

Crowd Funding For Startups in India

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Abstract: *Startup companies are newly founded companies or entrepreneurial ventures that are based on innovation, development and market research. Most startup companies seek to avoid bank loans as they are usually related to complex procedures and are given based on company's property or credit history. As investment modes are changing and evolving some new sources of investment for startup projects. In this paper we discuss the prominence of crowd funding as a mode of financing for startups. The various forms of crowd funding provide new ways to fund startup from the earliest days until very late in the development of the company. This Research introduces meaning, different forms of crowd funding suitable for startups. Analysis of merits, cautions to be taken and risks involved in crowd funding. Selection criteria of crowd funding from the view of capital seeking companies like startups. India as a developing economy can motivate investors for crowd funding. The extent the startups succeed in attracting Indian investors.*

Key words: *Startups, Crowd funding, Investors, India.*

I. Introduction:

Finance is an important factor for the growth and development of a company. Modes of financing depend upon the nature of the company and the risk involved. Startup is a company started by an individual or by a handful of entrepreneurs. As startups are initiative program by central government to motivate an individual to become an entrepreneur. Central government provides tax relief measures which encourage young industrialists. Online transactions facilitate not only marketing the products but also alternative sources of funding for the startups or ventures. In this Research paper we will discuss about how a startup is funded through crowdfunding.

Literature Review:

Crowdfunding main source of literature is from the research analysis of Professor Ethan Mollick "The dynamics of crowdfunding an exploratory study". Mollick Research study attempts to identify what makes for successful crowdfunding campaigns and how shared geography and personal networks. By using the source in this paper an attempt is made to know about crowdfunding platforms in Indian context. The startups are new ventures but how the startups were reinvented. NASSCOM data, World Bank report and journal papers about the crowdfunding are information gatherers for this Research paper. This paper made an attempt to study about crowdfunding as source of fundraiser for startup. Paper discuss about the guidelines given by SEBI for protecting the investors in India and the effects.

1.1 Objectives of the study:

- Crowdfunding meaning and platforms.
- Startups and their growth and modes of funding.
- Coverage of crowdfunding for startups.
- Review of crowdfunding from Indian context.

II. Methodology

Meaning of crowdfunding

Crowdfunding is the concept of funding a venture, project or a startup by way of raising money from multiple investors through an online platform. Crowd funding is online funding by unknown investors. Crowd funding platforms are used to raise money in form of equity, debt or donations. Among the various ways of funding most popular are venture capital, seed capital and crowd funding. Venture capital and seed capital are difficult to access for startups. Crowdfunding provides low cost of capital and higher returns for the investors. This made crowdfunding safe option for raising capital for startup's having less capital funds. Crowdfunding platforms are classified into four categories. They are

II.I. Donation based crowdfunding:

In donation based crowdfunding campaign funds are raised for charitable projects, disaster relief and non profits organizations. Donations are accepted from a large number of people in small proportions. People can avail an opportunity to share money towards a social causes. In this platform they is no financial return for the investors there is no chance of loss of investment. Ex. Indiegogo,

II.II. Reward based crowdfunding:

In this platform investors receive rewards in return for their investment. This can be product or service the company offers as token gift. In order to impress investors companies attract with different types of rewards as incentives .In Reward based crowdfunding the investors are not availing financial return. Ex: Kick-starter

II. III. Debt based crowdfunding (also known as “peer to peer”, “P2P” or crowd lending):

Companies can apply for debt on these platforms. Debt based crowdfunding platforms review and launches it online for funds. Online application for fund includes company’s interest rate, credit period and risk involved in the securities or bonds for sale. In return for the securities the investors get interest on these unsecured loans. Debt is repayable after a fixed period by the company. Ex: in UK are Zopa, Funding Circle etc.

