Are Syndicates the Killer App of Equity Crowdfunding?

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Information asymmetry presents a challenge to equity crowdfunding just as in other markets for equity capital. Investors are less likely to finance startups when it is difficult to assess quality. Syndicates reduce market failures caused by information asymmetry by shifting the focal investment activities of the crowd from startups to lead investors. Syndicates align the incentives of issuers, lead investors, and follow-on investors by providing incentives for lead investors to conduct due diligence, monitor progress, and exploit their reputation. Preliminary evidence foreshadows a meaningful role for syndicates in the allocation of capital to early-stage ventures. (Keywords: Internet, Entrepreneurship, Venture Capital, Crowdsourcing, Silicon Valley, Investments, Innovation, Economic Growth)

Information asymmetry is a primary barrier to the financing of early-stage ventures. An extensive literature in finance and entrepreneurship explore this in the context of venture capital and, to a lesser extent, angel investing.[1] Investors hesitate investing in a seemingly promising new venture because they do not have enough information to assess its true value. That is because a lot of information predictive of success is tacit. It is shared through socialization and difficult to transfer to others by writing it down.[2] For example, the personalities of and relationships among founders are of central importance in the early stage of a venture, especially since business plans often change many times before a company is profitable. Yet, information about the founders is difficult to codify and credibly communicate. At the same time, entrepreneurs are reluctant to sell equity in their venture for a price they perceive to be overly discounted for risk, given the more complete information they have about their own venture.

Markets for early-stage capital use a variety of mechanisms to overcome information asymmetry. Venture capital firms invest considerable resources in due diligence and monitoring. To do so efficiently, they often focus on startups located nearby. The shorter distance facilitates the flow of both tacit and codified information.[3] In other words, proximity reduces the costs associated with information asymmetry, enabling early-stage investments. Similarly, angel investors spend time and money

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on due diligence and monitoring, which generates highly localized patterns of angel investments.[4]

These information asymmetries limit the set of potential investment opportunities for a given angel investor or venture capital firm, suggesting a potential market failure: The monitoring and due diligence required for each transaction may be sufficiently costly that many potentially value-creating deals never happen, especially those where the investor and issuer are not co-located.

Venture capital firms use a variety of tools to try to overcome these challenges. They structure financing in stages, so that they can cut off new financing from unsuccessful firms.[5] They visit the entrepreneur to monitor activities and review financial reports.[6] They demand a role on the firm's board of directors.[7] In addition, they "syndicate" by making investments together with other venture capital firms. Syndication enables a venture capital firm to diversify their portfolio while providing incentives for due diligence and sufficient financing.[8] Syndication also provides a "second opinion" as other experienced venture capital firms often conduct their own due diligence.[9]

Angel investors face the same asymmetric information challenges as venture capitalists. They use some of the same tools to overcome these challenges. Still, both venture capital and angel investors make disproportionately local investments, largely in response to challenges related to information asymmetries.

Crowdfunding allows entrepreneurs to raise capital from many "strangers" online.[10] Equity crowdfunding is a relatively new tool for angel investors to finance early-stage ventures. Often, "the crowd" is limited to accredited investors only. Equity crowdfunding provides these investors with a wider range of investment opportunities than those available in their specific location. The term "equity crowdfunding" specifies that investors receive equity from the issuing firm in return for their capital, as opposed to rewards, such as in the case of popular crowdfunding platforms such as Kickstarter and Indiegogo. In the latter cases of non-equity-based crowdfunding, the funder pre-purchases a product or service or simply donates the funds with no expectation of a tangible return.

