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TEENAGE CROWDFUNDING

*Andrew A. Schwartz**

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I. INTRODUCTION

Entrepreneurship is widely viewed as socially beneficial because it lifts employment, grows the economy, and for many other reasons. Teenage entrepreneurship—that is, where teenagers organize and manage startup companies of their own—can be particularly valuable because teenagers have a special knack for creating revolutionary, new types of businesses. Consider that Bill Gates founded Microsoft, and Mark Zuckerberg founded Facebook, both as teenagers. This phenomenon of the teenage entrepreneur originated in the 1970s in the wake of Vietnam-era reforms that lowered the age of contractual capacity from twenty-one to eighteen.¹ This change in law, however, was partially rolled back by the federal Credit CARD Act of 2009, which raised the age of adulthood to twenty-one solely for purposes of credit card contracts.² Because most entrepreneurs use their personal credit cards for seed-stage financing, this portion of the CARD Act had the unfortunate effect of making it harder for American teenagers to

* Associate Professor of Law, University of Colorado Law School. For comments on prior drafts, I thank Joan Heminway, Allison Schwartz, Commissioner Andrea Seidt, and participants at the University of Cincinnati College of Law Corporate Law Center Symposium, “Crowdfunding Regulations and Their Implications,” where this paper was originally delivered. For research assistance, I thank Nathan Goergen, and for editorial assistance, I thank Diana Avelis and Lisa Willcox. This Essay is dedicated to my grandmother-in-law, Irene Parenteau, whose youthful outlook belies her ninety-five years.

1. Andrew A. Schwartz, *Old Enough to Fight, Old Enough to Swipe: A Critique of the Infancy Rule in the Federal Credit CARD Act*, 2011 UTAH L. REV. 407, 409–20 (2011) (recounting the history of legal adulthood, showing that it was originally set at twenty-one years in the Middle Ages, but was subsequently lowered to eighteen in the late twentieth century by constitutional amendment, federal and state statutes, and judicial decisions).

2. Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009, Pub. L. No. 111-24, § 301, 123 Stat. 1734, 1748.

launch new business ventures.³

But sometimes when Congress closes a door, it opens a window,⁴ and a few years later it did just that: in Title III of the JOBS Act of 2012, known as the CROWDFUND Act, Congress created a new method of financing startup companies, including those founded by teenage entrepreneurs. The CROWDFUND Act authorizes the “crowdfunding” of securities, meaning the sale of securities over the Internet to large numbers of investors (the crowd), each of whom invests a small amount.⁵ Unlike the CARD Act, there is nothing in the CROWDFUND Act to restrict crowdfunding to those over twenty-one, meaning that teenagers will be able to use crowdfunding once this market goes live.⁶

Importantly, crowdfunding will take place entirely over the Internet. Teenagers, being experts at Facebook, Snapchat, Twitter, Instagram and such, are very well positioned to take advantage of the online securities exemption that the CROWDFUND Act creates. Time will tell, but securities crowdfunding may well develop into an important funding source for financing teenage startup companies, to the benefit of us all.

II. TEENAGE ENTREPRENEURSHIP⁷

This Part identifies in Subpart A the relatively recent phenomenon of teenage entrepreneurship and explains why it is in the public interest.⁸ It then discusses in Subpart B why it is particularly difficult for teenagers to obtain the seed-stage financing needed to launch a startup company.⁹

A. *The Social Value of Teenage Entrepreneurship*

There is widespread agreement that entrepreneurship is vital to economic growth and employment in the contemporary United States. Startup firms in their first year have been responsible for all net job

3. See Schwartz, *supra* note 1.

4. Cf. THE SOUND OF MUSIC (20th Century Fox 1965) (“When the Lord closes a door somewhere he opens a window.”).

5. Andrew A. Schwartz, *Rural Crowdfunding*, 13 U.C. DAVIS BUS. L. J. 283, 284 (2013); see generally Andrew A. Schwartz, *Crowdfunding Securities*, 88 NOTRE DAME L. REV. 1457, 1459–66 (2013).

