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Crowdfunding Without the Crowd

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The final crowdfunding rules took three years for the Securites and Exchange Commission to pass, but crowdfunding—the offering of securities over the Internet—is now a reality. But now that crowdfunding is legal, will it be successful? Will crowdfunding be a regular means by which new companies raise money, or will it be relegated to a wasteland of the worst startups and foolish investors? This Article argues that crowdfunding has a greater chance of success if regulators abandon the idea that the practice does (and should) employ "crowd-based wisdom." Instead, I argue that crowdfunding needs intermediation by experts that mirrors the successful forms of entrepreneurial finance (e.g., angel investing and venture capital) that have preceded it.

The final Securities and Exchange Commission rules move us in the right direction. At the heart of the crowdfunding experience lies the "funding portal," or the website that will actually list the startup as an investment opportunity. Funding portals were originally conceived of as almost completely passive entities who could not subjectively "curate" (or screen) the startups that wished to list on the sites. The final Securities and Exchange Commission rules permit some funding portal curation, which will allow funding portals to list, on the whole, companies with a better chance of success for investors to choose from.

This Article argues, however, this permitted curation does not go far enough, given a funding portal's justified concern over becoming a broker-dealer. Thus, I suggest ways in which expert investors participating in crowdfunding offerings can and should use a site's message boards and investment clubs to further guide unsophisticated investors toward better investment choices. At the same time, I acknowledge potential liability concerns for experts who do so. Together, on balance, careful curation by funding

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portals and nudging from expert investors will give crowdfunding a better chance of facilitating market successes while improving investor transparency by offering heightened guidance from industry experts.

INTRODUCTION

Crowdfunding is now a reality. In October 2015, after a several-year wait, the U.S. Securities and Exchange Commission ("SEC") promulgated final rules to implement Title III of the Jumpstart Our Business Startups ("JOBS") Act ("Regulation Crowdfunding").[1] "Startup" companies can now use the Internet to offer securities to any investor with Internet access.[2]

1. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, §§ 301–05, 126 Stat. 306, 315–23 (2012) (codified in scattered sections of 15 U.S.C.).

2. A definitional problem tends to arise when writing about entrepreneurship. Gordon Smith and I situate opportunities at the heart of entrepreneurship and define entrepreneurial opportunities as "the subset of market opportunities that involve some form of novelty or innovation." D. Gordon Smith & Darian M. Ibrahim, *Law and Entrepreneurial Opportunities*, 98 CORNELL L. REV. 1533, 1540 (2013) (citing SCOTT SHANE, FOOL'S GOLD? THE TRUTH BEHIND ANGEL INVESTING IN AMERICA 39–41 (2009)). That means I am usually writing about companies with some sort of high-tech innovation; but as noted later, most of the initial crowdfunding offerings are lifestyle or alcoholic beverage companies. *See infra* note 117. This is still a novelty, just one in the "weak sense" rather than the "strong sense." *See* Darian M. Ibrahim & D. Gordon Smith, *Entrepreneurs on Horseback: Reflections on the Organization of Law*, 50 ARIZ. L. REV. 71, 84–85 (2008) (citing Smith & Ibrahim, *supra*).

I have previously written about crowdfunding.[3] My prior article took a comprehensive look at crowdfunding's evolution and its place in the entrepreneurial finance landscape.[4] I concluded that while crowdfunding could well turn into a "market for lemons[,]" in which bad startups seek dumb money as a last resort, possibilities for avoiding this outcome existed.[5] I argued that some promising startups—especially very early-stage startups—would have good reasons to crowdfund,[6] and that the key was to create an environment where investors could distinguish those promising startups from the many duds that will also populate crowdfunding sites.[7] In particular, I argued that the Securities and Exchange Commission ("SEC") should make certain changes to the concept and operation of "funding portals," the new intermediary between startups and investors in the crowdfunding space,[8] before adopting its final rules.[9] Funding portals are the websites that list the startups available for crowdfunding investments,[10] and I argued they

3. *See generally* Darian M. Ibrahim, *Equity Crowdfunding: A Market for Lemons?*, 100 MINN. L. REV. 561 (2015) (examining the development of crowdfunding as well as its potential advantages, disadvantages, and areas for improvement).

4. *Id.* I argued that, in addition to preexisting networks, close geographic proximity between startups and professional investors (angels and venture capitalists) are elements that have contributed to traditional entrepreneurial finance success. *Id.* at 564. The Internet, by its very nature, eliminates these things.

5. *Id.* at 591–606.

6. *See id.* at 589–90 ("[T]here are two types of high-quality startups that might elect to use Title III to raise funds. First, Title III should appeal to high-quality startups that are too young for 'professional' financing under Title II or traditional methods. . . . Second, even for high-quality startups that have progressed a bit further, Title III would appeal to that subset of startups that need cash but do *not* need value-added services from investors." (citations omitted)).

7. *Id.* at 592–603 (discussing disclosure, crowd wisdom, and reputational intermediaries as three possible ways of reducing information asymmetries between entrepreneurs and investors).

8. 15 U.S.C. § 77d (2015); Joan Macleod Heminway, *The New Intermediary on the Block: Funding Portals Under the CROWDFUND Act*, 13 U.C. DAVIS BUS. L.J. 177, 178–79 (2013) (taking an early look at funding portals as a "new, statutorily ordained and mandated intermediary in certain securities offerings made through the Internet"). *See* Stacy Cowley, *New Crowdfunding Rules Let the Small Fry Swim with Sharks*, N.Y. TIMES: DEALBOOK (May 14, 2016), http://www.nytimes.com/2016/05/15/business/dealbook/new-crowdfunding-rules-let-the-small-fry-swim-with-sharks.html?_r=0 [https://perma.cc/3E5J-75SJ] (describing funding portals as "a kind of online bazaar for investment deals").

9. Ibrahim, *supra* note 3, at 602–06 (arguing that funding portals should more closely resemble the "Nomads" that make London's Alternative Investment Market successful).

10. Stuart Cohn, *The New Crowdfunding Registration Exemption: Good Idea, Bad Execution*, 64 FLA. L. REV. 1433, 1439 (2012) (describing a funding portal as an "Internet site that lists crowdfunding opportunities and provides a matching service for interested investors").

should play a larger role as *reputational intermediaries* between startups and investors.[11]

In this Article, I further probe the question at the heart of the funding portal's role: Does crowdfunding need expert intermediation to succeed? Or is crowdfunding, as the name implies, a true "wisdom of the crowds" situation in which expert screening is unnecessary, and perhaps antithetical, to achieving an outcome where crowdfunding is a financial success for more companies and more investors? The answer to this question will go a long way toward determining Regulation Crowdfunding's success or failure, and indeed, goes to crowdfunding's fundamental nature as an investment option.

Ultimately, this Article argues that, like all securities offerings, crowdfunding *does* require expert intermediation to succeed. The Article then argues that the most logical expert intermediary is the funding portal itself.[12] Thankfully the SEC's final crowdfunding rules allow funding portals to do some screening among the startups that wish to list on its site, using the funding portal's judgment as to which startups are most likely to be successful.[13] However, funding portals can only do so much subjective curation without crossing the line into becoming a broker-dealer.[14] Thus, for crowdfunding to succeed, expert investors

11. Ibrahim, *supra* note 3, at 602–06.

12. *See* David M. Freedman & Matthew R. Nutting, 7-*Step Crowdfunding Investment Plan: Step 4: Select the Right Funding Portals*, CROWDFINANCEHUB (Mar. 30, 2016), http://www.financialpoise.com/crowdfundinginvestor/seven-steps/step-4-select-the-right-funding-portals/ [https://perma.cc/2XZ8-NP2V] ("Intermediaries known as funding portals and broker-dealer platforms lie at the heart of the equity crowdfunding experience.").

13. *See infra* text accompanying notes 80, 86.

14. *See, e.g.*, 17 C.F.R. § 227.300(c)(2)(i) (2016); *id.* § 227.402(a). A funding portal can choose to register as a broker-dealer. *See id.* § 227.300(a) (defining intermediaries that may sell under Regulation Crowdfunding as registered brokers, funding portals, and registered national securities association members). The benefits to broker-dealer status are that broker-dealers can offer investment advice to potential investors, compensate employees based on securities sales, and hold/handle funds or securities, while non-broker-dealers cannot. *See id.* § 227.300(c)(2) (defining "[f]unding portal" as "a broker acting as an intermediary in a transaction involving the offer or sale of securities in reliance on [Regulation Crowdfunding] that does not: (i) Offer investment advice or recommendations; (ii) Solicit purchases, sales or offers to buy the securities displayed on its platform; (iii) Compensate employees, agents, or other persons for such solicitation or based on the sale of securities displayed or referenced on its platform; or (iv) Hold, manage, possess, or otherwise handle investor funds or securities"); *id.* § 227.402(a) (prohibiting unregistered broker-dealers from participating in these activities); David M. Freedman & Matthew R. Nutting, *Distinguishing Crowdfunding Portals and Broker-Dealer Platforms Under Title III*, FIN. POISE (Apr. 4, 2016), https://www.financialpoise.com/columns/crowdfunding-for-investors/distinguishing-crowdfunding-portals-and-broker-dealer-platforms-under-title-iii/ [https://perma.cc/AN22-JQF8] ("Broker-dealer platforms are authorized to do, while funding portals (which are not owned or operated by broker-dealers) are prohibited from doing, the following: Offer investment advice or recommendations to

participating in crowdfunding offerings should be active on a site's message boards and investment clubs to guide unsophisticated investors toward the best startups—albeit carefully to avoid unwanted liability exposure.[15]

This Article begins with a brief history of the crowdfunding rules, both as originally proposed in the JOBS Act of 2012 and as finally promulgated by the SEC in October 2015. Second, the Article looks at the difference between expert-based and crowd-based approaches to investing as a general matter. The Article concludes that for startup investing, experts are necessary to achieve better financial outcomes for companies and investors. Third, the Article outlines precisely how expert opinions can and should work in the crowdfunding context. It argues that the SEC's changes to the funding portal concept, by allowing some curation, are a move in the right direction, while also acknowledging that further intermediation to guide unsophisticated investors is likely necessary for investor transparency. Finally, the Article suggests ways in which expert investors participating in crowdfunding offerings can also curate among startups for unsophisticated investors. In sum, funding portal and expert investor curation further pushes crowdfunding away from its moniker's bottom-up, crowd-based approach toward a more appropriate top-down, expert-based system.

