

Crowdfunding, Online Payments, and Charitable Fundraising

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What is Crowdfunding?

- “Crowdfunding” is simply raising funds from a large number of funders to support a project, cause, or organization
 - Nonprofits engaged in fundraising from the general public have been “crowdfunding” for centuries!
 - What’s new: A profusion of online crowdfunding platforms
 - Crowdfunding Centre:
Today there are
over 450 online platforms

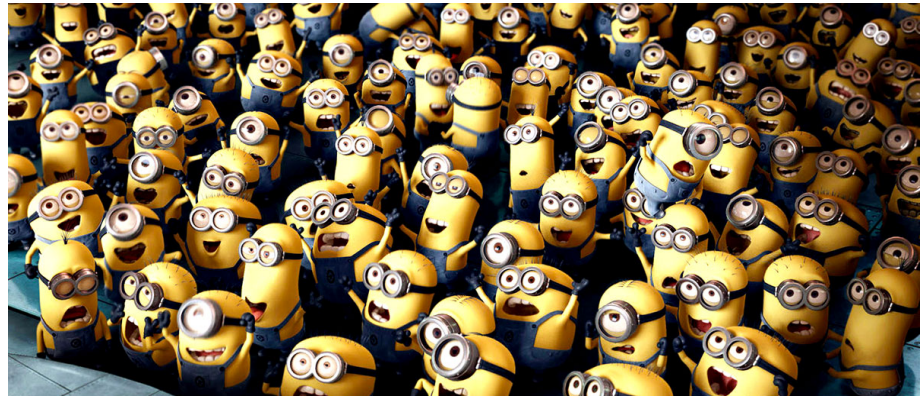


DONATIONS
REWARDS-BASED
CROWDLENDING
CROWDEQUITY

Crowdfunding Models (continued)

■ Donations

- Gifts from donors , no (legal) strings attached



■ Rewards-based

- A campaign stating that upon achieving a stated goal (*e.g.* receiving \$[x] in donations, having [y] number of people sign up for a marathon etc.), a reward will be provided to each participant
- Creates a contractual obligation to provide the reward once the stated condition(s) have been satisfied

Crowdfunding Models (continued)

- Crowdlending

- Borrowers are matched with lenders on a platform to make or receive unsecured microloans

- Crowdequity

- SEC rules allow a company to raise up to \$1M by selling securities through registered crowdfunding portals



- Provide some relief from SEC registration and reporting, or accredited investor requirements applicable to companies conducting larger offerings

Online Crowdfunding Options

■ Donations

- Add a “donate” button to your existing site



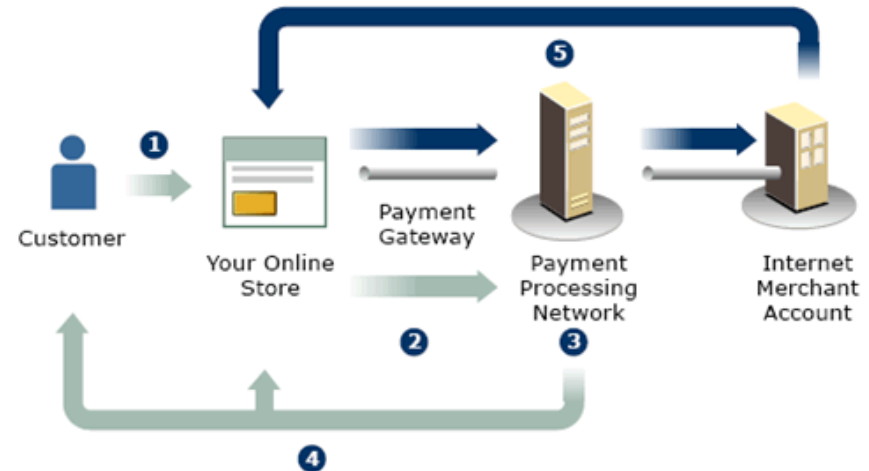
- Use a turnkey donation campaign solution