6. Securities crowdfunding will launch once the SEC issues final regulations. President Obama signed the JOBS Act into law in April 2012 and the SEC issued proposed regulations in October 2013. The final regulations are expected in October 2015. Mark D. Wood et al., *SEC Sets October 2015 Target Date for Certain Dodd-Frank and JOBS Act Rulemaking*, THE NATIONAL LAW REVIEW (Dec. 5, 2014), <http://www.natlawreview.com/article/sec-sets-october-2015-target-date-certain-dodd-frank-and-jobs-act-rulemaking>.

7. This Part is adapted from Schwartz, *supra* note 1.

8. See *infra* Part II.A.

9. See *infra* Part II.B.

creation in the United States since at least the 1970s, having added about three million jobs per year, even during recessions.¹⁰ Startups are similarly important for general economic growth.¹¹ And while many of these startups eventually fold,¹² those that survive are often the type of companies that create satisfying employment opportunities and whose products or services improve our quality of life.¹³

Our leaders and policy makers have long understood the importance of entrepreneurship to a thriving economy and society. President Clinton has extolled the “key role” of new and small firms “in the experimentation and innovation that leads to technological change and economic growth,” and opined that “their experimental efforts are an essential part of the organic and ever-changing American economy.”¹⁴ President Obama has concurred, adding that “entrepreneurialism is the key to our continued global leadership and the success of our people.”¹⁵ Congress, for its part, has twice declared that “it is the continuing policy and responsibility of the Federal Government to . . . provide an opportunity for entrepreneurship . . . and the creation and growth of small businesses.”¹⁶ And this has not been empty rhetoric, but rather has been directly implemented: A portion of all federal contract dollars are statutorily required to go to small businesses, and the Small Business Administration guarantees loans for small businesses and provides free counseling and training to entrepreneurs.¹⁷ Similarly, state and local

10. TIM KANE, KAUFFMAN FOUND., *THE IMPORTANCE OF STARTUPS IN JOB CREATION AND JOB DESTRUCTION* 5 (2010) (noting that all “net job growth in the United States comes from firms less than one year old, formally defined as startups”); *id.* at 2 (“[W]ithout startups, there would be no net job growth in the U.S. economy.”); John C. Haltiwanger et al., *Who Creates Jobs? Small vs. Large vs. Young* 2 (Nat’l Bureau of Econ. Research, Working Paper No. 16300, 2010) (“Business startups contribute substantially to both gross and net job creation.”).

11. *See, e.g.*, 15 U.S.C. § 631a(a) (2006) (“For the purpose of preserving and promoting a competitive free enterprise economic system, Congress hereby declares that it is the continuing policy and responsibility of the Federal Government to . . . provide an opportunity for entrepreneurship, inventiveness, and the creation and growth of small businesses.”).

12. Steve Lohr, *To Create Jobs, Nurture Start-Ups*, N.Y. TIMES, Sept. 12, 2010, at BU3 (“Within five years, half of [startup] businesses have folded.”).

13. *Id.* (“[T]he survivors are prime candidates to join the young, dynamic companies that make an outsize contribution to innovation, productivity gains and job growth.”).

14. Rutheford B Campbell, Jr., *Regulation A: Small Businesses’ Search for “A Moderate Capital”*, 31 DEL. J. CORP. L. 77, 86 (2006) (quoting U.S. SMALL BUSINESS ADMINISTRATION, *THE STATE OF SMALL BUSINESS: A REPORT OF THE PRESIDENT* (1998)).

15. Barack Obama, *Toward a 21st-Century Regulatory System*, WALL ST. J., Jan. 18, 2011, at A17; *accord* President Barack Obama, *State of the Union Address* (Jan. 27, 2010), *as reprinted in* 156 CONG. REC. H416-20 (daily ed. Jan. 27, 2010) (stating that “most new jobs” come from “companies that begin when an entrepreneur takes a chance on a dream, or a worker decides it’s time she became her own boss”).

16. 15 U.S.C. § 631a(a); *accord id.* § 631(a).