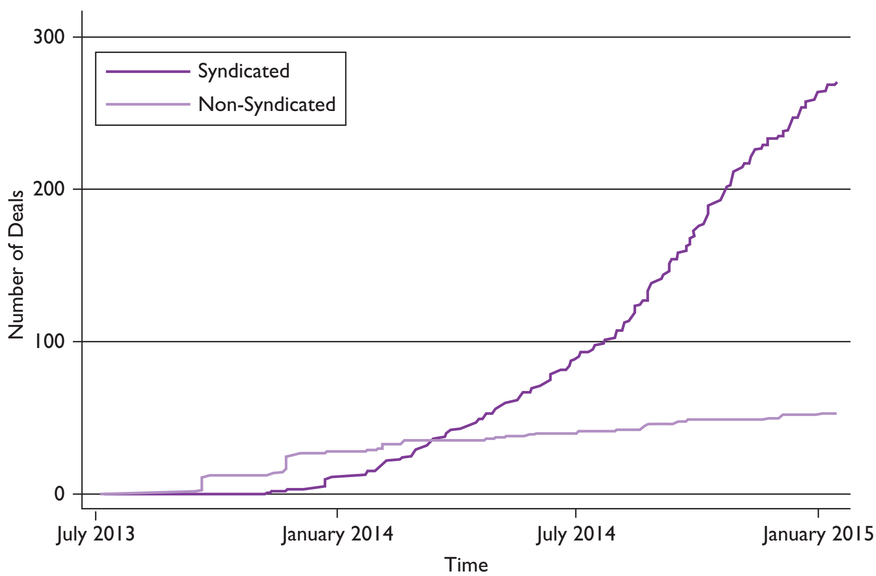
Despite the detailed information about founders and their ventures provided on crowdfunding platforms, information problems persist. The internet does not facilitate the transmission of certain types of information that require face-to-face interaction.[11] For example, using only online information makes it difficult to assess the founding team in terms of their grit, determination, interpersonal dynamics, and trustworthiness. Angel investors and venture capital firms, especially those leading an investment round, usually meet face-to-face with founders as they conduct due diligence in order to evaluate these and other characteristics they believe to be predictive of venture success.

In this article, we argue that equity crowdfunding syndicates can overcome many of these challenges. In many ways, they perform a role similar to venture capital syndicates. They enable a diversified portfolio while ensuring that due diligence is conducted. However, equity crowdfunding syndicates differ from venture capital syndicates in that they serve primarily as a way for well-informed lead investors to leverage their knowledge and bring in substantial funds from a less well-informed and well-connected "crowd."

Specifically, equity crowdfunding syndicates involve lead investors bringing deals to a crowd of backers. Syndicates have the potential to address key information problems and unleash the power of the internet on market failures in angel investing. Furthermore, the syndicate structure allows platforms to provide financial incentives to individuals for solving the information problem through the implementation of a "carry." (Carried interest is a fraction of the profits earned on capital invested by the other members of the syndicate.)

Preliminary evidence shows that the syndicate structure and incentive system may be quite effective for equity crowdfunding. Although it is recent, its use is growing in absolute and relative terms. According to the CEO of UK-based SyndicateRoom, the syndicate format in the UK has raised many times the amount raised by non-syndicate platforms.[12] On AngelList, the leading equity crowdfunding platform in the United States, syndicated deals have not only grown but overtaken non-syndicated deals in terms of the number of ventures attempting to raise capital, the number of ventures that successfully raise a seed round, and the total amount of capital raised. In Figure 1, we report the cumulative trend in

FIGURE 1. Cumulative Number of Successful Syndicated and Non-Syndicated Deals on AngelList



syndicated versus non-syndicated deals since AngelList began allowing online investments in March 2013. “Syndicates” were introduced in June 2013 and started to take off a few months later. By March 2014, the total number of successful syndicated deals exceeded the total number of successful non-syndicated deals, and this trend continues.

How Syndicates Work

There are many equity crowdfunding platforms (e.g., AngelList, FundersClub, WeFunder, Crowdcube, CircleUp, Crowdfunder, OurCrowd, and SyndicateRoom). These platforms operate as two-sided markets in which the platforms try to attract both investors and entrepreneurs.[13] In order to succeed, there need to be enough investors so that it is worthwhile for entrepreneurs to post their ventures on the platform and enough ventures so that it is worthwhile for investors. Although the various platforms are similar on some dimensions, they each have some unique market design features aimed at attracting certain types of investors or ventures.

In this article, we focus on a particular feature: syndicates. Not all equity crowdfunding platforms have syndicates. Among those that enable syndicate-like investing (including AngelList, SyndicateRoom, and OurCrowd), we focus on AngelList, the largest U.S.-based platform. The basic economic principles associated with syndication apply across platforms. We focus on AngelList for simplicity and to link this discussion with the data we present below.

On AngelList, individuals, angel groups, and venture capital (VC) funds can all form syndicates. We focus here on individuals. Individual angel investors create a syndicate profile online, providing basic information for potential backers such as how many deals they expect to syndicate each year and their typical investment size. As a syndicate “lead,” the investor commits to providing a written investment thesis for each investment and to disclosing potential conflicts of interest. Other accredited investors, who apply to participate in one or more specific syndicates, are referred to as “backers.” If accepted by a syndicate lead, then the backer agrees to invest in the lead’s syndicated deals on the same terms as the lead and to pay the lead a carry. These investments occur through the AngelList platform.