- Get listed on a charity directory



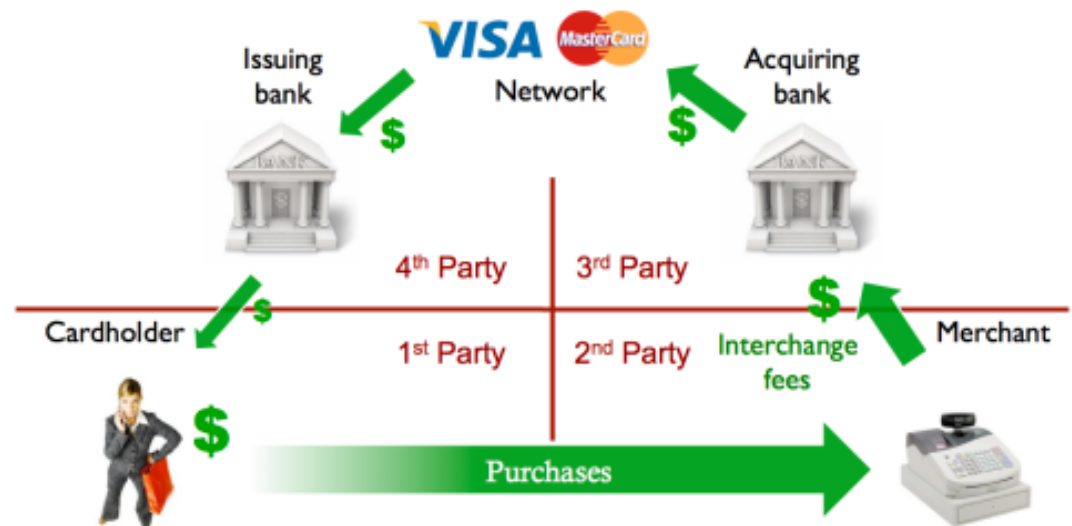
Online Payments – The Basics

- Online payments require a gateway, payment processor, and payment network
 - An online **gateway** captures payment card information, similar to a point-of-sale device at a store
 - A **payment processor** formats and batches the transaction, and transmits it to a member of the network that the payment card is on.
 - A **payment network** routes transactions between its members, and settles their net positions at the end of each day



Payment Networks – Inside the Black Box

- An open or four-party payments network consists of participating members and a central “switch.”
- Most payment networks only admit banks as members
 - A merchant can only submit transactions through an acquiring bank or its agent
 - A purchaser must have a bank-issued card or account in order to send money to the merchant



Donations – The DIY Option

- Online gateways/processors like PayPal and Stripe provide APIs or hosted white-labelled webpages that allow you to accept payments within your website.



– Pros:

- Lowest cost option – per transaction fee can be less than half of that charged by turnkey solutions
- Maintain full control over your site and user experience

– Cons:

- Requires some coding and integration to implement
- Does not drive traffic to your website or campaign

Donations – The Turnkey Solution Option

- Platforms like Network for Good and Indiegogo provide a complete suite of functionality needed to run a donation campaign, including customizable campaign website, social media integration, reports, and payments acceptance

- Pros:

- One-stop shop for all your crowdfunding donation needs
- Integrated social media and data analytics capabilities allow targeted marketing and promotion

- Cons:

- Highest cost option in terms of fees
- May present a credit or compliance risk depending on their level of involvement in payments acceptance



Donations – The Charity Directory Option

- Online directories like JustGive and Causes provide organized communities or searchable listings that connect individual or businesses with causes and nonprofits

- Pros:

- Provides access to community members with a common cause or interest
- May allow greater flexibility to use other services of your choice

- Cons:

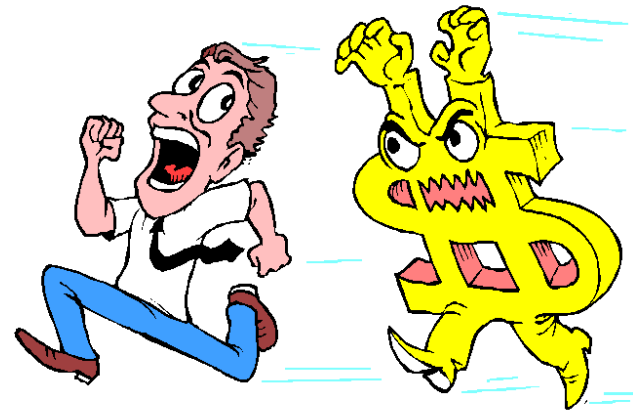
- Search and community functionalities will generate multiple results besides your organization
- User interface tends to be cluttered



Donations – Key Considerations

■ Cost

- Payment processor and platform fees are a mix of fixed per transaction fees, percentage per transaction fees, and monthly or annual fees
 - Build models incorporating your anticipated number of campaigns and participants, transaction amounts and volumes in order to meaningfully compare different options and platforms
- On some platforms, payment processor fees are passed through separately from platform fees
 - Make sure to read the fine print and not the advertising – or risk paying double what you expected in fees



Donations – Key Considerations (continued)

■ Third-Party Risk

- Donations that are processed directly between donors and donees by PayPal or Stripe only settle through entities that are subject to safety and soundness regulation (money transmitters, banks etc.)
- Some platforms accept payments on your behalf into their corporate accounts, and then periodically wire, write checks for, or ACH funds to donees
 - Risk of loss through platform bankruptcy, security breach or employee malfeasance
 - Risk that platform will be deemed a money transmitter by federal or state regulators and ordered to cease and desist their activities
 - Many sites disclaim all liability to you in their terms of use – even for donated funds

Donations – Key Considerations (continued)

■ Campaign Structure: Flexible vs. Fixed

- Flexible campaigns are “keep-what-you-make,” even if the fundraising target is not met
- Fixed campaigns are “all or nothing” where failure to meet the fundraising target results in the refund of all donations and the waiver of all fees
- If using a turnkey provider, make sure they support the structure that works for you



Donations – Key Considerations (continued)

■ User Experience

- Tradeoff between maintaining control of user experience and obtaining additional functionalities through outsourcing
 - If you are using a turnkey solution or a charity directory and the “look and feel” of your campaign site is important to you, look into the degree of customization that the platform supports



- Make sure the platform’s service and customer support meets your standards – review BBB ratings and conduct test transactions before running a full campaign

Donations – Key Considerations (continued)

■ Marketing

- Existing contacts: Which types of contacts and social media does your donor base use? Your platform should support integration of your campaign with these
- Prospective contacts: Charity directories can provide you with access to a network of potential donees. They and some turnkey solutions can also provide you with advice on how to effectively target donors



Some Major Compliance Areas of Concern

- Who is responsible? The crowdfunding platform, or the organization using that platform to raise funds?
- Federal tax compliance
 - Applies to recipient organization, platform, and donor alike
- Fair trade practices laws at both federal and state levels
- State and local law:
 - Charitable solicitation rules
 - State and local sales and use tax



Federal Tax Issues

- Charitable contribution deduction for contributions made through crowdfunding platforms
 - Who is the donee and is responsible for issuing the acknowledgment of each contribution? Factors to consider:
 - Is the crowdfunding platform operated by a charitable organization?
 - Does the crowdfunding platform have any discretion and control over the use of contributed funds, or is the relationship strictly one of agency?
 - What is the amount of the deduction? Does the deduction include the amount retained by the operator of the crowdfunding platform?



