A structuring aid for criteria-based decision-making about alternative financing models

Overview of alternative financing models

This tool helps you approach some key questions you need to consider when thinking about alternative ways to finance a project (as an addition or alternative to bank loans). They are generally community-based, that is to say, people who support your work and goals provide you with capital. Different types are distinguished as follows:

'(1) Pure financing instruments, e.g. crowdfunding, profit participation rights, direct loans.

(2) Financing models based on a particular legal form, e.g. cooperative, corporation.

(3) Financing in cooperation with an intermediary organization which pools citizens' capital, e.g. citizen shareholder corporation, land purchase cooperative.

(4) Others (mostly related to primary production), e.g. community-supported agriculture (CSA)[1], leasing and sponsorship.'[2]

In **crowdfunding,** a larger number of people provide capital. Typically, internet platforms organise the process. Different models can be distinguished: In reward-based and donation-based models, the capital providers do not expect to get their money back, while equity-based and lending-based crowdfunding, also called crowd-investing, are based on the principle that individuals provide capital that can be paid out again.

Profit participation rights entail investors acquiring a right to a share in profits (or losses). They get a return on the invested capital such as monetary interest or interest in kind (in the form of goods or coupons), but have no say in company decisions.

Capital can also be provided in the form of **direct loans** from private individuals. A high degree of trust is required as the capital provided could be lost in a bankruptcy. In most jurisdictions, private loans are in principle considered a banking transaction subject to authorisation, but exemptions for e.g. small amounts may exist; legal regulations and exemptions must be carefully researched.

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[1] CSA is not being introduced in more detail, as this Roadmap Tool focuses on models that are applicable independent of sector. For further information, please consult other sources.

[2] Behrendt, Gerlinde; Peter, Sarah; Sterly, Simone R.; Häring, Anna Maria (2019): Community financing in the German organic food sector: a key for sustainable food systems? No. 2019/18. Université de Liège (CIRIEC Working Paper).

Specific choices of legal form for a business, such as a **private company or corporation**, can involve citizens as partners. They contribute equity capital and thus receive a share in profits. A limited partnership is a form of private company that consists of fully liable general partners (the entrepreneurs) and limited partners liable with only their share. In a corporation, citizens can be shareholders. Private companies and corporations generally entail strict legal requirements and high set-up cost.

In a **cooperative**, members participate by acquiring shares. A democratic decision-making structure is a fundamental part of cooperatives, as members have equal voting rights. **Land purchase cooperatives** typically help the agricultural sector gain access to land. **Citizen shareholder corporations** bundle capital and then invest in various companies. They can be directed at specific sectors and aim to strengthen the cooperation between their partner enterprises, in material and ideal terms.[3]

In a **leasing**-based model, a good such as a farm animal is purchased and/or kept with the help of supporters. Expenses and profits are distributed between owner and user, often the supporter gets a specified share of a product made with the purchase, such as in the case of a farm animal, cheese or meat, or a discount for purchases of such products. A **sponsorship** model also entails contributions toward regularly occurring costs, and a material reward for the supporter may or may not be part of the agreement.

The information provided here has been compiled to the best of our knowledge, but is not guaranteed and is intended only as an initial guide for users. The information does not replace legal advice. As a user, you are responsible for all decisions you make based on the information provided. Please bear in mind that consulting a lawyer or tax advisor it is highly recommended.

[3] Information based on the BioFinanz website (www.biofinanz.info) and Sterly, Simone; Peter, Sarah; Behrendt, Gerlinde; Häring, Anna-Maria (2020): HOW ORGANIC FOOD NETWORKS IN GERMANY BENEFIT FROM COLLECTIVE ALTERNATIVE FINANCING. Contribution for IFSA Conference 2020, unpublished.

Criteria to consider in decision-making about using alternative financing models

Criterion	Possible manifestations
Stage of enterprise development The stage of enterprise development relates to the need for capital, production capacity, ability to give rewards to capital providers or to pay interest, risks, and client base relations. Decisions about the legal form (e.g. cooperative) may only be made at the founding stage. Fundamental changes to the business model may be necessary or only possible at certain stages.	Existing entity Founding
Funds needed Some financing models are better suited for smaller, some for larger sums needed. The sum required for your project should be considered, for instance in relation to: • Fees (crowdfunding), set-up costs (models based on legal form) and running costs for PR etc.; legal restrictions (direct loans) • Potential number of supporters that can be mobilised • Considerations of combining financing models • Necessity of getting a partner organisation on board (citizen	<10,000 EUR 10,000-100,000 EUR >100,000 EUR[4] N/A

[4] The sums named here are some typical border amounts (e.g. maximum allowed sum per year). Please seek for information on the specific legal regulations in your country.

Criterion	Possible manifestations
shareholder corporations, crowdfunding platforms…)	
Object or purpose to be financed The object or purpose to be financed impacts what reward can be given to the supporters, how progress can be communicated, and more fundamentally, the availability of certain forms of financing.	Running expenses Land Real estate, machines, equipment Plants Animals Other costs of market entry, setup etc.
Client base, (local) network For all financing models that do not involve an intermediary organisation (e.g. a land purchase cooperative), relations to a network of customers or other (potential) supporters are essential. What kind of financing model might your client base support, and how much might they be willing to invest, how many people can you mobilise? If no network is in place yet, community financing can be a great way to develop it, but it is also more difficult than if you can fall back on an existing network. These considerations do not replace general market research for your product or service!	In place Partly in place To be developed
(Resources for) Reward to supporters In many forms of community financing, supporters expect a reward or even purchase a product or service as part of the transaction. What do you have to offer? Is	Coupons & produce Monetary – share of profits or interest None Other

Criterion	Possible manifestations
it aligned with the goals and values of your client base?	
Reasons to seek alternative financing Depending on your reasons to seek alternative financing, different models may be preferred as they offer different balances of PR effects (and related efforts), accessibility of a model for start-ups etc. Another consideration is that if you need equity to get a bank loan, only some forms of alternative financing offer that. Please consider that alternative financing models are not the solution to cover running costs or debt in an unstable economic situation!	Customer retention Access to financing (alternative to banks) Setting up business
Resources (for administration, PR, legal matters etc.) Community financing typically involves a lot of work for staying in touch with supporters, often even producing videos, sending out rewards etc. Also, you should be comfortable with a high degree of transparency of your enterprise. If you anticipate this to be difficult, financing models that are based on legal form and those with an intermediary organisation may be better suited. Training, legal advice, fees etc. will need to be budgeted.	High Low

Criterion	Possible manifestations
Duration Consider for how long capital is needed and whether it will be a one-time investment or should cover a recurring expense. Although most community financing models collect capital at a single point in time, some models may permit collecting more capital as time passes. Others, such as leasing, are well suited to ensure certain regular running costs are covered. Only cover running costs this way if you have good reasons and are transparent about it, supporters do not usually want to help cover a general economic deficit!	On a regular basis (short- or long-term?) Long-term investment or lending One-time donation/purchase
Risks The risk of failure or increasing cost of a project should be considered. If banks consider your proposal too risky to finance, you should weigh carefully whether you want to pass that risk on to supporters. Consider the reputation loss a failure might incur. Nevertheless, if you are transparent about risks, people might be willing to support a risky but worthwhile endeavour.	High Low

Criterion	Possible manifestations
Goals and values Is your project aligned with values your supporters subscribe to? Do they consider it worthy of their support? Which financing model might fit with your long-term goals as well as those of your supporters? For instance, do they want to become shareholders, do you want to give up a degree of autonomy? Or is their main interest in a certain product or service and they don’t want to be involved after they get it from you?	