II.IV. Equity based crowd funding:

On this platform investors receive equity shares of the company in proportion to the money invested. Investors in return receive financial return on their investment. They receive a Share of the profit as dividend. In this form investors are prone to more risk as they are treated as investing in an unlisted company. Every country has its own set regulations regarding the investments through these crowdfunding platforms. Examples of equity crowdfunding platforms are Equity net, Syndicate Room, Crowd cube and Seedrs.

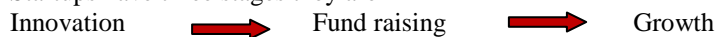
Reward and Donation based crowd funding are not related to financial gains so they is no chance of loss of investment. They are known as community crowd funding. Equity and Debt based crowdfunding face threat from the loss of capital, promise financial returns on investment. They are known as financial return crowd funding. Investors from this platform aim at returns once company establishes themselves and enjoys profits.

Some of the Indian websites are Impactguru, Milaap, ketto, wishberry, bitgiving; Fuel a dream & Dream wallet which successfully raised funds through crowdfunding platforms. Impact guru raised funds worth of 329 cr through online platforms and became India’s largest online fundraiser.

III. Meaning of Startup:

Founded by Indian origin individuals and which have its headquarters in India and major part of the product development centre is in India. Any company incorporated under company’s act 2013 less than 7 years from its incorporation. A company with annual turnover not exceeding INR 25crores in any preceding financial year, working towards Innovation, Development or Improvement of Product, Procedures.

Startups have three stages they are



III.I Crowdfunding as mode of finance for Indian startups:

Reforms and relaxation in Indian economy, large domestic market, availability of large workforce act as initiatives for startups. According to World Bank’s doing business report India’s ranking has improved from 130 (2015) to 100 (2017) in “ease of doing the business”. Cut or simplified post-registration procedures such as tax registration, tax relief measures, social security registration and licensing made startups or ventures are the factors for the improvement in ranking. Removing the minimum paid up capital and requirement of company seal made startups are more attractive. SPICe form is introduced for name registration and incorporation of company. With this they also obtain TAN, PAN and DIN. With these capital requirements of the startups enlarged. Startups introduce an innovative product or service in the market. The market response for their products is depends upon the acceptance of consumers. If they fail to attract consumers they are going to incur losses. As per Basel III norms banks have to maintain certain capital reserves. Because of this norm banks unable to fund startups for which success rate lower. Private equity, Venture capital and crowdfunding fill the space created by banks and provide funds for the startups. Debt based crowdfunding comes under the control and authorization of RBI. Equity based crowdfunding will become a best alternative sources of funds for startup or ventures. As a result startups are successful in their projects. India ranked 3rd amongst top 5 global list of startups growth and able to raise funds more than 4,200 cr. 35% of new startups are formed in Tier 2/3 cities this shows not only urban areas other semi urban areas also opting them. As a result a significant growth in the

economy is indicating. Startups success rate is 10% in India and 90% of startups are closing the ventures due some difficulties. Startups have three stages they are

Innovations → Fund raising → Growth

They are more than 5000 startups are India which are incorporated less than 5 years. Funds raised for startups in India from 2014 are increasing but reduced to USD 160mn in 2017. This shows downward trend in fundraising for startups. The causes for the same will in 2014-15 they got enough funds which were not utilized properly and easy availability of funds attracted more startups. This leads to tough competition among startups which made less innovative ideas and copying of innovations discouraged investors. In order to boost investors SEBI allowed equity crowdfunding by making certain alterations suitable for Indian investors.

III.II. Approaching towards crowdfunding campaigns

- The campaign is invitation to the investors for contributing towards venture/project. Startup has to approach the crowdfunding platform that will fulfill the requirement.
- They must have idea which is possible in every attempt and obtain a copyright. Clearly mention the purpose for which they require funds and present it in a creative way to attract investors.
- Fix the target fund minimum, so it can be easily reached. Surplus will be a bonus for the company. If target is maximum and not reached some sites will refund them to investors.
- Launch campaign about the venture on a single website, multiple websites will confuse the investors, can split the contribution.
- Campaign time for funding between 30 to 45 days. With this period startup have enough time to update about details. If the lengthy time is given campaign becomes less effective.
- When they campaign on sites they have to clearly mention the rewards for the investment. This is the point investors always look out while going through campaign.
- Communicate with your investors updated on every single development related to the venture or project. Maintain schedules for every aspect of campaign like press releases, posting updates etc.
- Crowdfunding campaigns are to be organized with perfect strategy i.e. planning, marketing and executing the campaign. The success of fund rise depends upon the how you win the faith of the investors.

