project developments are key in order to build a trustworthy identity.
Always keep the crowd in the loop about the initiative's state of art, both on the social media and on the crowdfunding platform!

Focus on: Communication with the crowd

One of the main elements of a crowdfunding campaign are the supporters, the financial contributors to the product or initiative developments – also defined as "**crowd**".
Understanding who these supporters are, their degree of affection to the product / initiative and a careful mapping of their presence on the territory will make the strategy more precise in terms of communication, timing and location.

Such an identification allows for understanding their needs and drawing a product that is respondent to the market but also cohesive with the firm's identity! Aditionally, it is also to remember that even the platform itself might have a crowd of reference and its network in which to create synergies and carry out ad hoc dissemination activities, in order to spread the voice about projects with high potential of success.

- Define the crowd, i.e. the target audience, stakeholders and market
- Benchmark the network of reference
- Frame the channels and tools to deploy for a fruitful communication and constant support
- Mainstream the presence and responsiveness on social media

The communication with followers enables to generate the promo momentum and builds up trust within the community of reference. Replying to questions, comments and suggestions from supporters does also count for confirmation of reliability. The possibility to organize events and offline / 'live' activities is also to be considered as to make the broader group of stakeholders know about the project and make hands-on experience of its strength points.

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Project Owner

Risk category: FINANCIAL

#5 - Exit strategy & fluctuation of cash flows

Definition

The exit strategy is the moment in which a larger company, a venture capital or a “business angel” absorbs or buys the start-up out. This implies for the smaller firm to be included within a broader production, investment or market spectrum – and ensures the innovative product or idea higher chances to survive. This happening is not certain or predictable, even if sometimes awaited or presumed. In practical terms, though, the success of a business cannot be assured merely by external purchase.

Additionally, if and when the exit happens, the economic value of shares might have varied since the initial appraisal – shares and investments can worth differently along the crowdfunding campaign, mostly if it takes longer than few months. It is to consider, in fact, that an investment may take up to 4-5 years to return into the investor's pockets.
During this time, the economy and the market change, resulting in a different appreciation of the capitals invested.

Mitigation strategy

An accurate market risk assessment and business valuation optimizes the project profitability and help estimate the average **return on investment** that could be expected, based on returns generated by the wider market. It is necessary to determine the **economic value** of a certain company unit and exit sale value, so to establish investors' rates of ownership and future taxation.

Estimating the **average market return** can help companies minimize total cost of capital, while providing the investors with a sense of real appreciation of the expected returns from their assets or shares, in comparison to the risk.
At the moment of an exit, these calculations permit to establish the **liquidation value** that investors will receive as their assets are liquidated and liabilities paid off.

It is highly suggested not to only rely on the happening of an exit/purchase. Being prepared for different scenarios and ready to embrace a “**Plan B**”, remembering that without an adequate business plan and support structure, even promising ventures can fail. In order to maintain a good and reliable reputation with the crowd of investors, it is good practice to envisage for them different financial options already in advance, in order to protect, guarantee and satisfy minor investors too – e.g. foreseeing the so-called **tag-along** option.

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Project Owner

Risk category: LEGAL

#6 - Intellectual Property Right & Copyright infringement

Definition

One of the key benefits of crowdfunding is that is enables highly-potential innovative projects and creative ideas to reach out and be supported by the wider public.
The internet, nonetheless, is not only a sea full of possible new backers and investors, but also of little sharks, competitors and spies, who might imitate the particular features of any given new product, replicate them and even put a patent on them.

If this happens within the frame of a larger-scale and more stable production activity, the short-term result will be the failure of the campaign, while the long-term one might be the loss of market shares and future investors.

Another peculiar issue that links crowdfunding to copyright is the use of particular media materials during the campaign. In fact, copyright infringement could occur in the event that a video, image, soundtrack or digital content is deployed without the necessary permission or license from its owner/creator. This violation would lead to a shutdown of the campaign or even to a lawsuit.

Mitigation strategy

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Project Owner

Risk category: LEGAL

#7 - Uneven or unclear regulatory system

Definition

Launching a project on a foreign platform might be attractive as it opens up to broader markets. Nonetheless, the lack of an international or EU-wide common crowdfunding regulation makes it unclear which law is to apply: the one of the SME's seat? Or does it depend on the platform? Or, even, on the supporter's location?

Same confusion might arise in relation to taxes. The latter, in fact, most of time depend on the national regulation, thus the fiscal impact or absorption of the investment may vary and not be clear in case of cross-border activity.

Lack of coordination between legislations in different countries and a scarce guidance on applicable fiscal regulation could result in market fragmentation and law-breach, even unintentionally.

Respecting the platform's fundraising terms and conditions is also key. Campaigns that run afoul of these rules may have their campaign suspended. Alternatively, they may face difficulties in accessing their funds, even if the campaign meets its targets. Either scenario represents a monetary and reputational distress.

Mitigation strategy

Ensuring a deep and careful review of the business and legal plan against the chosen platform's rules is essential before launching any campaign. Make sure the platform displays:

- legal framework
- the authority of reference
- division of responsibilities
- contractual details / obligations

Such information are an indicator of reliability, as they prevent future fiscal or legal issues: ensuring a fair campaign development towards supporters and firm is essential to protect brand, product, money and crowd.

Focus on: the European Crowdfunding Service Providers (ECSP)

In order to better coordinate and make the diverse national legislation uniform, a new legislation has been proposed and is being adopted by the European highest institutions. It is the European Crowdfunding Service Providers (ECSP) for Business Regulation - COM(2018)0113 – C8 0103/2018 – 2018/0048(COD), which has the potential to make **pan-European crowdfunding** a reality.
Such regulation will harmonize the legal framework for the sector, offering a well-defined and structured legal skeleton for the activities of crowdfunding for business (lending and equity) all over Europe. The main innovations will be :

- A **single set of rules** will apply to crowdfunding services in the EU, up to € 5 000 000
- Strict rules to **protect investors** from financial losses
- **Member states responsible** for authorizing and supervising crowdfunding providers

At the present, the regulation's details are still to be finetuned and technical work on the text is under way. The law Is expected to come into effect in 2021. This accomplishment will largely ease the crowdfunding process for all the involved actors, thus largely benefit European startups and SMEs and to European investors.

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