17. *See What We Do*, SBA.GOV, http://www.sba.gov/about-sba/what_we_do (last visited Nov. 17, 2014).

governments expend resources attracting entrepreneurs to their communities.¹⁸ In short, entrepreneurship is in the public interest and startup companies are actively encouraged as a matter of public policy.

All of this is doubly true for teenage entrepreneurs, for in addition to all the ordinary benefits of entrepreneurship just discussed, they possess the creativity and energy of youth.¹⁹ Teenagers are widely known to challenge orthodox thinking and may be able to offer fresh, new solutions to vexing problems.

Moreover, teenagers are better positioned to take a chance in the risky world of entrepreneurship than older people: they are generally not married or parents, so they have fewer responsibilities; they have no mortgage hanging over their head or even any debt at all. They also have not spent years perfecting a skill or trade. Having not yet spent years learning and practicing accounting, law, carpentry or any other skilled work, they have no sunk costs and relatively little to lose—apart from time—in trying to launch a startup.

Until late in the twentieth century, however, the so-called “infancy rule” of contract law prevented anyone under the age of twenty-one from starting a business. From as far back as the thirteenth century,²⁰ the common-law courts of England embraced a bright-line rule setting legal adulthood at twenty-one years.²¹ Twenty-one was initially selected because medieval Englishmen were eligible for knighthood only upon achieving twenty-one years of age.²² For purposes of contract law, this meant that a person lacked legal capacity to enter into a contract until age twenty-one, making it impossible for a teenager to found her own

18. See, e.g., Patrick McGeehan, *Hoping to Lure Tech Jobs, City Seeks a Partner to Open Graduate School of Engineering*, N.Y. TIMES, Dec. 17, 2010, at A34. The phenomenon is not limited to the United States. See, e.g., Clyde H. Farnsworth, *Russians Are Coming, but for Money*, N.Y. TIMES, Oct. 2, 1993, at A4 (reporting on “Canada’s strong desire to attract entrepreneurs”).

19. E.g., Daisuke Wakabayashi, *Tech Talent Hunt Tries New Venue: Middle School*, WALL ST. J., Aug. 30, 2014, at A1 (“If you start young, you will have an advantage over people who start in their 20s. Your brain has more plasticity when you’re younger.”) (quoting fourteen-year-old Grant Goodman, who designed and published three mobile apps before entering high school).

20. 5 RICHARD A. LORD, WILLISTON ON CONTRACTS § 9:2 (4th ed. 2010) (citing an English case from 1292).

21. *Id.* § 9:3 (“No distinction has generally been drawn so far as concerns contractual capacity between a minor of tender years and one who, having nearly attained his majority, has ample intelligence in fact.”).

22. WENDELL W. CULTICE, YOUTH’S BATTLE FOR THE BALLOT: A HISTORY OF VOTING AGE IN AMERICA 2 (1992); *Jolicoeur v. Mihaly*, 488 P.2d 1, 5 (Cal. 1971). This rule, in turn, was apparently a consequence of the heavy weight of the suits of armor worn by English knights. *Jolicoeur*, 488 P.2d at 5; S. REP. NO. 92-26 (1971) (report on “Lowering the Voting Age to 18”). Once translated into the common law, however, the rule was applied equally to both genders. CULTICE, *supra* at 2.

business.²³

Even the greatest entrepreneurs in American history either had to wait until reaching twenty-one to found their ventures or partner with their parents. In 1810, for example, when Cornelius Vanderbilt sought to start a ferry business at the tender age of sixteen, he was not able to do so on his own, but rather was forced to partner with his father.²⁴ The same can be said of John D. Rockefeller who at age nineteen partnered with his father to found a commission merchant business.²⁵ It was only a few years later, when he was twenty-three, that Rockefeller finally went into the oil refining business on his own.²⁶

The infancy rule remained remarkably stable from the Middle Ages until well into the twentieth century. But during the Vietnam era of the 1960s and 1970s, American society came to the conclusion that if eighteen-year-olds can be drafted to fight and possibly die for their country, they should be treated as adults under the law.²⁷ Americans were persuaded by the rallying cry, “Old enough to fight, old enough to vote,”²⁸ and the United States Constitution was amended in 1971 to extend the vote to all those eighteen or older.