IV. Crowdfunding Indian scenario:

An entrepreneur or a startup company wanted to rise for their project or venture they must register and add their projects to <http://buckscapital.com>. In their projects they have mention about the purpose for which they require funds and the how they spend it, the time slot of campaign and the rewards for the investment. The way the company is making correspondence with the investors. Crowdfunding is a new concept for Indian investors. Usage of internet for raising capital requirements is very low compare to western countries. When traditional financial system failed to support startups this alternative cropped up. Online marketing & online payment options made Indian investors accessible to crowdfunding ways. India is the second largest in operating the internet market. Now with the startups initiative and how to get funds made crowdfunding familiar. As per World Bank report 2012, India has only 10 crowdfunding platforms compared to 344 in the US and 87 in the UK. Business report estimates nearly to 200 companies have raised INR 35,057,840- INR 45,074,366 on these platforms over the past 18 months. Founded in 2005, Equity net bills itself as the “original equity crowdfunding site” and claims to hold the only patent for the concept. Many startups which are successful as well as innovative are merged and gone through acquisitions with the corporate entity. As many as 60 startups are already merged with large companies. Indian and Foreign companies are engaging with startups through collaboration, accelerations and investment...

IV.I. Websites used in India:

- Catapooolt – <http://www.crowdfundinsider.com>
- Lgnite intent – <http://igniteintent.com>
- Ketto – <http://ketto.org>
- Pick a venture – <http://www.signup.pikaventure.com>
- Start 51 – <http://www.start51.com>
- Wishberry – <http://www.wishberry.in/>

The following are the startups (Table I) raised funds through crowdfunding platform:

Table I

Startup	Year of incorporation	Crowd funding platform	Regions covered	Funds raised	Product
Sector gube	2011	N/A	Kerala & US	USD 125K	IOT product, MAID
Digital Gorkha	2015	Angel investors	Pune	INR1crore	Online visitor Registration app
▪ Swiggy	2014	N/A	Bangalore	\$155 million	Swiggy app

- Swiggy app which was named as best start up of the year by Economic times of India. And also the Best startup India is Swiggy app which was funded through crowdfunding.

IV.II.SEBI guidelines:

- In India considering the need for the funding source for startups and also to save Retail investors form the risk of startup companies SEBI has proposed to allow only Accredited Investors to participate in crowdfunding.
- These include QIB’s (Qualified Institutional Buyers), Companies incorporated under the companies act 2013 those companies whose minimum net worth is 20crores.HNI’s (High Net Worth Individuals) with a minimum net worth of Rs.2crore and Eligible Retail investors (individual investors with small investment)
- Collectively, QIBs will need to hold a minimum of 5% of the securities issued and a company will be required to purchase at least 4 times the min offer value per person. A high net worth individual is required to purchase at least 3 times the minimum offer value per person.
- Retail investors include those who can avail services of portfolio manager or investment advisor. Whose annual gross income is more than 10 lakhs and should have filed the tax returns for last 3 years. Those investors having sufficient resources with them they can face the loss, certify that upto max Rs.60000 in an issue through crowdfunding. Retail investor’s overall investment in a year should not exceed 10% of their net worth.