Throughout, this Article observes that crowdfunding's move toward an expert-based system means it should no longer be viewed as a revolutionary idea in entrepreneurial finance. Instead, the Article reveals that crowdfunding as implemented will more closely resemble angel and venture capital ("VC") investing models rather than something revolutionary.[16] In my opinion, this is a happy accident. As an expert-driven system, crowdfunding has a better chance for success than if the "crowd" leads the discussion as to which startups are the most viable. In short, "crowdfunding without the crowd" just might work.

investors."). However, broker-dealers are subject to strict due diligence standards, *see* 31 C.F.R. §§ 1023.100–.670 (2012), federal securities law's antifraud provisions, *see* 15 U.S.C. § 77q (2012), and becoming a broker-dealer is a costly step that is unlikely to be attractive to many, if not most, funding portals, *see* JOBS ACT CREATES TWO NEW EXEMPTIONS FROM BROKER-DEALER REGISTRATION, SHEARMAN & STERLING LLP 1–3 (2012), http://www.shearman.com/~/media/Files/NewsInsights/Publications/2012/04/JOBS-Act-Creates-Two-New-Exemptions-from-BrokerD__/Files/View-full-memo-JOBS-Act-Creates-Two-New-Exemptio__/FileAttachment/JOBSActCreatesTwoNewExemptionsfromBrokerDealerRe__.pdf [https://perma.cc/X839-VDDH].

15. *See infra* Section III.B.3.

16. *See infra* Section III.B.

I. THE EVOLUTION OF CROWDFUNDING

Scholars have long-cited a funding gap between investors and startups.[17] The claim is that promising startups exist, but due to the lack of geographic proximity to investors, they do not receive the funding they would absent these market failures.[18] Crowdfunding was designed to close the funding gap by harnessing the Internet's power to reduce transaction costs in matching startups and investors.[19] Crowdfunding was also designed to democratize startup investing, so that "ordinary Americans" could have a chance to own the next Facebook or Twitter before they are public (and commanding a much higher stock price).[20] Legislators viewed crowdfunding as a "job creation mechanism[]" and the legislation easily passed Congress with bipartisan support.[21] Crowdfunding was thus viewed as a win-win-win for everyone.

17. *See, e.g.*, John L. Orcutt, *Improving the Efficiency of the Angel Finance Market: A Proposal to Expand the Intermediary Role of Finders in the Private Capital Raising Setting*, 37 ARIZ. ST. L.J. 861, 874 (2005) ("[A] substantial funding gap has been documented for rapid-growth start-ups in the $250,000 to $5 million range." (citing U.S. GOV'T ACCOUNTABILITY OFF., GGD-00-190, SMALL BUSINESS: EFFORTS TO FACILITATE EQUITY CAPITAL FORMATION 12–13 (2000); Jeffery E. Sohl, *The US Angel and Venture Capital Market: Recent Trends and Developments*, J. PRIVATE EQUITY, Spring 2003, at 14–15); *id.* at 881–83 (stating that startups and angels have trouble finding each other due to high transaction costs, including legal barriers); William K. Sjostrom, Jr., *Relaxing the Ban: It's Time to Allow General Solicitation and Advertising in Exempt Offerings*, 32 FLA. ST. U. L. REV. 1, 3 (2004) ("Estimates indicate . . . that financial markets fall short by some $60 billion annually in meeting the demand of small companies for early-stage private equity financing. This unmet need is referred to as the funding gap." (citing U.S. GOV'T ACCOUNTABILITY OFF., GGD-00-190, SMALL BUSINESS: EFFORTS TO FACILITATE EQUITY CAPITAL FORMATION 2 (2000); Jeffery E. Sohl, *The Early-Stage Equity Market in the USA*, 1 VENTURE CAP.: INT'L ENTREPRENEURIAL FIN. 101, 110 (1999)).

18. *See* Orcutt, *supra* note 17, at 879–83. For example, a VC's business model of heavy due diligence and active monitoring does not support an investment of less than $5 million, far too much cash for a nascent startup; *see* Darian M. Ibrahim, *Financing the Next Silicon Valley*, 87 WASH. U. L. REV. 717, 733–34 (2010) (discussing why VCs eschew early-stage startups as a general matter).

19. *See* Joan MacLeod Heminway & Shelden Ryan Hoffman, *Proceed at Your Peril: Crowdfunding and the Securities Act of 1933*, 78 TENN. L. REV. 879, 931 (2011) ("Crowdfunding enables entrepreneurs to more quickly and easily identify supporter-investors who are willing and able to fund their businesses or projects."); *see also* Ibrahim, *supra* note 3, at 585–86 (noting that Title II of the JOBS Act, which permits online fundraising from accredited investors only, likewise reduces transaction costs for angels looking to add passive investors to their deals).

20. *See* Jean Eaglesham, *Crowdfunding Efforts Draw Suspicion*, WALL ST. J., Jan. 18, 2013, at C1 (quoting President Obama as calling crowdfunding a "game changer" that allows "ordinary Americans . . . to go online and invest in entrepreneurs they believe in").

21. Donald C. Langevoort & Robert B. Thompson, *"Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101 GEO. L.J. 337, 339 (2013) (stating that crowdfunding and other provisions of the JOBS Act "were all styled as job creation

Crowdfunding derives its origin from crowd*sourcing*, the same idea behind websites like Yelp and Wikipedia.[22] Through crowdsourcing, the collective wisdom of the people tells others what the best restaurants are in a town, or produces an accurate biography of a notable person, for example.[23] Crowd*funding* applies that idea to financially backing a project or a company, whether it is the Veronica Mars movie[24] or a new whiskey.[25] Thus, crowdfunding allows more people to own a private startup that might ultimately become the next Facebook. It also, theoretically, allows them *to drive* the choice of which startup will become the next Facebook through the crowd's collective wisdom.

Prior to the JOBS Act of 2012, the Internet could not be used to match startups and investors due to SEC Rule 506's ban on "general solicitation."[26] However, Title II of the JOBS Act removed this ban for *accredited* investors in 2012, the same wealthy club of individuals who previously financed startups offline.[27] Thus, Title II started closing the purported funding gap by taking the geography out of startup investing.

To truly democratize startup investing, however, Title III (Regulation Crowdfunding) was needed to open up Internet investing to

mechanisms—a particularly potent political label heading into an election year—and bipartisan momentum grew").

22. *See* Andrew A. Schwartz, *Crowdfunding Securities*, 88 NOTRE DAME L. REV. 1457, 1459 (2013).

23. *Id.*

24. Ibrahim, *supra* note 3, at 568 (discussing this "[n]on-equity crowdfunding" (citing Chance Barnett, *Crowdfunding Sites in 2014*, FORBES (Aug. 29, 2014, 6:11 PM), http://www.forbes.com/sites/chancebarnett/2014/08/29/crowdfunding-sites-in-2014 [https://perma.cc/R6PJ-JUY4]).

25. *Cleveland Whiskey: Whiskey 2.0/Disruptive Technology*, WEFUNDER, https://wefunder.com/cleveland.whiskey [http://perma.cc/EXH2-JN2S].

26. 17 C.F.R. § 230.501(a) (2011) (amended 2012); Ibrahim, *supra* note 3, at 570 (quoting 17 C.F.R. § 230.506 (2014)) (explaining the general solicitation ban and its hindrance of Internet offerings).

27. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, §§ 201(a)(1), 126 Stat. 306, 313 (2012) (codified at 15 U.S.C. § 77(d)); 15 U.S.C. § 77b(a)(15) (2016) (defining "accredited investor" as: (1) certain bank or development entities or (2) "any person who, on the basis of such factors as financial sophistication, net worth, knowledge, and experience in financial matters, or amount of assets under management qualifies as an accredited investor under rules and regulations which the [SEC] shall prescribe"). *But see* Robert B. Thompson & Donald C. Langevoort, *Redrawing the Public-Private Boundaries in Entrepreneurial Capital Raising*, 98 CORNELL L. REV. 1573, 1616 (2013) ("Accredited-investor status is no longer for the very well off by virtue of inflation over time and now encompasses a broad swath of retail investors in the United States . . . ." (citing U.S. SEC. & EXCH. COMM'N, FINAL REPORT OF THE SEC ADVISORY COMMITTEE ON SMALLER PUBLIC COMPANIES TO THE U.S. SECURITIES AND EXCHANGE COMMISSION 77 (2006)).

even *unaccredited* investors, or the "non-one percenters."[28] Although it took several years for the SEC to implement the final rules, Regulation Crowdfunding recently became a reality.[29] The three-year delay between passing the JOBS Act and the final Regulation Crowdfunding rules was due to concerns over fraud and other investor protection worries in this new medium.[30] The SEC always attempts to balance a business's ability to raise capital with protecting the investors who will supply that capital.[31] The JOBS Act, and in particular Regulation Crowdfunding, favors economic growth and job creation over investor protection.[32]

Investor protection in Regulation Crowdfunding comes primarily from limiting the amount any one investor can lose. As I observed in my previous article, "Title III [Regulation Crowdfunding] attempts to limit the downside for unaccredited investors in a novel way—by specifying

28. Ibrahim, *supra* note 3, at 572 ("Title III of the JOBS Act would make it possible, for the first time, for unaccredited investors to purchase equity in nascent startups through the Internet.").

29. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, §§ 301–05, 126 Stat. 306, 315–23 (2012) (codified in scattered sections of 15 U.S.C.). Albeit with limitations for unaccredited investors. *See* 17 C.F.R. § 227.100(a) (2016) (creating monetary caps for unaccredited investors purchasing crowdfunded securities).

30. *See* Thomas Lee Hazen, *Crowdfunding or Fraudfunding? Social Networks and the Securities Laws—Why the Specially Tailored Exemption Must Be Conditioned on Meaningful Disclosure*, 90 N.C. L. REV. 1735, 1753–54 (2012) (arguing for greater disclosure in crowdfunding offerings); Cowley, *supra* note 8 ("Concerned about protecting investors from charlatans, bad ideas and their own poor judgment, the [SEC] spent years drafting its proposed rules. The final version, released in October [2015], runs to 685 pages." (citing Stacy Cowley, *S.E.C. Gives Small Investors Access to Equity Crowdfunding*, N.Y. TIMES: DEALBOOK (Oct. 30, 2015), https://www.nytimes.com/2015/10/31/business/dealbook/sec-gives-small-investors-access-to-equity-crowdfunding.html [https://perma.cc/Y4WB-GY5Q]; Crowdfunding, Exchange Act Release Nos. 33-9947; 34-76324 (Oct. 30, 2015), https://www.sec.gov/rules/final/2015/33-9974.pdf [https://perma.cc/WU4E-SNB4]); *see also* Thompson & Langevoort, *supra* note 27, at 1617 ("[A]s distributions of securities move from bargaining with a small group of buyers to mass marketing directed at a large, dispersed group of well-off retail investors, the likelihood of successful opportunism grows.").

31. *The Role of the SEC*, INVESTOR.GOV: U.S. SEC. & EXCH. COMM'N, https://investor.gov/introduction-investing/basics/role-sec [https://perma.cc/73Z3-G7CW] ("The U.S. Securities and Exchange Commission (SEC) has a three-part mission: [1] Protect investors, [2] Maintain fair, orderly, and efficient markets [3] Facilitate capital formation[.]"). C. Steven Bradford, *Crowdfunding and the Federal Securities Laws*, 2012 COLUM. BUS. L. REV. 1, 117 (2012) (observing that "investor protection and capital formation are, to some extent, incompatible goals").

32. Thompson & Langevoort, *supra* note 27, at 1573 ("Congress enacted the Jumpstart Our Business Startups (JOBS) Act in 2012 amidst a perceived crisis in entrepreneurial capital raising." (citing Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306 (2012) (codified in scattered sections of 15 U.S.C.)); *see also id.* at 1574 (stating that Congress "demonstrat[ed] a political willingness to trade off some level of investor protection in order to promote capital formation and its hoped-for payoff, job creation").

how much they can purchase in Title III startups in any given year."[33] The final rules limit investment by unaccredited investors to $2,000, or 5% of annual income or net worth, for investors making less than $100,000 annually, or up to 10% of annual income or net worth for investors making over $100,000 annually.[34] Funding portals are tasked with ensuring investors comply with these limits.[35] Other than that, and some background checks on the issuer's principals,[36] funding portals were originally to play a passive role in the crowdfunding process.[37] They were not designed to guide investors toward the best startups—that was left up to the "crowd."

II. INVESTING GENERALLY: CROWDS VERSUS EXPERTS

When it comes to investing, who is better equipped to choose winners: crowds or experts? Proponents of the crowd observe that actively managed investment funds usually do not outperform the market average.[38] Sections A and B below respectively compare and contrast core principles of crowd-based versus expert-based approaches and how they apply to investing, particularly to startup investing.

33. Ibrahim, *supra* note 3, at 572.

34. 15 U.S.C. § 77d(a)(6) (2012).

35. *Id.* § 77d-1(a)(7).

36. *Id.* § 77d-1(a)(5).

37. Jumpstart Our Businesses Startup Act, Pub. L. No. 112-106, § 304, 126 Stat. 306, 321–22 (codified in scattered section of 15 U.S.C.). Ibrahim, *supra* note 3, at 602–03; *see* DAVID M. FREEDMAN & MATTHEW R. NUTTING, EQUITY CROWDFUNDING FOR INVESTORS: A GUIDE TO RISKS, RETURNS, REGULATIONS, FUNDING PORTALS, DUE DILIGENCE, AND DEAL TERMS 120–21 (2015) (suggesting that before the final SEC Regulation Crowdfunding rules, it was unclear that funding portals could use subjective criteria to screen startups).

38. *See* Alan M. Palmiter & Ahmed E. Taha, *Mutual Fund Performance Advertising: Inherently and Materially Misleading?*, 46 GA. L. REV. 289, 302 (2012) (discussing a mutual fund study finding "that only 0.6% of [mutual] funds actually exhibited skill in their long-term performance[, a statistically insignificant result] . . . . meaning that there was not strong evidence that *any* fund managers are skillful enough to outperform their benchmarks in the long run" and noting that "[a] recent study by Professors Eugene Fama and Kenneth French reached a similar conclusion" (first citing Laurent Barras, Oliver Scaillet & Russ Wermers, *False Discoveries in Mutual Fund Performance: Measuring Luck in Estimated Alphas*, 65 J. FIN. 179, 181 (2010), then citing Eugene F. Fama & Kenneth R. French, *Luck Versus Skill in the Cross-Section of Mutual Fund Returns*, 65 J. FIN. 1915, 1915 (2010)); Burton G. Malkiel, *Searching for Rational Investors: Explaining the Lowenstein Paradox*, 30 J. CORP. L. 567, 571 & Exhibit 2 (2005) (presenting evidence that "two-thirds or more of professionally managed large capitalization equity mutual funds are outperformed by the S&P 500 stock index after expenses").

A. Crowds

At the heart of this Article is the claim that when it comes to startup investing, crowds are not as good as experts at screening among the many potential startups seeking funding. Much has been written on crowds versus experts, or bottom-up versus top-down approaches, as a general matter.[39] James Surowiecki's popular book *The Wisdom of Crowds* recites colorful examples of when crowd-based wisdom has produced better results than expert-based wisdom.[40]

A particularly remarkable illustration of crowd-based wisdom, recounted in *The Wisdom of Crowds*, was when a team of salvage men, mathematicians, and others tried to determine the location of a lost U.S. submarine in 1968.[41] The naval officer leading the search had each participant submit his or her best guess of where the submarine was located, based on very limited information and without consulting others.[42] No participant alone came up with the submarine's exact location. But when the participants' guesses were aggregated, they pinpointed the submarine's location to within 220 yards—remarkably close given the wide search parameters.[43] This example illustrates Surowiecki's central claim that "chasing the expert is a mistake," and instead "ask the crowd . . . [because c]hances are, it knows."[44]

39. Michael B. Dorff, *The Siren Call of Equity Crowdfunding*, 39 J. CORP. L. 493, 505 (2014) (observing the notion "as old as the Republic—that the common people as a whole possess a deeper wisdom than the educated elites" (citing JAMES SUROWIECKI, THE WISDOM OF CROWDS: WHY THE MANY ARE SMARTER THAN THE FEW AND HOW COLLECTIVE WISDOM SHAPES BUSINESS, ECONOMIES, SOCIETIES, AND NATIONS, at xiii–xiv (2004)); John Ferejohn, *The Lure of Large Numbers: A Constitution of Many Minds*, 123 HARV. L. REV. 1969, 1980 (2010) (reviewing CASS R. SUNSTEIN, A CONSTITUTION OF MANY MINDS (2009); ADRIAN VERMUELE, LAW AND THE LIMITS OF REASON (2009)) (quoting Aristotle and noting that "[i]n some ways the idea that ordinary people can make wise choices is very old").

40. JAMES SUROWIECKI, THE WISDOM OF CROWDS: WHY THE MANY ARE SMARTER THAN THE FEW AND HOW COLLECTIVE WISDOM SHAPES BUSINESS, ECONOMIES, SOCIETIES, AND NATIONS, at xii–xiii, xx–xxi, 3–5, 7–8 (2004).

41. *Id.* at xx (citing SHERRY SONTAG & CHRISTOPHER DREW, BLIND MAN'S BLUFF 146–50 (1998)).

42. *See id.* ("[T]he area where the navy began searching for the [submarine] was a circle twenty miles wide and many thousands of feet deep. You could not imagine a more hopeless task.").

43. *Id.* at xxi ("The final estimate was a genuinely collective judgment . . . [i]t was also a genuinely brilliant judgment.").

44. *Id.* at xv (citing Richard P. Larrick & Jack B. Soll, *Intuitions About Combining Opinions: Misappreciation of the Averaging Principle*, 52 MGMT. SCI. 111, 125 (2006)). In another famous example, 800 county fair participants guessed an ox's weight. *Id.* at xii (citing FRANCIS GALTON, MEMORIES OF MY LIFE 280–81 (1908); Francis Galton, *The Ballot-Box*, 75 NATURE 509, 509 (1907); Francis Galton, *Vox Populi*, 75 NATURE 450, 450–51 (1907)). When all votes were averaged, their collective guess was within one pound of the ox's actual

For the crowd-based problem-solving approach to work, however, Surowiecki cautions that five factors are necessary: (1) diversity of opinion; (2) independence; (3) decentralization among participants; (4) a method for aggregating participants' individual solutions; and (5) the existence of a well-defined problem having a definitive solution.[45] These factors were present in the lost-submarine example. The question becomes, are these factors also present when it comes to investing, and in particular when using crowdfunding to invest?