At around the same time, and for analogous reasons, every state lowered the age of contractual capacity to eighteen. By the late 1970s, this lower age of contractual capacity had become so universally accepted that the 1979 Second Restatement of Contracts added a new section, not present in the 1932 original, stating as black-letter law that eighteen-year-olds possess capacity to contract.²⁹

This seemingly arcane change in contract law in the 1970s gave rise to a new social phenomenon—that of the teenage entrepreneur. Once eighteen- to twenty-year-olds were empowered with the capacity to enter into legally binding contracts, some of them decided to launch

23. *Gastonia Pers. Corp. v. Rogers*, 172 S.E.2d 19, 20 (N.C. 1970) (“Under the common law, persons . . . are classified and referred to as *infants* until they attain the age of twenty-one years.”) (emphasis in original).

24. EDWARD J. RENEHAN, JR., *COMMODORE: THE LIFE OF CORNELIUS VANDERBILT* 25–26 (2007); see also T.J. STILES, *THE FIRST TYCOON: THE EPIC LIFE OF CORNELIUS VANDERBILT* 23–24 (2009).

25. PETER COLLIER & DAVID HOROWITZ, *THE ROCKEFELLERS: AN AMERICAN DYNASTY* 12–13 (1976).

26. *Id.* at 16–22.

27. *Lowering the Voting Age to 18: Hearings Before the Subcomm. on Constitutional Amendments of the Comm. on the Judiciary*, 90th Cong. 20–21 (1968) (statement of Rep. Spencer Oliver) (arguing that it was “surely unjust . . . to command men to sacrifice their lives for a decision which they had no part in making.”); *accord Oregon v. Mitchell*, 400 U.S. 112, 141–42 (1970) (Douglas, J., dissenting).

28. CULTICE, *supra* note 22, at 234.

29. RESTATEMENT (SECOND) OF CONTRACTS § 14 (“Unless a statute provides otherwise, a natural person has the capacity to incur only voidable contractual duties until the beginning of the day before the person’s eighteenth birthday.”); *id.* Reporter’s Note (“This section is new.”).

business ventures of their own, something they never before-in-history had the chance to do. Many of these youths surely failed. But some teenage startup companies have succeeded in a spectacular fashion, employing tens of thousands, and creating products and services that have changed the world.

One of the first teenage entrepreneurs to emerge was Bill Gates, who co-founded Microsoft in 1975 at age nineteen,³⁰ just four years after the relevant state passed legislation lowering the age of contractual capacity to eighteen.³¹ Microsoft, whose software has noticeably increased the productivity of the American worker, is presently worth more than \$400 billion³² and employs approximately 128,000 people.³³ More recently, Mark Zuckerberg co-founded Facebook at age nineteen.³⁴ The online social network created by Facebook, which currently counts more than one billion users worldwide, has changed the way people interact.³⁵

Gates and Zuckerberg are clearly exceptional, but the phenomenon of the youthful entrepreneur is broader than one or two instances.³⁶ A recent survey found that 38% of eighteen- to twenty-one-year olds want to start a business of their own.³⁷ Despite the risks, many youths these days see entrepreneurship as “a viable career path, not a renegade choice.”³⁸ Billionaire philanthropist Peter Thiel has created a fellowship for teenage entrepreneurs that pays them \$100,000 to start a business

30. STEPHEN MANES & PAUL ANDREWS, GATES 82–83 (1993).

31. N.M. STAT. ANN. § 28-6-1(A) (1978); see *Mason v. Mason*, 507 P.2d 781, 783 (N.M. 1973) (observing that the legislature lowered the age of capacity to eighteen in 1971).

32. *Microsoft Corporation*, GOOGLE FIN., <https://www.google.com/finance?q=NASDAQ:MSFT> (last visited Nov. 18, 2014) (reporting a market capitalization of \$407 billion).