Backers are able to opt out of specific deals, but this is not encouraged. Backers pay a 5–20% carry per deal to the syndicate lead as well as 5% to AngelList. Thus, backing a syndicate is similar to investing in a VC fund but with at least four important differences: backers may choose which portfolio companies to invest in; backers can stop backing at any time; VC funds usually require significantly higher minimum investment amounts; and leads typically invest more than general partners per deal on a percentage basis (general partners of VC funds invest only 1% on average).

AngelList provides the following example on its website to illustrate how it works: “Sara, a notable angel, decides to lead a syndicate. Investors ‘back’ her syndicate by agreeing to invest $200K in each of her future deals and pay her a 15% carry. The next time Sara decides to invest in a startup, she asks the company for a $250K allocation. She personally invests $50K in the startup and offers an opportunity to invest up to $200K to her backers.” A detailed description of how this works is provided on the AngelList website here: <https://angel.co/syndicates>.

FIGURE 2. Top Five Individuals Who Are Syndicate Leads on AngelList as of February 2nd, 2015

Lead	Markets	Backers	$ backed	Past Investments	Location
Gil Penchina	Mobile, e-commerce, marketplaces	767	$5,240,451	LinkedIn, PayPal, Fastly, Rally Software	San Francisco Bay Area
Tim Ferriss	Consumer internet, Collab. consumption	776	$4,133,063	Twitter, Facebook, Alibaba, Duolingo	San Francisco Bay Area
Jason Calacanis	Mobile, e-commerce, video streaming	527	$1,889,812	Uber, Evernote	Greater Los Angeles
Dave Morin	Digital Media, Crowdfunding, content discovery	423	$1,709,050	Path (founder), Slow, Nest, Pinterest	San Francisco Bay Area
Naval Ravikant	Clean technology, e-commerce, mobile commerce	126	$1,474,483	Twitter, Uber, Yammer, Stack Overflow (AngelList cofounder)	San Francisco Bay Area

As of February 2015, AngelList has approximately 120 active syndicates. Some have invested with top-tier venture capital firms (e.g., Sequioa (Lifx), Andreessen Horowitz (uBiome), Khosla Ventures (OpenDoor), and Accel Partners (Gametime)). Unsurprisingly, the distribution of syndicates is highly skewed. For example, the median number of backers in successfully closed deals is 29 whereas the maximum is 141. Similarly, the median investment amount is $2,500 and the maximum is $860,000. In Figure 2, we summarize key characteristics of the top five individuals who lead syndicates. This list highlights four key observations. First, concerning the skewness in the distribution, there is a significant spread even among the top five individuals. The top individual has six times as many backers and 3.5 times as much capital from backers than the fifth individual. Second, all five are focused on broad, internet-related categories that are likely of interest to and accessible by a wide range of backers (as opposed to medical technology or advanced materials, for example). Third, all have easily interpretable reputations due to prior investments in high-profile, consumer-facing ventures such as PayPal, Facebook, and Uber. Finally, four of the five live in the Bay Area, and the other is also based in California.

The Information Problem

Given that information asymmetry is a primary barrier to the financing of new ventures, we next discuss how this asymmetry can impede the creation of a well-functioning market. This idea was formally introduced to economics by George Akerlof in his Nobel Prize-winning research on the market for used cars.[14] He demonstrated how the existence of “lemons,” or bad cars, in a population of otherwise good cars could create the conditions under which no one is willing to pay a good used-car price, even for a used car in good condition. That is because it is costly for sellers of good cars to credibly communicate their private information—that their car is in good condition—because buyers know that the sellers of bad cars have an incentive to represent their cars as "good" and because it is difficult for buyers to tell the difference. This problem—labeled *information asymmetry* because it arises when the buyer has significantly less information than the seller and it is costly to credibly communicate the truth—poses a substantial challenge to the operation of efficient markets across many industries (including finance, insurance, health care, and online retailing) and early-stage equity capital.

