

## Investing locally: Forging a better future for all

Even before COVID, investors and community leaders were thinking about how a shift of capital from Wall Street to Main Street could be instrumental in strengthening their local economies, creating jobs, and making quality of life improvements that are accessible to all members of their community. Add a global pandemic, an even starker understanding of structural inequities, and a planet that is continuing to react to the stressors placed upon it, and investors are becoming even more passionate about being “the change you wish to see in the world”, as Mahatma Gandhi has counseled.

Whether this was already on your radar or this is the first time you are thinking about it, including local investments in your portfolio has its merits and its risks. This handout was written by investment advisors who have helped their clients invest locally as restrictions have relaxed in recent years. Our goal is to help you have an informed discussion with your financial advisor as you consider how this may or may not fit within your investment and life goals. If you are part of the growing DIY investor community, then we hope you find this equally as helpful as the rest of the resources we included in this kit.

To be sure, learning how to be a prudent investor takes years of practice and experience, but it all starts with putting one foot in front of the other. This handout cannot include all the things you may want to know in the years ahead as you dive into what your local community has to offer, so think of it as one of those first steps to help you in your journey and commit to the process of lifelong learning. We hope with that framing you both learn and enjoy this and other resources on the Local Investing Resource Center website!

### What exactly is local investing?

Local investing may go by many names (some of which are used interchangeably here), including *community capital*, *community investing*, *impact investing*, *direct investing*, *investment crowdfunding*, or even *equity crowdfunding*. Of all these monikers, equity crowdfunding is a bit of a misnomer because local investments can be debt (also called *loans*), equity (also called *stock*), or something in-between that acts like both, like a royalty agreement (also called a *revenue-sharing agreement*).

Organizations raising capital can be for-profit, non-profit, or investment funds run by local or regional institutions. Although, the moniker direct investing refers to capital placed directly with the business that needs it, rather than being routed through a fund. While for-profit companies can raise either debt or equity, non-profit organizations can only raise debt, since they are not owned by anyone.

Ever since the 1930s, investing in privately-held companies or non-profit organizations was only accessible to high net worth investors (called *accredited investors*, which are about 6% of the population) or to people who personally knew the business, like a friend or family member. In

2012, the JOBS Act was passed, which created a way for companies to raise capital from the other 94% of the population, however it took several years for the rules to be crafted for the marketplace.

Fast forward to today and now over half of U.S. states have passed their own laws making it easier to invest and companies have the federal option through the JOBS Act (called *regulation crowdfunding*, or *Reg CF*, for short). Notably, while this handout was being drafted in August 2020, the SEC updated its accredited investor definition to now include a variety of professionals, including your financial advisor – a major victory after nearly 40 years of advocacy from industry associations.

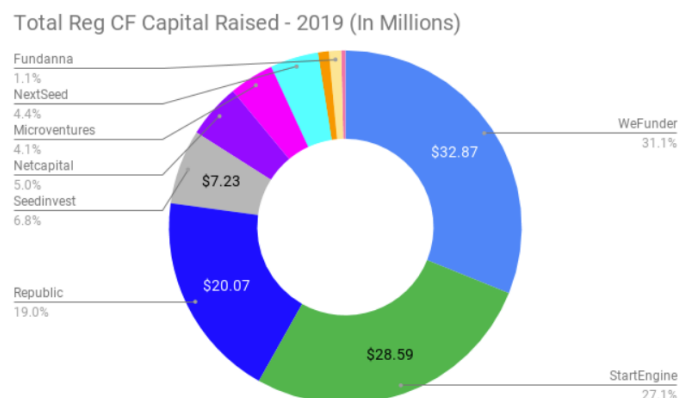
### How *big* is the local investment movement?

Surprisingly, that is a difficult question to answer. We have a few clues to go by, however, because of where local investments sit within the rest of the investment universe. First, local investments are considered part of the *private market* because the companies are not publicly traded. There is about \$100 trillion of wealth in the U.S., according to a [2018 report from the Brookings Institute](#), and \$4 trillion of that is held in investments in the private market, according to [McKinsey's 2020 market review](#). Since this figure includes private equity and large real estate funds, it is hard to know how much of that are community-based investments.