Some leading commentators are optimistic about using the wisdom of crowds in Title III investing. For example, Professor Andrew Schwartz argues that "[c]rowdfunding is well positioned to capitalize on the wisdom of crowds[,]" and that instead of "chaos and anarchy . . . the 'wisdom of the crowd' theory suggests that [equity crowdfunders] will do a relatively good job at picking winners."[46] Professor Joan Heminway suggests that "preliminar[y] indicat[ions are] that the crowd of crowdfund investors has the potential for wisdom[,]" but cautions that "[s]ignificant empirical research is needed" to determine this.[47] I too suggested in my previous article that crowd-based wisdom could reduce information asymmetries between entrepreneurs and unsophisticated Title III investors—I was writing about "knowledgeable segment[s] of the crowd" serving as signals to unsophisticated investors, which are in fact expert opinions.[48]

weight. *Id.* at xiii. The Iowa prediction markets likewise rely on crowd-based wisdom to predict the results of presidential elections. *Id.* at 17–19 (citing Robert Forsythe et al., *Anatomy of an Experimental Political Stock Market*, 82 AM. ECON. REV. 1142, 1142–61 (1992); Joyce Berg et al., Results from a Dozen Years of Election Futures Market Research (Mar. 2003) (unpublished manuscript), http://www.biz.uiowa.edu/faculty/trietz/papers/iemresults.pdf [https://perma.cc/BF7L-NRJ5]; Joyce Berg et al., Accuracy and Forecast Standard Error of Prediction Markets (July 2003) (unpublished manuscript), https://tippie.biz.uiowa.edu/iem/archive/forecasting.pdf [https://perma.cc/R23Z-NCDN]).

45. *Id.* at 21–22 (describing "diversity, independence, and decentralization" in decision markets); *id.* at 236 ("With football games, elections, *Millionaire* questions, and Google searches, there is a definitive answer, which at some point is settled once and for all."); *id.* at 237 ("The problem with the stock market is that there never is a point at which you can say that it's over, never a point at which you will definitively be proved right or wrong.").

46. Andrew A. Schwartz, *The Digital Shareholder*, 100 MINN. L. REV. 609, 661 (2015) (citing Thompson & Langevoort, *supra* note 27, at 1605).

47. Joan MacLeod Heminway, *Investor and Market Protection in the Crowdfunding Era: Disclosing to and for the "Crowd"*, 38 VT. L. REV. 827, 845 (2014).

48. Ibrahim, *supra* note 3, at 598 (citing Keongtae Kim & Siva Viswanathan, The Experts in the Crowd: The Role of Reputable Investors in a Crowdfunding Market 3 (Nov. 2013) (unpublished manuscript), https://pdfs.semanticscholar.org/aa82/f39d6736a59c0e368470603779a6aec1c828.pdf?_ga=1.13005047.1170105659.1493596887 [https://perma.cc/UUU4-ULF9]). For a discussion of this expanded definition of an "expert," see *infra* note 117.

However, not all commentators are comfortable with deploying crowd-based approaches in the investment context. In the context of stock markets generally, Surowiecki himself—obviously a crowd-over-experts proponent—identifies significant problems in applying crowd-based wisdom to investing.[49] First, Surowiecki argues that although stock markets seem diverse due to their large volume and many participants, the relative lack of short sellers negates diversity because all buyers are betting on a stock's price to rise.[50] Further, beyond the elements suggested by Surowiecki, herd behavior is a well-documented investor behavioral bias that undercuts the independence criterion.[51] The independence criterion is also undercut by the realization that investors buy stocks not simply based on what they think of them, but whether they think *others* will also find them attractive when they decide to resell.[52] A third problem with applying crowd-based wisdom to investing is that there is never a definitive "answer" to a stock's inherent value; unless the company goes bankrupt, the stock price continues to fluctuate in perpetuity. A final problem, it seems, is that crowd-based wisdom does not apply well to weighted averages because stock prices are not dictated by a representative segment of investors but are instead skewed by the most active or wealthy investors.[53]

Applying the criteria for crowd-based wisdom to investing generally reveals a bad fit. Applying these criteria to *startup and crowdfunding* investing, specifically, reveals an even worse fit. First, the investor pool

49. SUROWIECKI, *supra* note 40, at 228, 237.

50. *Id.* at 228. Of course, having as many sellers as buyers in the stock market generally could be seen as the requisite diversity of opinion.

51. *See, e.g.*, David S. Scharfstein & Jeremy C. Stein, *Herd Behavior and Investment*, 80 AM. ECON. REV. 465, 470–75 (1990) (presenting a model of herd equilibria and its decision-making implications on managers and investors); *see also* SUROWIECKI, *supra* note 40, at 229 ("[I]nvestors sometimes herd, preferring the safety of the company of others to mak[ing] independent decisions.").

52. Ken Eisold, *Investors Following the Crowd*, PSYCHOLOGY TODAY (Dec. 1, 2014), https://www.psychologytoday.com/blog/hidden-motives/201412/investors-following-the-crowd [https://perma.cc/JMJ4-L8A9] (arguing that "[t]he wisdom of crowds doesn't apply to picking stocks" and that "the pressure to fit into the crowd and conform takes over and will lead [crowd investors] astray").

53. DAVID EASLEY & JON KLEINBERG, NETWORKS, CROWDS, AND MARKETS: REASONING ABOUT A HIGHLY CONNECTED WORLD 618 (2010) (stating that the wisdom of the crowd is limited by "two important qualifications," one of which is "that all beliefs are equally weighted"); *see id.* at 641 (noting that market performance in markets using weighted averages "is not based on the benefits of averaging, as in . . . the 'wisdom of crowds.' Rather . . . the crowd is exactly as smart as its smartest participant . . . [T]his idea draws on a long history of economic markets for market efficiency based on natural selection, in which smart traders come to hold an increasingly large fraction of wealth in the market and thereby exert an increasingly large influence on the market" (citations omitted)).

in any given crowdfunding offering is likely to be very small relative to a publicly traded stock, thus negating the diversity criterion. Further, all investors in a crowdfunding offering are betting *for* the startup—no one is betting against it.[54] Herd behavior (and thus dependence) is likely in crowdfunding, as investors will want to choose "winners" to fund.[55] Also, most crowdfunding offerings operate on an all-or-nothing basis, meaning that a startup must raise all of the funds it seeks or it gets no funds at all, thus exacerbating the herd mentality.[56] Conversely, however, the all-or-nothing approach provides a somewhat more definitive solution than is present in public markets: either the crowdfunding offering is successful or it is not. But of course, raising the desired Title III funds in no way ensures the startup's eventual success or an investor's liquidity.[57] Overall, the criteria necessary for crowd-based wisdom to function efficiently do not appear to be remotely met in startup investing.

B. Experts

While crowd-based wisdom does not seem to be a good fit with startup investing, expert-based investing has a proven track record in similar areas. As a preliminary observation, experts are known to play an important role in investing generally. For instance, reputational intermediaries serve important signaling and bonding roles in public company investing.[58] Initial public offering ("IPO") issuers hire well-

54. Without resale markets there are no sellers, and certainly no traditional short sellers. *See Regulation Crowdfunding: A Small Entity Compliance Guide for Issuers*, U.S. SEC. & EXCH. COMM'N (May 13, 2016) https://www.sec.gov/info/smallbus/secg/rccomplianceguide-051316.htm [https://perma.cc/DQ8V-W7W6]; *see also infra* note 106. *But see* Steve LeVine, *Investors Have Placed a One-Way Bet on Uber—Which Made Us Want to Find a Way to Short It*, QUARTZ (Aug. 5, 2016), http://qz.com/707947 [https://perma.cc/8MN6-32MK] (explaining why investors may want to short Uber, but noting that because Uber is currently not publicly traded, shorting the stock is difficult, and can currently occur only through indirect means, or possibly by purchasing derivative forward contracts or using credit default swaps).

55. *See* Eisold, *supra* note 52.

56. *See* 17 C.F.R. § 227.304(d) (2016) (requiring intermediaries to return investor funds if an offering is not completed); *see also id.* § 227.201(g) (requiring intermediaries to inform investors that if "[t]he target offering amount and the deadline to reach the target offering amount . . . does not equal or exceed the target offering amount at the offering deadline, no securities will be sold in the offering, investment commitments will be cancelled and committed funds will be returned[.]").

57. Crowdfunded securities are subject to resale restrictions for one year. *Id.* § 227.501(a). Also, it remains to be seen what secondary markets might develop for crowdfunding securities.