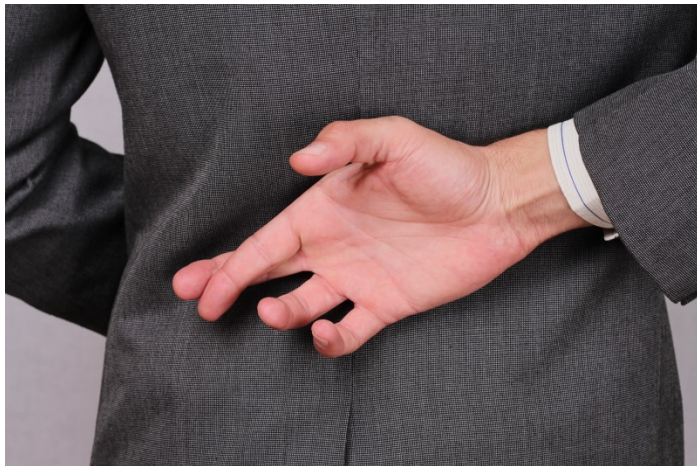
Federal Tax Issues

- 501(c)(3) organizations operating crowdfunding platforms
 - These are issues for both donors and recipient organizations, too!
 - Due diligence for recipient organizations
 - Private inurement or more-than-incidental private benefit
 - May threaten a platform’s 501(c)(3) status or trigger punitive excise taxes against the platform
 - Operated for charitable purposes? Some operators may provide service “like a business” and run afoul of the Commerciality Doctrine
 - Public charity status is essential; it is virtually impossible for a private foundation to run a crowdfunding platform and comply with PF rules



Fair Trade Laws

- Federal law and state laws in all 50 states proscribe business practices that are deceptive or unfair
 - Federal fair trade laws apply to interstate commerce and are enforced by FTC
 - State fair trade laws enforced in most states by the Attorney General



- Both crowdfunding platforms and recipient organizations may be held liable
 - Both civil and criminal penalties apply
- Ensure all communications to public are complete, accurate, and not deceptive, particularly concerning use of funds

State Charitable Solicitation Laws

- Perhaps the biggest minefield in charitable fundraising, whether crowdfunding is involved or not
- Use of crowdfunding platform **does not** insulate a charitable organization from state charitable solicitation laws, and can increase exposure in some respects
- Crowdfunding platform operators are not always informed
- Key players may be classified as any of the following:
 - Professional fundraiser
 - Fundraising counsel
 - Commercial co-venturer
 - Charitable organization



State Charitable Solicitation Laws

- What states have jurisdiction?
 - The state where an organization soliciting funds is domiciled
 - Any state where the organization is targeting its fundraising
 - What about Internet solicitation?

- Charleston Principles
 - Law in only two states (TN and CO), but represent charity regulators' most up-to-date thinking, and are helpful elsewhere
 - Jurisdiction applies if organization receives contributions:
 - “on a substantial basis”
 - “on a repeated and ongoing basis”

State Charitable Solicitation Laws

■ Registration for Charities

- Approximately 45 states require registration for any organization soliciting funds for charity, including charities themselves
- Which states have jurisdiction over my organization's fundraising?
- Use of a crowdfunding platform may trigger Charleston Principles analysis
- Is the crowdfunding platform operator required to register?
- On the other hand... can the presence of a registered crowdfunding platform operator relieve the recipient organization of registration?
- Can be a complex, expensive, bureaucratic process

State Charitable Solicitation Laws

- Professional fundraiser (“PFR”) status
 - A PFR **solicits** funds for **consideration**
 - PFR status triggers heavy regulation in almost every state
 - Some states exclude 501(c)(3) organizations from PFR status
 - Are crowdfunding platforms PFRs? The question is unsettled. Who is doing the soliciting?
 - Crowdfunding platforms serving nonprofit organizations should be aware of this issue

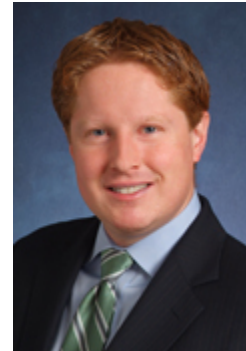
State Charitable Solicitation Laws

- Commercial co-venturer (“CCV”) status
 - A CCV is a for-profit business that **represents to the public** that sales of goods or services benefit a charitable purpose
 - Some crowdfunding promotions where goods are sold may trigger CCV requirements
 - Key question of CCV status: **Who is making the representation?**
 - CCVs are regulated in 24 states; requirements vary widely, but usually include:
 - Written contract between CCV and charitable organization
 - Disclosure of amount per unit sold that goes to charity
 - Registration (in 10 states)

Questions?



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