Second, local investments are considered part of the sustainable, responsible, impact investment (SRI) movement, which counts *community investments* from institutions and fund managers under its umbrella. Community investments are the fastest rising subset within the SRI movement, as reported in the [U.S. Sustainable Investment Forum's 2018 trends report](#). They show a total market size of \$689 billion.

Lastly, several industry advocates have kept a close eye on Reg CF activity and report this figure regularly. The total amount raised since the JOBS Act rules went into effect was \$339 million, according to [Crowdrise's 2019 annual stats](#).

Additionally, the [SEC reported in 2018](#) that in the prior year \$1.8 trillion had been raised using the Reg D registration type, which can also be used by companies to raise local capital.



While we may be able to find stats like this for other registration types, the one kind that does not seem to have been reported in any aggregated way is the amount of capital raised by the relatively newer *intrastate securities exemptions*. This is the state-by-state movement that has been spreading across the U.S. since 2013, paving the way for companies to raise capital within their state without having to deal with federal registration requirements. This may also be why

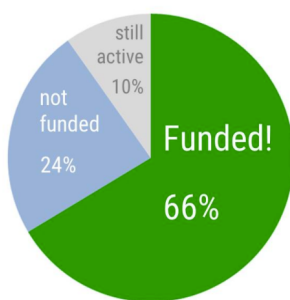
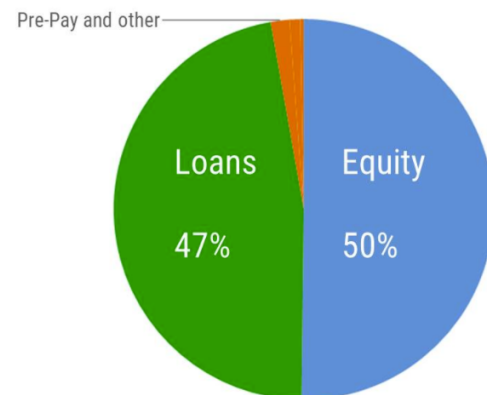
this conversation is gathering steam in your community, especially if the law has just recently changed. To see if your state has taken action yet, [look them up here](#).

None of these facts give us a comprehensive sense of how much capital is being invested by people like you into communities like yours, however they do tell us that activity is happening, companies are getting funded, and investors are rooting even deeper within their own backyard. We share these stats to let you know that while local investments may be a relatively new asset class for you and your advisor, it is arguably a large part of how capital circulates around you on a daily basis.

### What does a typical offering look like?

Given what you now know about the scattered data collection, imagine how much variety there can be in the offerings (also called *deals*) themselves! Every community is unique, every company and its culture are shaped by the specific stewards within, and every registration type drives a different set of standards and behaviors.

Fortunately, we have at least one representative data set to refer to for some trends on the types of offerings you might see in your own town – thanks to the folks behind [Investibule](#), which is the country's only website that aggregates offerings from across 30+ platforms so you can easily search for something that fits your interests. Investibule published a study in 2019 called [Community Capital 2000](#), which shared insights from the first 2,000 offerings that showed up in their search engine from around the U.S.



#### Successful Raises

\$134K (avg)

Range: \$5K – \$12M

131 Investors (avg)

Range: 1 – 3,515

The study revealed that offerings were split nearly evenly between debt and equity, dispelling the myth inferred in the term *equity crowdfunding*. We can also see that the average raise amount was \$134,000 and included 131 investors. As advisors who have looked at hundreds of offerings, we can confirm that most community-based businesses (who are raising funds for purposes outside of real estate acquisition or refinancing) tend to raise \$100,000-\$250,000.

Now, we know the next two questions on your mind, and trust us when we say they are on your advisor's mind too.

- *But what is the return on investment (ROI) on these deals?*
- *And how likely am I to lose my money?*

These are great questions and are arguably the most fundamental questions to ask as you consider your next move! The return on investment you achieve and your risk of losing your investment will ultimately depend on both the costs of adding this asset class to your portfolio and the offerings you choose, which will be largely informed by your risk tolerance.

- For instance, if you invest outside of a self-directed IRA or solo 401k, then you get to skip the various fees imposed by custodians, which affect your net ROI.
- If you have a low risk tolerance or you decide to be an incredibly patient, almost charitably minded investor, then you may only feel comfortable with 2% simple interest collateral-backed loans made to non-profits, for example.
- Or perhaps you have a very high tolerance for risk and want to give companies the most amount of time possible to convert your capital into long-term value, then you may choose to diversify across ten different growth-oriented companies by becoming an equity owner in each and hoping at least one or two of them do great (this is more of an angel investor mindset).