58. Donald C. Langevoort, *Angels on the Internet: The Elusive Promise of "Technological Disintermediation" for Unregistered Offerings of Securities*, 2 J. SMALL & EMERGING BUS. L. 1, 14 (1998) (observing the "function that financial intermediaries play in signaling and bonding the informational credibility of issuer disclosure").

known investment banks to rent their reputations to the offering, thus enticing investors who might otherwise be wary of funding the company due to its limited track record.[59] Often times, "[t]he participation of reputational intermediaries in a transaction . . . acts as a signaling device to the market, enhancing trust in the transaction."[60]

As applied to startup investing specifically, there is a proven track record of success due to expert investors populating a similar space. Angel and VC investors have long succeeded because those investors are repeat players and experts in this particular niche.[61] For example, angel investors are usually ex-entrepreneurs who successfully sold a startup in the same technical field in which they now invest.[62] These investors are also experts in understanding what makes a successful entrepreneur and how to grow and scale a startup.[63]

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59. Bernard S. Black, *The Legal and Institutional Preconditions for Strong Securities Markets*, 48 UCLA L. REV. 781, 787 (2001) ("[I]ntermediaries can credibly vouch for the quality of particular securities because they are repeat players who will suffer a reputational loss, if they let a company falsify or unduly exaggerate its prospects, that exceeds their one-time gain from permitting the exaggeration."); *see also* Ronald J. Gilson, *Engineering a Venture Capital Market: Lessons from the American Experience*, 55 STAN. L. REV. 1067, 1086 (2003) (presenting the idea that reputation markets are extralegal mechanisms that constrain parties' behavior and exist in the corporate community when there are (1) repeat players in a close knit community, (2) "shared expectations of what constitutes appropriate behavior," and (3) an ability to police whether behavior conforms to those expectations).

60. Heminway, *supra* note 8, at 186.

61. *See* Bijan Khosravi, *A Deeper Look at the Venture Capital Landscape in 2016*, FORBES (Apr. 1, 2016, 8:00 AM), https://www.forbes.com/sites/bijankhosravi/2016/04/01/a-deeper-look-at-forbes-the-midas-list-2016/#2c3635c31fba [https://perma.cc/TX45-MUKF] ("Sometimes tried and true is the way to go, especially when it comes to finding a solid, reliable investor. There are a number of VCs who have repeatedly appeared on the Midas List over the past five years . . . ."); Darian M. Ibrahim, *The (Not So) Puzzling Behavior of Angel Investors*, 61 VAND. L. REV. 1405, 1424 (2008) ("[E]ven if angels invest in a number of start-ups, their preference [is] for start-ups in their field of expertise[.]").

62. *See* Ibrahim, *supra* note 61, at 1427 ("[A]ngels are overwhelmingly ex-entrepreneurs, which suggests that they not only understand investing as a general matter, but start-up investments in particular. Many angels made their fortunes after going through the very same funding process on the other side, when running their own start-ups." (citing John Freear et al., *Angels and Non-Angels: Are There Differences?*, 9 J. BUS. VENTURING 109, 111 (1994); MARK VAN OSNABRUGGE & ROBERT J. ROBINSON, ANGEL INVESTING: MATCHING START-UP FUNDS WITH START-UP COMPANIES—THE GUIDE FOR ENTREPRENEURS, INDIVIDUAL INVESTORS, AND VENTURE CAPITALISTS 108 (2000)).

63. See Vivek Wadhwa, *Venture Capital: The Good, Bad, and Ugly*, BLOOMBERG (July 17, 2006, 5:04 PM), https://www.bloomberg.com/news/articles/2006-07-17/venture-capital-the-good-bad-and-uglybusinessweek-business-news-stock-market-and-financial-advice [https://perma.cc/R723-KQBT] ("Venture capitalist firms are usually staffed by experienced executives who have not only been successful on their own, but have also watched dozens of startups succeed and fail. They can guide you through your journey."). According to Silicon Valley guru Paul Graham, in terms of selecting investments, someone who "knows what a successful startup founder looks like is actually far ahead of someone who knows terms

Angel investors almost always invest in syndicates, in which passive angels rely on an "expert" active angel to take the lead on *ex ante* screening and due diligence and to actively engage, *ex post*, with the startup.[64] In Title II crowdfunding (accredited investors only), I have noted that early successes are due to angel investors' ability to move this same business model online and add even more non-expert, passive angels at low transaction costs.[65] I have also noted that having an expert angel lead a funding round also provides a positive signal to the VCs who might follow, just as a strong venture capital round provides a signal to investment bankers who might underwrite the startup's IPO.[66]

Angels and VCs have backed Facebook,[67] Google,[68] Tesla Motors,[69] and many other notable tech company successes of the last few decades. These companies now employ hundreds of thousands of individuals and contribute substantially to our economy.[70] This Article argues that, for

sheets . . . inside out." FREEDMAN & NUTTING, *supra* note 37, at 115 (citing Paul Graham, *How to be an Angel Investor*, PAULGRAHAM.COM (Mar. 2009), http://www.paulgraham.com /angelinvesting.html [https://perma.cc/QX9G-P6VB]).

64. *See* Ibrahim, *supra* note 61, at 1439 n.174 ("[S]yndication means that each start-up will have an active angel and several passive ones; those passive angels may be the active angels in other ventures.").

65. Ibrahim, *supra* note 3, at 584 ("AngelList [a Title II website] has a function called 'syndicate,' which operates in exactly the same way as a traditional angel syndicate, except online. New investors are passive and turn over decision-making to an active angel."(citing Brad Stone, *AngelList, the Social Network for Startups*, BLOOMBERG BUS. (Jan. 16, 2014), https://www.bloomberg.com/news/articles/2014-01-16/angellist-the-social-network-for-startups [https://perma.cc/2QM5-GYKF]).

66. Ibrahim, *supra* note 18, at 748–53 (exploring the signaling function of angel financing); *id*. at 749 ("VCs send positive signals about the start-ups they fund . . . . [both] to labor markets and later investors, including investment banks and public investors." (citing Antonio Davila, George Foster & Mahendra Gupta, Venture-Capital Financing and the Growth of Startup Firms 16 (Aug. 2002) (unpublished manuscript), http://citeseerx.ist.psu.edu /viewdoc/download?doi=10.1.1.201.2971&rep=rep1&type=pdf [https://perma.cc/R97P-ZMT7 (staff-uploaded archive)]).

67. Tomio Geron, *The Untold Story of Two Early Facebook Investors*, FORBES (Feb. 1, 2012, 4:32 AM), http://www.forbes.com/sites/tomiogeron/2012/02/01/the-untold-story-of-two-early-facebook-investors/#27bf7042f259 [https://perma.cc/AVA5-VAJV] (discussing Venky Harinarayan and Anand Rajaraman, two early angel investors in Facebook who did not receive much media attention).

68. Ibrahim, *supra* note 61, at 1410 (noting "the funding of Google in 1999 by leading Silicon Valley firms Kleiner Perkins and Sequoia Capital" (citing *Google Milestones*, GOOGLE, http://web.archive.org/web/20080102101316/http://www.google.com/corporate/history .html [https://perma.cc/2AFN-GEF9]).

69. Press Release, Tesla Motors Secures $40 Million Investment Round Led by VantagePoint Venture Partners and Elon Musk, BUS. WIRE (May 31, 2006, 7:19 PM), http:// www.businesswire.com/news/home/20060531006128/en/Tesla-Motors-Secures-40-Million-Investment-Led [https://perma.cc/M954-DGGT].

70. Mary J. Dent, *A Rose by Any Other Name: How Labels Get in the Way of U.S. Innovation Policy*, 8 BERKELEY BUS. L.J., 2011, no. 2, at 128, 137 (2011) ("To give a sense for

Title III crowdfunding to work for unsophisticated investors and the startups that seek their funds, the system must be more expert based, despite its moniker implying use of the crowd.[71]

III. CURATION AND EXPERT OPINION IN CROWDFUNDING

Having argued that expert curation is optimal in startup investing, this Part examines how such curation can and should work in crowdfunding. This Part first explores funding portals, the natural reputational intermediary for sorting among the promising and unpromising startups seeking to list on their websites. Second, for those startups that a funding portal does list, this Part explores the role that expert investors can play to further guide unsophisticated investors toward the most promising of the choices.

A. Funding Portals

Regulation Crowdfunding in its original form as envisioned by the JOBS Act sought to implement a true "wisdom of the crowds" regime, where funding portals played an almost completely passive role.[72] I have previously argued that funding portals should be allowed to do more screening of startups to offer investors better (and fewer) choices.[73] Regulation Crowdfunding in its final form implemented some of these

the long-lasting impact of the venture ecosystem on the American economy, as of 2008, eight out of ten people employed in the software development industry worked for a company with venture capital roots; seven out of ten people employed in the telecommunications and semiconductor industries worked for a company with venture capital roots; and more than half of the people employed in the networking and equipment and electronics/instrumentation industries worked for a company with venture capital roots." (citations omitted)).

71. In his new book on investor protection, Donald Langevoort quotes an experienced angel investor as "stress[ing] that crowd-based investing ignores nearly every lesson he learned about how to succeed." DONALD C. LANGEVOORT, SELLING HOPE, SELLING RISK: CORPORATIONS, WALL STREET, AND THE DILEMMAS OF INVESTOR PROTECTION 130 (2016) (citing Daniel Isenberg, *The Road to Crowdfunding Hell*, HARVARD BUS. REV. (April 23, 2012), https://hbr.org/2012/04/the-road-to-crowdfunding-hell [https://perma.cc/K99T-EFXH]).

72. Jumpstart Our Businesses Startup Act, Pub. L. No. 112-106, § 304, 126 Stat. 306, 321–22 (2012) (codified in scattered section of 15 U.S.C.); Ibrahim, *supra* note 3, at 603–04 ("[U]nder Title III as currently written, a funding portal must basically act as a 'neutral third party[.]' " (citing Jacques F. Baritot, Note, *Increasing Protection for Crowdfunding Investors Under the JOBS Act*, 13 U.C. DAVIS BUS. L.J. 259, 277 (2013)).