Many financial institutions and rules have been created to overcome issues of information asymmetry, including credit scores, reporting requirements, accounting processes, and rules on insider trading. As noted above, venture capital firms and angel investors spend considerable effort in due diligence and monitoring. Interpersonal relationships are particularly important in early-stage finance.[15] This includes support from friends and family, whose investments may provide a signal to others that the entrepreneur is trustworthy and serious about building their business.[16]

Many also recognize information asymmetry as a core issue for non-equity crowdfunding.[17] To partly address this issue, crowdfunding platforms have emphasized capital raised to date as an important signal of quality. This signal drives further investments.[18] Thus, in a sense, potential funders use prior funding by others as a signal of the "wisdom of the crowd." Research on crowdfunding in theatre has shown that the tastes of the crowd are somewhat similar to the tastes of experts.[19]

In other types of online transactions, the information asymmetry problem is addressed through a variety of market mechanisms. For example, online sellers engender trust through feedback systems (e.g., eBay, Amazon), branding and advertising (e.g., Nespresso), and trustworthy intermediaries (e.g., credit card companies).[20]

How Syndicates Solve the Information Problem

Syndicates employ a market design feature that enables a division of labor among investors. Lead investors conduct due diligence and monitor progress on behalf of other investors. Syndicates are designed such that lead investors endure a reputational and financial penalty for poor performance and enjoy reputational and financial rewards for good performance. Entrepreneurs face a reputational cost within their professional network if they fail to deliver results to the lead. This aligns the incentives of leads, backers, and entrepreneurs in a manner that directly addresses information asymmetry problems.

Overall, there are three central costs associated with asymmetric information in angel investing. The first is general awareness of the deal. It is costly to learn about early-stage deals, especially when ventures are prohibited from advertising private placements due to general solicitation regulations. The second is transaction costs. The overhead associated with small, ad hoc equity investment transactions increases with added communication and delivery costs. Third, the due diligence necessary to address the information asymmetry problems discussed above requires face-to-face interactions between investors and founders; thus, the cost increases with distance between the investor and the venture.

The first wave of equity crowdfunding platforms delivered a market design solution that significantly reduced the first two costs but not the third. Specifically, crowdfunding platforms enabled ventures to communicate key elements of their business plan to a wide audience of accredited investors in a manner that was standardized and efficient to consume. Furthermore, electronic platforms enabled accredited investors to invest relatively small amounts of capital in a cost-efficient manner. In other words, these platforms enabled investors to both learn about investment opportunities and to execute transactions, expanding the addressable market for early-stage capital. However, the third cost, resulting from information asymmetry, remained. Although investors could now make early-stage investments at a much lower cost, they had limited incentive to do so because they still faced a high cost of conducting due diligence.

Syndicates have provided a solution to the final cost barrier. They give lead investors both the ability and incentive to leverage the information they collect through their relationships and due diligence on behalf of other investors. Platform tools and features enable lead investors to communicate their skills and performance history and to put their reputation at stake. Unlike ventures that may only raise a single round of capital, active lead investors may raise multiple funds such that the value of protecting their relationship is high. Thus, like a trusted brand, a lead's reputation certifies the expected quality of a deal. Furthermore, lead investors earn a carry on their backers' capital, so their interests are aligned. The long-term success of syndicates will depend, among many things, upon an unrelenting enforcement by equity crowdfunding platforms of lead investors reporting any and all potential conflicts of interest, as well as by the availability of performance metrics on syndicate outcomes over time. The economics of this system rely upon backers trusting that the interests of the lead investor are fully aligned with their own and that the lead is actually able to select, monitor, and support high-quality deals.

It is important to recognize that syndicates are not unique to equity crowdfunding. Long before the rise of equity crowdfunding, syndicates had been used to reduce information asymmetry issues in venture capital investments. Venture capital syndicates enable information flows and investments across wider networks.[21] Even in venture capital syndicates, information flows are important: risky investments are relatively local.[22] Generally, venture capital syndicates help solve many, but not all, of the information problems in venture capital financing. The firms with the richest networks of syndicates have the widest set of possible investments. In addition, syndication provides lead investors with a second opinion on the quality of the investment and provides an opportunity for other investors to diversify their portfolios.[23]

Equity crowdfunding syndicates are similar to venture capital syndicates in that they encourage information flows about deals over wide networks. Furthermore, they enable a diversified portfolio while maintaining incentives for conducting due diligence. There are also some differences between equity crowdfunding syndicates and venture capital syndicates. Equity crowdfunding syndicates are particularly useful in creating incentives for lead investors to conduct due diligence. While venture capital syndicates do play a role in increasing due diligence incentives, researchers have focused on their more focal roles of encouraging information flows, enabling diversified portfolios, and providing a second opinion.[24] Furthermore, online crowdfunding syndicates are more sensitive to the cost of diligence than offline syndicates because the size of online investments can be so much smaller. The economics of investment are no longer attractive below some diligence-cost-to-investment-size ratio.