The overriding message here is that your return and risk of loss is determined **by you and your choices**. While you cannot control what the leaders of companies in your portfolio do with the opportunity in their hands, you *can* control how much capital you put at risk and where you put that capital.

To help you and your advisor build a profile of the types of opportunities that may be most appropriate for you and your portfolio, so you can more easily narrow down the universe of options available to you, we have included a worksheet in this resource kit called **Your Ideal Deal** that will guide you through some common decision-points that may shape your choices.

### **What if my advisor is not on board for this?**

First, if you have a great advisor that you trust and who knows you well, good for you! Many Americans are flying solo for their finance questions or are not that thrilled with their advisors. However great your advisor relationship may be though, they or their firm may not be enthusiastic or may be completely unable to help you with community investments.

If that is the case for you, then you may need to serve as your **own advisor** for this asset class in your portfolio, like what investors with rental properties often must do. If you have ever owned rental properties, then you know there are a host of people 'on your bench' that help make that asset class a success for you, people who go well beyond the expertise and service that your financial advisor can provide. They might include a property manager, mortgage broker, realtor, assessor, title company, inspectors, and specialist contractors. Similarly, investors wishing to invest locally may be wise to stack their bench with an attorney, tax advisor, two or three wise people they know, and a short list of subject matter expert friends they can call when they encounter an offering in an industry they are less familiar with.

Beyond serving as your own advisor for this asset class, there is another very important thing you can do – **educate your advisor**. It may seem odd to think that your advisor needs education or even that it is your job to educate them, but they only know what they know and at

this point you may find yourself outpacing them in experience and knowledge in this particular area. While they may not be able to help you directly because their firm prohibits it, they are not prohibited from hearing your updates and consuming the knowledge you advance to them.

### Okay, cool, I'm ready! Now what?

Awesome! Whether you are able to work with an advisor for this type of investment or you are serving as your own advisor, then we recommend the following next steps to keep you moving on your journey:

1. **Read and think** – consume the handouts in the Advisor Resource Kit and follow the links in the resources section below. Think deeply about the risks involved in investing locally.
2. **Identify Your Ideal Deal** – using the worksheet provided, scope out what you're most interested in finding, then update your Investment Policy Statement (IPS) to incorporate local investments into your asset allocation.
3. **Look for opportunities to invest** – search [Investibule](#), ask your friends, ask your favorite business owners in your town, add yourself to the mail list of two or three platforms that are targeting the type of opportunities you are looking for.
4. **Perform due diligence** – use the *due diligence checklist* and *financial checklist* in the resource kit, read investor packages front to back, ask 'your bench' for their opinion, work with a buddy even.
5. **Make decisions** – say yes or say no to each opportunity as it arises.
6. **Track it** – add the investment to your portfolio tracker (don't have one? Create a simple Excel worksheet) and look for annual reports to learn how the companies are doing as time goes on.

## Resources

- **Regulatory insights**
  - [SEC Investor Bulletin: 10 Red Flags That an Unregistered Offering May Be a Scam](#)
  - [SEC Investor Bulletin: Crowdfunding for Investors](#)
- **Books and education**
  - [Moving Mountains: The Power of Main Street Americans To Change Our Economy](#), Shade, 2020
  - [Put Your Money Where Your Life Is](#), Shuman, 2020
  - [The Resilient Investor](#), Brill, Kramer, Peck, 2015
  - [Local Dollars, Local Sense](#), Shuman, 2012
  - [The Ownership Revolution](#), Kelly, 2012
  - [Essential Knowledge For Transition Online Course](#): Towards Aware and No-Harm Investing
  - [Grubstake YouTube channel](#): investor education videos
- **Updates, news, and community connection**
  - [Locavesting website](#): tools, sector news, regulatory updates
  - [CrowdfundInsider website](#): tools, sector news, trends tracking
  - [National Coalition for Community Capital \(NC3\)](#): peer learning and advocacy
  - [The Next Egg](#): online community for those using self-directed IRAs to invest
  - [Angels of Main Street](#): online community for peer-to-peer investor connection
  - [DisclosureQuest](#): database of registered offering disclosure documents

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