73. Ibrahim, *supra* note 3, at 603–06.

improvements.[74] In particular, funding portals may screen startups using some subjective, "is it a promising company?" criteria.[75]

The funding portal, as an intermediary, "is the vital link between the issuer and her investors."[76] And indeed under Regulation Crowdfunding, it is the *only* link, as startups must channel all fundraising activities through one funding portal.[77] Funding portals were originally conceived of as a relationship between portal and *investor*, not portal and startup.[78] As written in the JOBS Act, a funding portal's only task with respect to startups was to do background checks on its principals.[79]

But changes between the original passage of Title III in the 2012 JOBS Act and the actual implementation of Title III in 2015 now allow funding portals to do more screening of startups.[80] In other words, some curation on substantive grounds is now allowed. The final rules specify that "the ability of a funding portal to determine which issuers may use its platform is important for the protection of investors, as well as to the viability of the funding portal industry, and thus the crowdfunding market."[81] Without this change, funding portals would have to "post all investment opportunities that meet objective criteria [which would] . . . . eliminate any advantage that [funding portals] have in knowing how to select businesses to feature on their sites."[82] The final

74. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, §§ 301–05, 126 Stat. 306, 315–23 (2012) (codified in scattered sections of 15 U.S.C.).

75. *See* 17 C.F.R. § 227.301(c) (2016).

76. Gregory D. Deschler, Comment, *Wisdom of the Intermediary Crowd: What the Proposed Rules Mean for Ambitious Crowdfunding Intermediaries*, 58 ST. LOUIS U .L.J. 1145, 1167 (2014); *see* Freedman & Nutting, *supra* note 12 ("[F]unding portals and broker-dealer platforms lie at the heart of the equity crowdfunding experience.").

77. 17 C.F.R. § 227.100(a)(3) (requiring issuers offering or selling securities under Regulation Crowdfunding to conduct its "transaction . . . through an intermediary that complies with the requirements in [Regulation Crowdfunding and] is conducted exclusively through the intermediary's platform"); Crowdfunding, Securities Act Release Nos. 33-9974, 34-76324, 80 Fed. Reg. 71,387, 71,395 (Nov. 16, 2015) (to be codified at 17 C.F.R. pts. 200, 227, 232, 239, 240, 249, 269 & 274) ("[The SEC] believe[s] that requiring an issuer to use only one intermediary to conduct an offering or concurrent offerings in reliance on [Regulation Crowdfunding will] help foster the creation of a 'crowd' and better accomplish the purpose of the statute.").

78. *See* Ibrahim, *supra* note 3, at 602–03.

79. *See* 15 U.S.C. § 77d-1(a)(5) (2012).

80. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, §§ 301–05, 126 Stat. 306, 315–23 (2012) (codified in scattered sections of 15 U.S.C.).

81. Crowdfunding, 80 Fed. Reg. at 71,462.

82. Scott Shane, *Why Kickstarter and Indiegogo Won't Go Into Equity Crowdfunding*, ENTREPRENEUR (Sept. 9, 2015), http://www.entrepreneur.com/article/250355 [https://perma.cc/VL8E-B4CG]; *see* Jacques F. Baritot, Note, *Increasing Protection for Crowdfunding Investors Under the JOBS Act*, 13 U.C. DAVIS BUS. L.J. 259, 277 (2013) ("Intermediaries could . . . perform their own due diligence by focusing on the merit of technology or services

rules also allow funding portals to have some "skin in the game" by receiving equity in listed startups as compensation on the same terms as offered to investors[83]—usually a trigger for broker-dealer fears.[84] Funding portals may also advise the issuer on offerings and offering documentation.[85]

These changes are important for allowing a funding portal to use its expertise to screen startups based on their chances for success, not just on whether or not the startups are businesses free from fraud. As one commentator noted, "[t]he most important change [in the new rules] is probably the SEC's decision to permit funding portals . . . to selectively curate which issuers may list on their sites."[86] The commentator further contended that "[f]ailing to permit funding portals to take on this important investor protection function could have spelled disaster for the nascent crowdfunding industry."[87] The signal of having a funding portal stake its reputation, in part, on the startups it allows to list is an important step in the right direction.[88] I previously observed that FundersClub, an online offering site for accredited investors under Title II of the JOBS Act, seemed to be successful due to the site's prelisting curation.[89] In fact, at the time I wrote that article, each of the startups listed on FundersClub was a graduate from the prestigious Y Combinator or 500 Startups.[90]

Funding portals should also have the *incentive* to curate, as a competitive reputation market among funding portals should quickly

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offered." (citing Letter from T.W. Kennedy, funder, Regulated Funding Portal Industry Ass'n, to Sec. & Exch. Comm'n (Aug. 18, 2012), https://www.sec.gov/comments/jobs-title-iii/jobstitleiii-133.pdf [https://perma.cc/GB3X-BSFN]).

83. 17 C.F.R. § 227.300(b).

84. *But see* FundersClub Inc. & FundersClub Mgmt. LLC, SEC No-Action Letter, 2013 WL 1229456, at *9 (Mar. 26, 2013).

85. 17 C.F.R. § 227.402(b)(5).

86. Evan Engstrom, *The Good and the Bad in the SEC's New Crowdfunding Rules*, ENGINE (Nov. 5, 2015), http://www.engine.is/news/issues/the-good-and-the-bad-in-the-secs-new-crowdfunding-rules/6124 [https://perma.cc/XZ2K-3NG9].

87. *Id.*

88. Ethan Mollick, Swept Away by the Crowd? Crowdfunding, Venture Capital, and the Selection of Entrepreneurs 21–26 (Mar. 25, 2013) (unpublished manuscript), http://ssrn.com/abstract=2239204 [https://perma.cc/Z83H-3W47 (staff-uploaded archive)].

89. Ibrahim, *supra* note 3, at 583 (discussing the FundersClub case, which at the time written allowed only startups graduating from the prestigious Y Combinator accelerator to list on its site); *How FundersClub Selects Companies*, FUNDERSCLUB, http://web.archive.org/web/20150320203530/https://fundersclub.com/vetting [https://perma.cc/JXQ6-EFQY].

90. Ibrahim, *supra* note 3, at 583; *Portfolio*, FUNDERSCLUB, http://web.archive.org/web/20150315093040/https://fundersclub.com/portfolio/#fc [https://perma.cc/THG9-6WAE]; Matthew Zeitlin, *FundersClub Takes Crowdsourcing Approach to Early-stage Venture Capital*, DailyBeast (Mar 3, 2013, 5:45 AM), [https://perma.cc/X4UP-ZLX2].

form. If the startups listed on a funding portal's site do well, this may cause other startups to list there in search of viable opportunities. Conversely, a funding portal that lists startups that do not meet their funding goals or often fail will suffer reputational harm that will be bad for business. WeFunder appears to be out to an early lead, hosting half of the first fifty Title III offerings.[91]

B. Expert Investors

I applaud these changes to the funding portal's role and think they give crowdfunding a better chance to succeed. However, this Article's goal is to suggest further steps to improve crowdfunding's long-term viability.

First, as a practical concern, despite the permitted curation, a funding portal is still limited in signaling its opinion about a startup's merits to unsophisticated investors unless it registers as a broker-dealer, an expensive step.[92] Financially, it seems unlikely that funding portals that are not already broker-dealers will register as such.[93] For example, after curating who may list with them, a funding portal may "highlight offerings" on its website, but only based on "objective criteria . . . where the criteria are reasonably designed to highlight a broader selection of issuers[.]"[94]

Accordingly, this Article suggests that *more* curation is necessary to allow unsophisticated investors to make better investment decisions among the startups that make it past a funding portal's initial litmus test for listing. This Article proposes to allow expert investors to signal

91. Marc. A. Leaf, Robert T. Esposito & Abigail Luhn, *Leading the Crowd: An Analysis of the First 50 Crowdfunding Offerings*, DRINKER BIDDLE & REATH LLP (July 14, 2016), http://www.drinkerbiddle.com/resources/publications/2016/following-the-crowd-an-analysis-of-the-first-50-crowdfunding-offerings?Section=Publications [https://perma.cc/VZG2-H7ZG].

92. See Jumpstart Our Businesses Startup Act, Pub. L. No. 112-106, § 304(a)(1), 126 Stat. 306, 321–22 (2012) (codified in scattered section of 15 U.S.C.); David A. Lipton, *A Primer on Broker-Dealer Registration*, 36 CATH. U. L. REV. 899, 907–08 (1987) ("Once registered, a broker-dealer is required to comply with specific record keeping, financial compliance, and financial reporting requirements . . . . Registered broker-dealers . . . are subject to rigorous net worth and capital requirements . . . . Further protection is provided investors by the Securities Investor Protection Act, which requires all registered brokers to join an insurance program to cover customer losses in instances of brokerage house failure." (citations omitted))

93. Raxit Shah, Note, *Staying the Course with Broker-Dealer Registration: The SEC's Impending Regulation of Crowdfunding Portals Under the JOBS Act*, 40 J. CORP. L. 275, 281 (2014) ("Registering as a broker-dealer is prohibitively expensive . . . . Recognizing [this] . . . , the JOBS Act created an exception to broker-dealer registration for crowdfunding portals." (citing Douglas S. Ellenoff, *Making Crowdfunding Credible*, 66 VAND. L. REV. EN BANC 19, 20 (2013); Lipton, *supra* note 92, at 907–08).

