

NATIONAL REVIEW

How a 2012 Law Unleashed ‘Crowdfunding’ — in Entertainment and Elsewhere

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In 2000, Paul Scanlan and Jeff Annison had the prescient idea for MobiTV, a service that would stream live TV to phones. Thinking their business proposal had a real chance, the two pitched it to their friends and family, who agreed and wanted to show their financial support. By selling shares in the company to a number of small contributors, they managed to secure seed money.

But when they tried to move forward, they ended up having to return that money. Their investors were not “accredited,” and therefore could not legally invest in securities that were not registered with the authorities. According to SEC regulations, “accredited investors” needed to be millionaires, which naturally ruled out a lot of people who might be interested in investing in a young business. Annison and Scanlan did eventually raise over \$100 million for MobiTV, but the way an arbitrary regulatory barrier set back their start stuck with them.

The Jumpstart Our Business Startups (JOBS) Act was passed in 2012, and starting in 2016 it removed a number of barriers to these kinds of investments — now called “equity crowdfunding.” As it turns out, the law also facilitated a number of films starring A-list actors, thanks to Scanlan, Annison, and a new company called Legion M.

“Crowdfunding” tends to bring to mind platforms such as Kickstarter, Indiegogo, and GoFundMe. Such platforms existed before the JOBS Act — but, as Thaya Brook Knight of the Cato Institute explains, until then they were not legally allowed to facilitate actual investments. Companies could provide various perks to those who contributed, such as “preferred status on a waitlist for the forthcoming product, a T-shirt, or a handwritten letter of thanks from the company’s founder.” But they couldn’t give a traditional return: a promise that if the project succeeded, a portion of the profits would go to the contributors.

In theory, this protected unsophisticated investors from securities that were not subject to various transparency requirements and other regulations. In practice, it meant that investing in many new projects was the place of the very rich alone — and, bizarrely, that one could solicit money from the public only if one did not plan to pay a return on the investment. Certainly there is something to be said for restrictions that curb irresponsible behavior, but this setup essentially walled off an entire part of the economy.

This situation attracted criticism, both from free-market Republicans and from Democrats. As a result, Congress debated a series of reform packages and enacted the JOBS Act in 2012. The act's crowdfunding provisions created portals through which a firm could solicit funds from small investors. These funding portals are strictly regulated, and the new system does limit how much someone can invest, which has earned complaints from some libertarian-minded observers. But it's a reasonable compromise, and, if nothing else, it's certainly an improvement on the previous rules.

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Scanlan and Anison closely followed the course of these economic reforms, and their next business idea was built around the possibilities of equity crowdfunding. Anison wrote a 2016 blog post celebrating the reforms in the language of economic freedom and personal empowerment; he pointed out that, during the years when actual investments had been out of reach, there had been “nothing stopping ordinary Americans from ‘investing’ money in Las Vegas, lottery tickets, or TV evangelists.” With the barriers removed, he wrote that “the general public [can] participate in early stage financing, a domain that for the last 80 years has been the exclusive purview of venture capitalists and high-net-worth individuals.”

Almost immediately after the provisions took effect, Legion M hit the ground running, says Terri Lubaroff, the company's chief operating officer. For a few years, fans had been crowdfunding creative projects, including video games and movies — the Veronica Mars film was famously funded by fans — but the JOBS Act created the opportunity for fans to be real stakeholders in an entertainment business. And equity-crowdfunded entertainment companies take that to another level.

Legion M, which calls itself “the world's first fan-owned entertainment company,” is able to leverage its widely distributed ownership to take on projects that major studios won't — such as this year's Mandy, a critically acclaimed psychedelic horror film starring Nicholas Cage — and is able to attract other major actors, such as David Tennant and Anne Hathaway, to its films. The company's next film, Girl with No Name, visits another neglected genre: It tells the story of a lone female gunslinger and will be accompanied by a comic book by acclaimed artists Tula Lotay and Dani Strips, both of whom are longtime Western enthusiasts.

In two years, Legion M has already released several films, as well as other projects, and that is just one company. Equity crowdfunding opens the door for new kinds of business models to emerge in all kinds of industries, not just entertainment. Among the startups using Wefunder (one of the new investment portals) are Phenomix Sciences, a blood-testing system developed by two Mayo Clinic obesity doctors to allow for more tailored weight-loss treatment, and Tesseract, a company that is developing cheaper propulsion systems for satellites.

The startup world is dynamic by its nature, and there is risk involved with any new venture. But the fact that ordinary people can now invest at this stage of a business is changing the landscape. For some projects, it's easier to find a large number of people each willing to put up \$100 than it is to find a venture capitalist eager to fork over millions.

The JOBS Act empowered individuals and small businesses in various ways; it also, for example, increases the number of shareholders that companies may have before they face the requirement to register as public companies. But its equity-crowdfunding provisions might prove

to be the most transformative. In just two years, a new startup atmosphere has been flourishing — and within two more, we should expect to see its effects ripple even further.