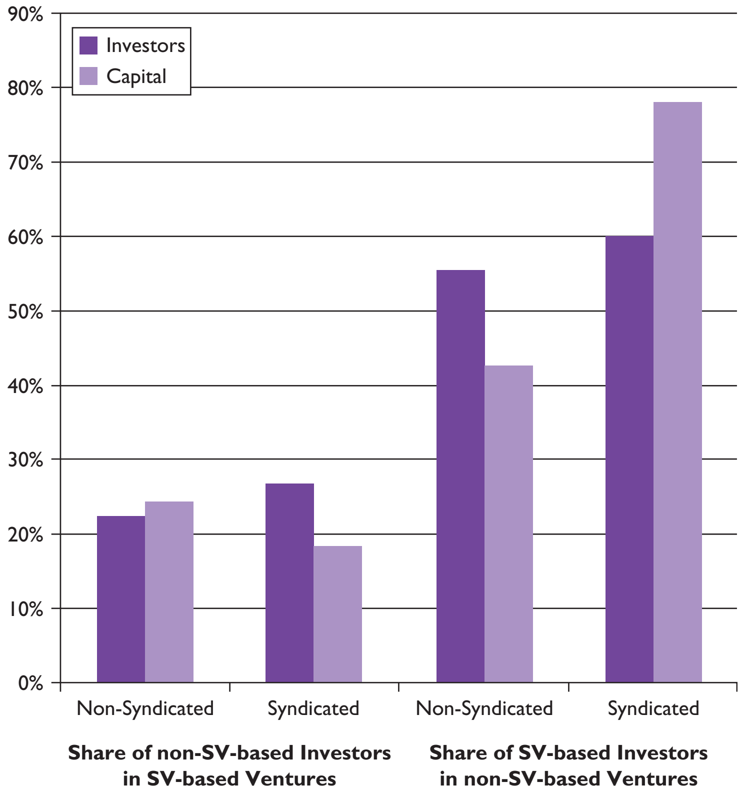
We use data on the geography of capital flows to provide preliminary evidence that is consistent with the thesis that syndicates significantly reduce the information asymmetry problem. Because information flows more easily when distance is smaller[25] and because social networks and social interaction both tend to be local,[26] researchers have used geographic proximity to measure the importance of information asymmetry.[27] For example, widespread home bias in investing has been used to document the importance of asymmetric information in investment decisions.[28] Such home bias is especially prevalent for new ventures, suggesting a particularly important role for asymmetric information. Given this, we use the degree of home bias in investing as a proxy for the importance of asymmetric information in restricting investment opportunities.

In Figure 3, we compare the geographic location of backers for syndicated versus non-syndicated deals, both of which are conducted online using the AngelList platform. If syndicates reduce the information asymmetry problem, then we expect to see more distant backers on syndicated compared to non-syndicated deals because investors have less need to be co-located with the venture in order to meet them offline to address information asymmetry issues, since investors can rely on the lead investor to do that offline work.

The data supporting this are striking. The share of investors (darker columns) that are distant from the startup is measurably greater for syndicated deals. This is true both for investors based outside of Silicon Valley (SV) investing in SV-based startups (bars 1 and 3), as well as for SV-based investors participating in non-SV-based startups (bars 5 and 7). In other words, syndicates give investors based outside SV enhanced access to SV-based deals. Moreover, syndicates are more likely to deliver better outcomes for other locations hoping to attract capital flows from SV, perhaps due to the benefits from connections to the SV-based network made possible by a SV-based lead investor (more than 60% of leads are based in SV). This is even more salient when looking at the share of capital instead of investors (lighter columns): whereas SV-based investors only account for 43% of the capital allocated to non-SV-based startups without syndication (bar 6), they account for 78% of the capital in syndicated deals (bar 8). However, non-SV-based investors represent a larger share of the capital invested in SV-based ventures in non-syndicated deals (bar 2 versus 4); this may be due to syndicate leads selecting investors they are familiar with or have offline information about (e.g., the value they offer beyond capital).