94. 17 C.F.R. § 227.402(b)(2) (2016).

relative quality about startups that pass the funding portal's curation. There are various ways to effectuate this suggestion. This Part will focus on increasing the usage of message boards and investment clubs, both current options on funding portal sites.[95]

1. Message Boards

Regarding message boards generally, Professor Andrew Schwartz observes that "[u]sing online chatrooms, bulletin boards and the like, potential investors and others can directly communicate with one another and share material information about various crowdfunding investments."[96] He also correctly observes the monetary impetus for investors to share information: each individual investor is limited in how much they can invest, so it will take others investing as well for the startup to reach its fundraising goal.[97] Indeed, a study in the *Journal of Finance* found that Internet stock message boards for public companies can contain "financially relevant information[.]"[98]

The final rules require funding portals' websites to include avenues for investors to communicate with startups and with each other.[99] Funding portals can create message boards without fear of this action making them broker-dealers.[100] The final rules notice states that "communication channels on the intermediary's platform will provide a centralized and transparent means for members of the public that have opened an account with the intermediary to share their views about investment opportunities[.]"[101] The startup's representatives may also communicate with investors through message boards so long as they

95. *See* Werner Antweiler & Murray Z. Frank, *Is All That Talk Just Noise? The Information Content of Internet Stock Message Boards*, 59 J. FIN. 1259, 1259, 1292 (2004) (finding that posting on stock message boards influences trading). Langevoort and Thompson worry that such communication may undermine crowd-based wisdom by "introducing the risk of anchoring crowdmembers' beliefs and undermining the average effect of many independent beliefs." Thompson & Langevoort, *supra* note 27, at 1606–07 (citing Richard P. Larrick, Albert E. Mannes & Jack B. Soll, *The Social Psychology of the Wisdom of Crowds*, *in* SOCIAL JUDGMENT AND DECISION MAKING 227, 232–33 (Joachim I. Krueger ed., 2012). As I prefer following the expert, I am not overly concerned with the risk Thompson and Langevoort raise.

96. Schwartz, *supra* note 46, at 663 (citing DAREN C. BRABHAM, CROWDSOURCING 12–13 (2013)).

97. *Id.* at 666–67.

98. Antweiler & Frank, *supra* note 95, at 1292 ("The evidence clearly rejects the hypothesis that all talk is just noise. There is financially relevant information present.").

99. 17 C.F.R. § 227.402(b)(4).

100. *See id.* § 227.402(b).

101. Crowdfunding, Securities Act Release Nos. 33-9974, 34-76324, 80 Fed. Reg. 71,387, 71,446 (Nov. 16, 2015) (to be codified at 17 C.F.R. pts. 200, 227, 232, 239, 240, 249, 269 & 274).

identify themselves as startup representatives.[102] As with Amazon or Yelp, the final rules specifically envision some method of quantifying the ratings to guide other investors.[103] One challenge will be to develop methods of policing self-interested reviews as Amazon and others have done.[104]

Does such a system create cause for concern over an investor saying overly optimistic things on a startup's message board to entice others to invest as well? Possibly. However, promoting a startup that does not warrant it will not be a successful technique in crowdfunding,[105] as resale restrictions and other liquidity issues prevent making a quick buck this way.[106] Because there is no resale market for these investments, the investor will bear the brunt of a bad investment regardless of whether he

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102. 17 C.F.R. § 227.204(c) ("[A]n issuer, and persons acting on behalf of the issuer, may communicate with investors and potential investors about the terms of the offering through communication channels provided by the intermediary on the intermediary's platform, provided that an issuer identifies itself as the issuer in all communications."); Crowdfunding, 80 Fed. Reg. at 71,425. *See generally* Deschler, *supra* note 76 (supporting a requirement that issuers identify themselves when posting on funding portal message boards).

103. Crowdfunding, 80 Fed. Reg. at 71,465 ("[A] communication channel may permit investors to rate or comment on an issuer or offering, or to assign quantifiable indicators to one other's comments.").

104. For example, Amazon reviews can be filtered to include only those that have received a "verified purchase" badge, meaning the reviewer actually bought the product at or near market price. Chris Morran, *Is Amazon Doing Anything to Fight Latest Wave of Fake, Paid-For Reviews?*, CONSUMERIST (Feb. 8, 2016, 12:25 PM), https://consumerist.com/2016/02/08/is-amazon-doing-anything-to-fight-latest-wave-of-fake-compensated-reviews/ [https://perma.cc/M5QB-RUMX].

105. *See, e.g.*, Christine Hurt, *Moral Hazard and the Initial Public Offering*, 26 CARDOZO L. REV. 711, 716–17 (2005) (summarizing pump-and-dump schemes in public company stock).

106. 17 C.F.R. § 227.501(a). Crowdfunding securities are subject to resale restrictions for one year. 17 C.F.R. § 227.501(a). In addition, even after the year-long sales prohibition has ended, there are issues regarding the avenues available through which a party can sell these platforms. Although there are "[s]econdary private investment markets such as SecondMarket and Shares Post [which] allow shares in pre-IPO private companies to be sold by employees and investors," James Johnson, *Rule 144 Privately Offered and Restricted Securities*, CROWDEXPERT.COM, http://crowdexpert.com/investment-crowdfunding/rule-144-privately-offered-restricted-securities/ [https://perma.cc/9HY3-D7PH], it is unclear whether these secondary private investment markets will allow crowdfunded securities to resell in these markets or whether these secondary private investment markets are even appropriate for reselling crowdfunded securities, *see* Scott Shane, *Will Equity Crowdfunding Buyers Be Able to Sell Their Shares?*, ENTREPRENEUR (June 30, 2015), https://www.entrepreneur.com/article/247832 [https://perma.cc/QR99-9V99] (arguing that SecondMarket and SharesPost are inappropriate "for non-accredited investors' equity-crowdfunding holdings [because] . . . . [t]hese market makers generally require the approval of the companies that issued the shares before the stock can change hands, making them a better fit for the transferring shares of employees than those of investors [and because] . . . . [t]he markets themselves are also labor intensive and would not be economical for the buying and selling [of] small numbers of shares").

encourages others to join; either the company succeeds and he will make a profit, or it will fail and his investment will not be returned. Further, there are also potential liability concerns that should keep fraudsters at bay, which I discuss below.[107]

2. Investment Clubs

The second potential mechanism for guiding unsophisticated investors is investment clubs, which have the benefit of being more expert based than message boards. Over half of the first fifty Regulation Crowdfunding offerings were conducted on the funding portal WeFunder.[108] While WeFunder claims it does not curate startups for their merits, WeFunder's key sorting mechanisms are the various "investment clubs" it hosts. On WeFunder, "[i]nvestment clubs are groups of industry experts who can choose to endorse companies. If your business gets endorsed by a club, it will appear higher in the sorting algorithms on WeFunder, and be much more likely to be featured on the home page."[109] As WeFunder advertises, investment clubs allow investors to follow "the wisdom of the *experts*."[110]

One prominent WeFunder investment club is the "The Order of the Orange Hand," a self-described "mafia of Y Combinator alumni."[111] When investors "back the club," they commit to invest a certain amount per deal that the club invests in.[112] In short, investors are not even choosing startups at this point, but totally relying on Y Combinator alumni's expertise in doing so.

Investment clubs on WeFunder are similar to piggybacking on an AngelList (another funding portal that operates under Title II) investment because a prominent angel invested in the company, a concept AngelList calls "social proof."[113] In short, AngelList works because all potential investment opportunities are accompanied by a list

107. *See infra* Section III.B.3.

108. Leaf et al., *supra* note 91.

109. *Why Wefunder?*, WEFUNDER, https://wefunder.com/faq/founders [https://perma.cc/3QmJ-KLTW].

110. *Clubs*, WEFUNDER, https://wefunder.com/faq/clubs#club-overview [https://perma.cc/4ERN-K5GC].

111. *The Order of the Orange Hand*, WEFUNDER, https://wefunder.com/companies [https://perma.cc/985Y-CGL7].

112. *Clubs*, *supra* note 110.

113. Ibrahim, *supra* note 3, at 584 (quoting *Why I Deleted my AngelList Account*, BRYCE DOT VC, http://bryce.vc/post/3520840379/why-i-deleted-my-angellist-account [https://perma.cc/9GM5-JHVZ]).

of the notable investors participating in the offering.[114] Thus, less knowledgeable investors can "tag on" to LinkedIn founder Reid Hoffman's or Yahoo! CEO Marissa Mayer's picks.[115] This is likewise the formula behind angel groups' "sidecar" funds, or investment pools in which a group of non-expert angels co-invest small amounts with expert angels in larger deals.[116] Investment clubs represent another move toward expert-based investing through Regulation Crowdfunding.[117]

3. Liability Concerns

There are some potential liability concerns for those experts who promote particular offerings. One liability concern is whether self-professed experts could be liable for fraudulent or failed offerings as investment advisers[118] under the Investment Advisers Act of 1940

114. *Id*. ("As one former AngelList investor writes, 'Nearly every email [AngelList] send[s] includes names of people or firms who've committed to invest.' " (alteration in original) (quoting *Why I Deleted my AngelList Account*, BRYCE DOT VC, http://bryce.vc/post/3520840379/why-i-deleted-my-angellist-account [https://perma.cc/9GM5-JHVZ]).

115. *See id*. ("Top angels, by followers, on AngelList are household names: Reid Hoffman (founder of LinkedIn), Marissa Mayer (CEO of Yahoo), and the actor Ashton Kutcher."(citing Andrew Davidson, *Follow the Money: AngelList Has Blown Open Early-Stage Investments*, WIRED (May 17, 2013), http://www.wired.co.uk/article/follow-the-money [https://perma.cc/D7QW-LBNG]).

116. *See* Ibrahim, *supra* note 18, at 743 ("Angel group members still invest personal funds, although some of the larger groups have also established 'sidecar' funds to co-invest in the group's most attractive deals." (citing Carol M. Sands, *The Angels' Forum and The Halo Fund: The Rise of the Professional Angel*, *in* STATE OF THE ART: AN EXECUTIVE BRIEFING ON CUTTING-EDGE PRACTICES IN AMERICAN ANGEL INVESTING 32, 39 (John May & Elizabeth F. O'Halloran eds., 2003)).

