Real Estate Crowdfunding

By ANNA CHANG-YEN | Green Shoot Media

You — yes you — can become a real estate investor.

Crowdfunding is a way for the average Joe to make small investments in projects ranging from video games, technology and movies to board games and household gadgets. Websites such as Indiegogo, Kickstarter and GoFundMe have led the way.

Real estate now joins that list, thanks to a relatively recent law that loosened regulations on private investments.

THE JOBS ACT

The Jumpstart Our Business Startups Act, or JOBS Act of 2012, rolled back Depression-era restrictions on soliciting for private equity investments. Before the JOBS Act, the Securities Act of 1933 made it illegal to publicly market private security investments, creating what Forbes calls "the old country club model of finding and investing in real estate." In other words, you had to know somebody who knew somebody, and even then, you'd need a six-figure sum to invest.

But the JOBS Act changed all that, opening real estate deals to the crowdfunding model.

The Cambridge Judge Business School reports that investors poured $484 million into real estate projects via crowdfunding in 2015.

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Illinois law lets investors contribute as little as $1 to these types of deals. Technically a first-grader could invest his allowance in a posh luxury skyscraper.

Crain's reports that a north suburban Chicago homebuilder raised more than $1 million from 80 investors in just 18 days, with some investors chipping in just $10,000.

WHO SHOULD GET INVOLVED?

Builders, flippers, lenders and investors of all types are getting in on the real estate crowdfunding action. Often the loans are structured as short-term, high-interest loans, say for a period of six months. Though crowdfunding contributors have traditionally taken home mementos such as T-shirts, as well as early access to products, real estate crowdfunding investors will have to wait until the time specified in the deal to ideally reap their rewards in the form of cash.

Since the entire idea of crowdfunding is to combine many small investments to back a project, there's no bottom limit on who can invest in real estate these days. Illinois law, for example, lets investors contribute as little as $1 to these types of deals. Technically a first-grader could invest his allowance in a posh luxury skyscraper.

THE RISKS

As with almost any investment, there is risk. Jordan Fishfeld, founder of PeerRealty, told Crain's that the Internet has a solution for that, too, saying the public nature of the Internet will subject fundraisers to "much more accountability than if I come into your house and make some promises while I'm talking to you."

BiggerPockets.com warns potential investors to do their homework on investors. That includes questioning why the project ended up in the crowdfunding arena. Was the project denied a traditional loan? If so, why? Investors should take note of any failed projects and ask what changes will be made, BiggerPockets.com warns.

Bloomberg sounds an even more cautious note. In a story featuring the subhead, "There are more than 125 places for investors to lose their shirts in real estate crowdfunding," the website profiles a Florida investor who found that only one in five of the real estate crowdfunding sites he evaluated "passed the sniff test." The investor, Ian Ippolito, warned in the 2016 article that the relatively new industry needed another year or two to weed out sketchy players.

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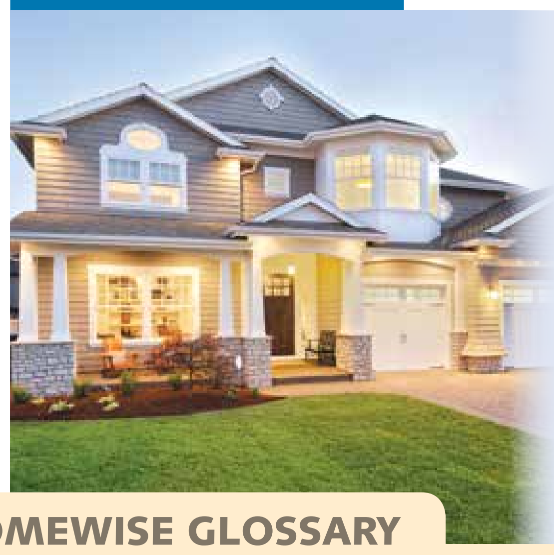
REAL ESTATE 101



Getting Started

- **Fundrise.com** was one early player in the real estate crowdfunding field, even advocating for loosened regulations before the U.S. Securities and Exchange Commission. Today the site claims to have more than 80,000 members with nearly $3 billion worth of real estate investments, including the new World Trade Center.
- **Groundfloor.com** navigates state investing rules to draw in novice investors with as little as $100 to lend.

HOMEWISE GLOSSARY

Real Estate Settlement Procedures Act (RESPA): A federal law that requires lenders to provide home mortgage borrowers with information about transaction-related costs prior to settlement, as well as information during the life of the loan regarding servicing and escrow accounts. Prohibits kickbacks and unearned fees in the mortgage business.

SOURCE: California Bureau of Real Estate