33. *Facts About Microsoft*, MICROSOFT NEWS CENTER, <http://news.microsoft.com/facts-about-microsoft/#RevenueHeadcount> (reporting 128,076 employees as of June 2014) (last visited Nov. 18, 2014).

34. See BEN MEZRICH, *THE ACCIDENTAL BILLIONAIRES: THE FOUNDING OF FACEBOOK, A TALE OF SEX, MONEY, GENIUS, AND BETRAYAL* 79–83 (2009).

35. Alvan Balent, Note, *An Energy-Efficient Internet: The Next Revolution*, 37 FLA. ST. U. L. REV. 981, 981 (2010) (observing that Facebook is “changing basic modes of social interactions”); *THE SOCIAL NETWORK* (Columbia Pictures 2010) (film based on the meteoric rise of Facebook); see, e.g., Schwartz, *supra* note 1, at 422 & n.108 (noting that the 2011 Egyptian revolution was launched via Facebook); Jose Antonio Vargas, *Spring Awakening: How an Egyptian Revolution Began on Facebook*, N.Y. TIMES, Feb. 19, 2012, at BR12 (2012) (same).

36. See also, e.g., Brian Stetler, *He Has Millions and a New Job at Yahoo. And Soon He'll Be 18.*, N.Y. TIMES, Mar. 26, 2013, at A1 (reporting that seventeen-year-old Nick D'Aloisio sold his news-summarizing app Summy to Yahoo Inc. for \$30 million); Adrienne Burke, *How a 15-year-old entrepreneur got her product into Nordstrom*, YAHOO! NEWS, <http://news.yahoo.com/blogs/profit-minded/15-year-old-entrepreneur-got-her-product-nordstrom.html> (describing fifteen-year-old entrepreneur whose products are sold at Nordstrom).

37. KAUFFMAN FOUND., YOUTH PULSE 2010, at 15 (2010).

38. Hannah Seligson, *No Jobs? Young Graduates Make Their Own*, N.Y. TIMES, Dec. 12, 2010, at BU1.

rather than matriculate in college.³⁹ One popular business for teenagers is to develop and sell “apps” for mobile devices.⁴⁰ Indeed, Google and Apple both host developer conferences that include teenagers as young as thirteen.⁴¹

In short, the statutory revolution that lowered the age of contractual capacity to eighteen has had a beneficial effect both for the newly empowered youths and for society as a whole. Perhaps an older person could have founded Microsoft or Facebook, but their founders demonstrated an ability to overcome convention that is more commonly found in the young. By unleashing the energy and creativity of eighteen- to twenty-year-olds into the commercial realm, the statutory reforms of the 1970s have allowed youthful entrepreneurs to build amazing companies that have advanced the economy and changed the world.

B. The Challenge of Financing Teenage Ventures

Aspiring teenage entrepreneurs may have dreams of being the next Gates or Zuckerberg, but they cannot get there without financing. Starting any business costs money, and access to capital is critical to a startup’s success. Unfortunately, as this Subpart will show, teenage entrepreneurs cannot access most sources of early stage business capital.

The traditional first source for entrepreneurial financing is from the entrepreneur’s friends and family, as well as their own personal savings.⁴² Most teenagers, however, have negligible personal savings, and the same can be said of their friends, so it comes down to whether the entrepreneur has a wealthy relative. Even then, it is questionable whether a relative would be willing to invest in a business founded by an inexperienced teen.⁴³

Moving beyond friends and family, a bank is another potential source of startup capital, at least in theory. In fact, however, banks are generally hesitant to extend credit to startup companies in their earliest stages, as the risk is simply too high.⁴⁴ Another option is to obtain

39. See *About the Fellowship*, THIEL FELLOWSHIP, <http://www.thielfellowship.org/about/about-the-fellowship>.

40. Aimee Heckel, *Boulder High students create best-selling iPhone app*, DAILY CAMERA, Apr. 7, 2013, at B1; Jessica E. Vascellaro, *App Developers Who Are Too Young to Drive*, WALL ST. J., June 18, 2012.