117. *See supra* notes 108–17 and accompanying text. Interestingly, many of the initial Title III offerings are not tech startups, but lifestyle companies selling alcoholic beverages and the like. *See* Leaf et al., *supra* note 91. Does this change my "experts versus crowds" analysis? I submit that it does not, but would expand my definition of an expert in those cases to be broader than tech expertise or experience. For example, an "expert" in evaluating a fast maturing Scotch company could be an expert in Scotch tasting. *See Cleveland Whiskey: Whiskey 2.0/ Disruptive Technology*, *supra* note 25. Although one concern could be that such experts would be changing on a company-by-company basis, thus negating any kind of a reputation-based screening approach to tagging along as one would have with Reid Hoffman.

118. Under the Advisers Act, an investment adviser is "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities[,]" but excludes

> (A) a bank, or any bank holding company as defined in the Bank Holding Company Act of 1956 . . . which is not an investment company . . . [unless] the bank or bank holding company serves or acts as an investment advisor to a registered investment company . . . (B) any lawyer, accountant, engineer, or teacher whose performance of such services is solely incidental to the practice of his profession; (C) any broker or

("Advisers Act").[119] If so, experts could be considered investment advisers under the Act, and thus, subject to the Adviser's Act duties and restrictions. Thus, experts could be liable for fraudulent or failed offerings.[120] Possible liability concerns under the Advisers Act include financial penalties or imprisonment for willfully violating[121] the Advisers Act's registration[122] or reporting requirements;[123] duty to "prevent misuse . . . of material, nonpublic information";[124] and ban on "fraudulent, deceptive, or manipulative" "acts, practices, and courses of business[.]"[125]

A second liability concern is that Regulation Crowdfunding offerings are expressly subject to section 12(a)(2) antifraud liability under the Securities Act of 1933.[126] Following the U.S. Supreme Court

> dealer whose performance of such services is solely incidental to the conduct of his business as a broker dealer and who receives no special compensation therefor; (D) the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation; (E) [government securities advisers]; (F) [credit rating agencies], unless such organization engages in issuing recommendations as to purchasing, selling, or holding securities or in managing assets, consisting of in whole or in part of securities, on behalf of others; (G) any family office . . . (H) such other persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order.

15 U.S.C. § 80b-2(11) (2012). The SEC has noted three elements to qualify as an investment adviser, (1) compensation is "broadly construed" and generally refers to "the receipt of any economic benefit"; (2) "[g]enerally, a person providing advice about specific securities [is] 'engaged in the business' unless specific advice is rendered only on a rare or isolated occasion"; and (3) a person "clearly" advises others about securities "if he provides advice to others about specific securities," although "more difficult questions arise with less specific advice, or advice that is only indirectly about securities." DIV. OF INV. MGMT., U.S. SEC. & EXCH. COMM'N, REGULATION OF INVESTMENT ADVISERS BY THE U.S. SECURITIES AND EXCHANGE COMMISSION 2–3 (Mar. 2013) (citations omitted), https://www.sec.gov/about/offices/oia/oia_investman/rplaze-042012.pdf [https://perma.cc/2QNK-DABK]. Additionally, the SEC has indicated that an individual or entity does not act as an investment adviser by merely hosting issuer-provided information on an investment online. *See* Angel Capital Elec. Network, 1996 SEC No-Action Letter, 1996 WL 636094, at *1–2 (Oct. 25, 1996).

119. Mark Roderick, *Are Crowdfunding Portals Investment Advisers?*, CROWDFUNDING & FINTECH L. BLOG (Feb. 9, 2015), https://crowdfundattny.com/2015/02/09/are-crowdfunding-portals-investment-advisers/ [https://perma.cc/BDJ6-7D93] (discussing whether crowdfunding portals are investment advisers under the Advisers Act).

120. *See, e.g.*, 15 U.S.C. §§ 80b-17, 80b-3, 80b-4, 80b-4a, 80b-6. For the codified version of the Advisers Act, see 15 U.S.C. §§ 80b-1 to 80b-21.

121. 15 U.S.C. § 80b-17.

122. *Id.* § 80b-3.

123. *Id.* § 80b-4.

124. *Id.* § 80b-4a.

125. *Id.* § 80b-6.

126. Pub. L. No. 73-22, 48 Stat. 74 (1933) (codified as amended at 15 U.S.C. § 77 (2012)); 15 U.S.C. § 77*l*(a)(1).

case of *Pinter v. Dahl*,[127] section 12(a)(2) defendants include (1) those that pass title to securities, which is in this case the startup, and (2) those that solicit investors for value, potentially the experts.[128] The pertinent question in crowdfunding is whether experts, by promoting a particular investment through message boards or investment clubs, rise to the level of solicitors for value.

According to Professor Steven Bradford, "[u]nfortunately, '[t]he courts have had a great deal of difficulty in defining precisely how much active participation is required [for a solicitation].' Several courts have read *Pinter* to require that the defendant must urge or persuade the investor to buy *the particular security*."[129] Such an interpretation would be a step closer to liability for experts promoting particular crowdfunding offerings. Thus, experts should walk a fine line in enticing others to join them in crowdfunding offerings but not becoming responsible for the startup's mistakes. Perhaps an expert can simply acknowledge they are participating in a particular investment, as AngelList emails do,[130] but not promote it beyond that. More clarity from the SEC is required to understand the limits of expert opinion in crowdfunding offerings.

CONCLUSION

The great experiment of crowdfunding is off and running. The law firm Drinker Biddle recently performed an analysis of the first fifty

127. 486 U.S. 622 (1988).

128. *Id.* at 647 ("The language and purpose of § 12(1) [(now § 12(a)(1))] suggest that liability extends only to the person who successfully solicits the purchase, motivated at least in part by a desire to serve his own financial interests or those of the securities owner. If he had such a motivation, it is fair to say that the buyer 'purchased' the security from him and to align him with the owner in a rescission action."); *see* C. Steven Bradford, *Shooting the Messenger: The Liability of Crowdfunding Intermediaries for the Fraud of Others*, 83 U. CIN. L. REV. 371, 392 n.125 (2014). The Supreme Court in *Pinter* took no position on whether its analysis under section 12(a)(1) also applies to section 12(a)(2). *See Pinter*, 486 U.S. at 642 n.20. But the lower courts have held that it does apply. *See, e.g.*, Craftmatic Sec. Litig. v. Kraftsow, 890 F.2d 628, 635 (3d Cir. 1989); Moore v. Kayport Package Express, Inc., 885 F.2d 531, 536 (9th Cir. 1989); Crawford v. Glenns, Inc., 876 F.2d 507, 510 (5th Cir. 1989); Capri v. Murphy, 856 F.2d 473, 478 (2d Cir. 1988).

129. Bradford, *supra* note 128, at 393 (second alternation in original) (quoting THOMAS LEE HAZEN, 2 TREATISE ON THE LAW OF SECURITIES REGULATION 290 (6th ed. 2009)) (citations omitted).

130. *See* Ibrahim, *supra* note 3, at 583–84; *Terms of Service*, ANGELLIST (Mar. 31, 2016), https://angel.co/terms [https://perma.cc/27BR-XWAS] (stating that AngelList "do[es] not act as an investment adviser to any [i]nvestor(s) and no part of [the AngelList website] is intended to constitute investment advice").

crowdfunding offerings.[131] It found that issuers sought to raise a median of only $55,000 per offering, but would take more should there be additional interest.[132] The analysis also found that these were startups with a median age of just less than a year, so very early stage.[133] This fits with my earlier prediction that potentially promising startups seek crowdfunding dollars as a substitute for friends and family money.[134] These startups are not being rejected by angels or VCs per se—they are simply too early stage to put to good use the amounts angels and VCs would invest. Or, perhaps they are not the type of companies that will attract angels or VCs at all. Still, these startups will now have a better chance of succeeding in crowdfunding due to the ever-increasing role that expert opinion will play in this medium.

True crowd-based investing was always a fantasy. A website named Piqqem tried it. In Piqqem, "before you can see what the crowd thinks you have to give your own prediction."[135] As its then-CEO explained, "we differ from other sites in that we are a true wisdom of crowds sourcing application."[136] Piqqem appears to have failed,[137] and with good reason. Crowds are not well equipped to make wise investments in startups, but experts are. And these experts can send signals to unsophisticated investors to allow these investors, too, to participate in early-stage startup investing—thus potentially fulfilling crowdfunding's promise.

131. Leaf et al., *supra* note 91.

132. *Id.*

133. *Id.* ("Early data shows that issuers tend to be early-stage startups, with a median issuer age of just 354 days. Nevertheless, nine of the issuers were more than five years old . . . .").

134. Ibrahim, *supra* note 3, at 589 (stating that startups who crowdfund "might seek only $20,000 to develop a prototype, hire a lawyer to incorporate, or obtain a patent. Instead of bootstrapping with credit cards or hitting up the entrepreneur's parents, these startups might look to Title III" (footnote omitted)).

135. Erick Schonfeld, *Can Piqqem Use the Crowd To Pick Stocks? Don't Bet On It*, TECHCRUNCH (Nov. 7, 2008), https://techcrunch.com/2008/11/07/can-piqqem-use-the-crowd-to-pick-stocks-dont-bet-on-it/ [https://perma.cc/7AYN-X6EH].

136. *Id.*

137. *Welcome to Our Site*, PIQQEM: INVESTING & INVESTMENT TIPS, http://www.piqqem.com/# [https://perma.cc/CN8D-6KVS]. There is no recent information on the Piqqem crowdfunding site online—all news articles about the company are at least 6 years old. Piqqem.com is still an active website, but the company's provided phone number has been disconnected. The site most recently appeared to host a blog. *Id.*