We focus on Silicon Valley-centric data because that region is disproportionately important in the market for early-stage capital and is the locus of entrepreneurial activity. However, we see similar patterns when we examine the full set of transactions: local investors represent 46% of investors (45% of the capital) for non-syndicated deals, but only 36% (40% of the capital) for syndicated

FIGURE 3. Investment Flows In and Out of Silicon Valley



ones. This is important. Reduced information asymmetries lessen the economic frictions associated with distant investments and thus extend the pool of potential matches between ventures and investors. This enhances the efficiency of the market for early-stage capital such that more and better (i.e., more strategic value) capital flows into entrepreneurial ventures, which facilitates more experimentation with respect to technologies, products, and business models. Thus, this shift in trade patterns for seed-stage capital across regions creates opportunities for entrepreneurs, investors, and policymakers.

Opportunities for Investors, Entrepreneurs, Platforms, and Policymakers

Syndicates enable a broad community of investors interested in exposure to the pre-VC asset class to leverage the expertise and due diligence of lead angel investors from around the world. As such, syndicates unlock meaningful opportunities for investors, entrepreneurs, platforms, and policymakers. We describe these opportunities below and summarize them in Table 1.

TABLE 1. Opportunities in Equity Crowdfunding Syndicates

Economic Agent	Opportunities
Lead Investors	Syndicates provide lead investors the opportunity to leverage their reputation, capability, network, and effort to generate higher returns. This is accomplished through a combination of: 1) the global distribution of standardized and verifiable information through the online platform, and 2) the market design that enables lead investors to collect a "carry" such that their return is not only a function of their own capital but also the capital of their backers.
Other Investors ("Backers")	Syndicates provide investors an opportunity to greatly expand their access to investment opportunities in the pre-VC asset class. This is accomplished by enabling investors to "back" lead investors who have both the capability and incentives to conduct due diligence and share investment opportunities, including those based in locations distant from the investment target.
Entrepreneurs	Syndicates provide opportunities to entrepreneurs who are well-connected to high-performing angel investors, perhaps because they are located in a region with many such investors. This is accomplished by increasing access to capital and relationships for entrepreneurs through angel investors who attract other backers with both capital and relationships to support the lead angel's investments.
Platforms	Syndicates provide platforms with a mechanism to overcome some of the challenges in equity crowdfunding related to information asymmetry. Platforms that can attract a critical mass of respected lead investors are likely to be able to attract both backers and entrepreneurs.
Policymakers	Syndicates provide policymakers an opportunity to take actions that influence capital flows into their jurisdiction. The rise of syndicates increases the returns to having high-quality angels in the focal region. Therefore, policymakers will benefit from the careful management of levers they control to attract and retain in their jurisdiction angel investors with strong reputations.

Investors

Syndicates facilitate opportunities for both general investors ("backers") as well as for lead angel investors. For general investors, syndicates increase the set of opportunities for allocating capital to the early-stage asset class. Investors now may choose to invest directly in local ventures with whom they have a personal connection, as they did before, but also in deals where they do not have a personal relationship and thus did not have access to in the past (both local and non-local). They accomplish the latter by relying on the reputation and incentives of lead investors. Syndicates shift the locus of investment from early-stage ventures to early-stage investors. In other words, general investors increase their reach by backing lead investors who then source investment opportunities. This increases diversification and might enable less consumer-oriented ventures to raise money through equity crowdfunding.[29] Although backers choose to invest in a lead's portfolio on a venture-by-venture basis, norms forming on these platforms suggest that the dominant pattern is for backers to back lead investors overall, rather than on specific transactions. Thus, syndicates may be viewed as offering general investors a new form of exposure to this asset class by way of backing lead investors rather than backing ventures.

Syndicates offer lead investors the opportunity to leverage their reputation, capabilities, relationships, and effort to increase their influence and returns.

Traditionally, the returns to angel investors with good reputations, capabilities, and relationships have been limited by the size of their local market because, with the exception of a few high-profile angel investors such as Fred Wilson, Ron Conway, and Paul Graham, most transactions at that early stage are local and therefore the sphere of influence and reputation of angel investors is also local. In addition, the return to angel investors is a function of the capital they deploy. Syndicates increase returns by scaling reputation and influence through the reporting of standardized information on transactions on a verifiable and globally accessible platform. In addition, syndicates enable lead angel investors to scale their returns through the carry mechanism that allows them to generate returns not just on their own capital but also on that of their backers. Thus, by increasing the returns to reputation, capabilities, relationships, and effort, syndicates enhance the incentives for angels to improve their performance with respect to sourcing and overseeing early-stage investment opportunities with significant upside potential. In addition, syndicates enable individuals with a valuable skill (e.g., a computer science professor with the ability to evaluate the technical advantages of startups in a specific domain, such as machine learning) to lead angel investment rounds despite not having access to significant amounts of capital either directly via their own personal wealth or indirectly through personal relationships. Thus, syndicates create opportunities for certain types of individuals to engage in lead investing, whereas this was less feasible before.