IV.III. Limits for crowdfunding investment:

- Startup is incorporated under company’s act 2013 in India and having business as head office located in India and can have branches globally. Startup is not listed in any of the stock exchanges.
- A person is eligible to become an investor only if he is citizen of India or a NRI. Investment is done through Demat account. Payment has to be made through a DD or Cheque. Payments by cash and credit cards are not authorized.
- Startup must be less than 4 years old and cannot raise money more than Rs.10crore in a year. SEBI will allow private investment through crowdfunding platforms to any number of QIB’s and a maximum of 200 HNIs and Eris investors combined.
- A company must not be a subsidiary or not related to any other company whose turnover is more the Rs.25 crore. Companies not allowed raising capital from multiple platforms, and must issue through SEBI recognize crowdfunding platform. A company which is not engaged in real estate and activities which are not permitted under industrial policy of Government of India are not allowed to crowdfunding investment.
- The companies should not have directors, promoters or associates mentioned as a ‘defaulter’ or a ‘willful defaulter’ by RBI or CIBIL. The company interested in crowdfunding should also provide provisions for oversubscription.
- Single investor is not allowed to hold more than 25% stake in the company and the promoter(s) shall be required to maintain a minimum of 5% equity stake in the company for at least 3 years.

V. Conclusion:

As per World Bank report regarding protecting minority investors India was in 4th rank compared to 13th rank in 2016. This made India more attractive for the startups with ease of doing the business.

V.I.Benefits of crowdfunding:

- Crowdfunding provides a new alternative to traditional financial operators for startups. They can raise capital or credit at low cost without complicated procedure. They created tough competition for traditional financial operators.
- Startup’s can campaign online in creative way than any other company. By launching a campaign on crowdfunding platform startup’s can measure its marketability at early stage. By choosing crowdfunding platform startup or venture can reach thousands of accredited investors who are willing to invest. They can utilize the online marketing opportunities fully. Introduce overall mission and vision to the market.

- Invitation for the funds on these platforms is free or minimum charges applicable compared to bank loans and venture capital charges. The fee paid for the services of this platform is minimum percentage of the investment amount received.
- Crowdfunding created a new product for the portfolio of investors. All the documents and related information is kept updated online for investors. This makes investors secure and connected. Investors can access the startup's position, risk.
- The venture can access the situation from the point of investors. They can directly contact the investors online and errors can be rectified.
- Many platforms return the money from investors if the minimum goal is not reached. This makes startups easy to step back.
- Startups can Avoid accumulating debt or give up equity through crowdfunding. Both can be diversified.

V.II. Limitations:

- Equity crowdfunding raises huge sum which can lead to money laundering.
- Crowdfunding platforms are risk for investors as investment through this platform is as investing in unlisted companies.
- Risk of default by the ventures on crowdfunding platform is higher. There is always a risk related to closure of crowdfunding platform suddenly leaving investors and borrowers in loss.
- Risk of liquidity as there is no secondary market for the investors on this platform. Which makes entry is easy but exit rigid. Liquidity of the investment is very low compared to the other traditional modes of finance for companies.
- Crowdfunding platforms accumulate funds from multiple small investors (Retail investors) the risk of default can be difficult for these Retail investors. Because of this SEBI's rules allowed only selective investors allowed on these platforms.
- Risk of online frauds or cyber attacks because of online payments for investment. Lack secrecy is a major threat for any venture. Unless the idea has copyrighted startups cannot invite funds on this platform.

Startups can raise funds through crowdfunding platform smoothly. In India equity based crowdfunding is going through lot of scrutinization. SEBI wants to protect these investors as they are unaware about the limitations. Equity and debt based Crowdfunding platforms are subject to laws of region. SEBI also analyzing the situation as startups are raising funds the failure chances of these ventures is 90%. Angel investment in seed stage startup in India is decreased by 53% in 2017 as compared to 2016. The investors must be ready to face loss of investment. This can make adverse effect on the Indian economy. Many universities in India are setting up startup programmes which encourage student startups. This is first step towards creating awareness about startups as well as online investment like crowdfunding. Because of this the investment pattern of investors is going through changes. India as a developing country has many potential entrepreneurs and investors. India grown up as 3rd largest startup base giving tough competition globally.

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