Entrepreneurs

Syndicates provide opportunities to entrepreneurs located in regions with high-performing angel investors who have or develop a good reputation since such lead angel investors attract capital from outside the region to back their investments. Because lead investors still focus most of their investments on ventures with which they can develop and nurture relations, they continue to concentrate their investments locally. Therefore, entrepreneurs who launch their businesses in regions with such angel investors benefit from increased access to both capital and the network of individuals who back lead investors. Some backers will be in a position to benefit the companies that receive their investment capital by providing access to relationships for customers, recruits, or partners. However, entrepreneurs in regions without reputable angel investors may not benefit. Under certain circumstances, entrepreneurs may even be harmed if the net effect of syndicates is to cause capital that might otherwise be invested in their region to instead flow out to other regions with more compelling angel investors.

Platforms

Because of the potential appeal of syndicates to investors and entrepreneurs, syndicates can help platforms attract participants on both sides of the market. A key challenge will be to attract high-profile, trustworthy lead investors who bring potentially valuable deals. The syndicates model depends on the idea that a lead investor's reputation will be easier to establish, and more enduring, than a particular entrepreneur's reputation. Thus, a platform cannot successfully implement a syndicates program without ensuring a large number of high-profile investors are willing to bring deals to the platform. If lead investors bring good deals to the platform, other investors are likely to be eager to participate and entrepreneurs are likely to be willing to have their ventures posted.

Policymakers

Syndicates provide policymakers an opportunity to take actions that influence capital flows into their jurisdiction. Policymakers are already acutely aware of the importance of local entrepreneurship; interventions abound to stimulate the birth and development of startups. The regulations that arise around equity crowdfunding will be important for shaping the industry in the future.[30] However, the rise of syndicates puts increasing emphasis on the role of angel investors. Not only are high-performance angels important for allocating early-stage capital, but in a world of syndicates, high-quality angels are critical for attracting capital from outside the region. The capital pool associated with investors who back a local lead investor is made even more valuable by the accompanying social networks that expand the reach of funded ventures through backers' relationships with potential customers, recruits, partners, and follow-on investors. In other words, from the perspective of the policymaker, the rise of syndicates increases the returns to attracting high-quality angels to the focal region. Accordingly, policymakers should look more closely at levers they control to attract and maintain the number of star angels in their jurisdiction.

This means that not all locations will benefit equally. Regions that have both quality ventures and angel investors with reputation and profile will benefit even more than before as they attract increased capital flows from other locations.

While most policy points in articles on crowdfunding are focused on existing or anticipated securities regulations administered by the United States Securities and Exchange Commission (SEC), the more relevant regulatory bodies in this case are those outside the United States. In March 2013, AngelList obtained a "No-Action Relief" from the SEC indicating that their "[staff] will not recommend enforcement action against AngelList." At present, it is less obvious whether investors from outside the U.S. can lead investment rounds for ventures inside the U.S. or within their own countries and attract backers from both inside and outside the U.S. using AngelList or similar platforms. Jurisdictions that anticipate this channel of capital flows becoming important will adapt their securities laws to ensure their venture and investor communities are connected to the global flows of capital in this asset class.

Summary

It is too early to state with certainty that syndicates are the "killer app" of equity crowdfunding. However, it is not too early to observe that syndicates have economic properties that lend themselves to significantly reducing the information asymmetry problem. In other words, the economics of information associated with early-stage investing are much better suited to crowdfunding lead investors than crowdfunding ventures. This is not only true in theory but also evident in the data on AngelList investment activity. Syndicates amplify the impact of high-performing angel investors by providing them with a more explicit reputation and online tools, both of which can be leveraged to attract capital from a global rather than local community of investors. Syndicates increase the volume and also influence the pattern of capital flows in this asset class. Overall, syndicates enhance economic growth by reducing market failures and allocating capital more efficiently.

Notes

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