41. Wakabayashi, *supra* note 19, at A1.

42. PERI PAKROO, THE WOMEN’S SMALL BUSINESS START-UP KIT 104 (2010).

43. *But cf.* Burke, *supra* note 36 (teenage startup was “launched with ‘friends and family’ financing”).

44. RHONDA ABRAMS, THE OWNER’S MANUAL FOR SMALL BUSINESS 215–16 (2005) (“[B]anks generally aren’t an appropriate place for start-up capital”); Pakroo, *supra* note 42, at 98–99

capital from professional early-stage investors, such as angel investors or venture capital funds. But there is tremendous competition for such investments and such investors are interested in certain types of companies, often in certain geographic areas. Finally, an entrepreneur could attempt to obtain capital from the public through an initial public offering (IPO), but an IPO implicates the Securities Act's registration provisions and the Securities Exchange Act's reporting obligations, which would clearly be too burdensome and costly for a teenage startup.

If capital is not available from the above sources, where can an entrepreneur obtain a relatively small amount of cash to start a new company? One answer is a personal credit card, which provides an immediate line of credit and the freedom to spend the money as the holder sees fit.⁴⁵ Even the most speculative ventures can be financed on plastic—simply because the lender places no limit on the purpose for which the credit can be used. It should therefore come as no surprise that most American entrepreneurs use credit cards to finance their startup companies, particularly in their earliest days.⁴⁶ This has leveled the playing field for aspiring entrepreneurs, allowing those who hail from modest backgrounds to compete with those whose parents can provide startup funds.⁴⁷ And some of these credit-card backed startups grow into mighty oaks. Well-known examples include Cisco Systems, CA Technologies, the Oscar-winning film “Dallas Buyers Club,” and Spike Lee’s film production studio, 40 Acres and a Mule, all of which were started by credit card financing.⁴⁸

(“[B]anks are notoriously reluctant to lend start-up funds to first-time entrepreneurs . . .”); Ruth Simon and Angus Loten, *Small-Business Lending Stuck in the Slow Lane*, WALL ST. J., Aug. 18, 2014, at A1 (“The number of loans for \$1 million or less held by banks is down about 14% to 23.5 million since 2008.”); Kristina Shevory, *With Squeeze on Credit, Microlending Blossoms*, N.Y. TIMES, July 28, 2010, at B7 (“Most banks, large or small, do not bother granting business loans of less than \$50,000 because there’s not enough profit to balance the risk.”).

45. ROBERT D. MANNING, CREDIT CARD NATION 229-30 (2000) (“[U]nlike bank loan officers, private angel investors, or SBA bureaucrats, credit cards do not require extensive documentation or entail second guessing of business decisions.”); see also ERIC TYSON & JIM SCHELL, SMALL BUSINESS FOR DUMMIES 85 (2d ed. 2003) (“No personal guarantees here, no bankers looking over your shoulder, just sign your name and get on with the business at hand.”).

46. ABRAMS, *supra* note 44, at 214 (“most entrepreneurs use credit cards for many start-up expenses”); MANNING, *supra* note 45, at 228 (“credit cards have become the number one source of financing for small businesses—supplanting bank loans in the late 1990s.”); *id.* at 229 (“[M]ost business start-ups owe their early survival to plastic money.”); *id.* at 241 (“For most aspiring entrepreneurs, . . . credit cards [are] their most reliable source of start-up capital.”); ROBERT H. SCOTT III, THE KAUFMAN FIRM SURVEY: THE USE OF CREDIT CARD DEBT BY NEW FIRMS 1 (2009).

47. MANNING, *supra* note 45, at 231; see *id.* at 238–56 (collecting stories of startup companies financed with credit cards).

48. DAVID BUNNELL, MAKING THE CISCO CONNECTION: THE STORY BEHIND THE REAL INTERNET SUPERPOWER 24 (2000) (Cisco); MANNING, *supra* note 45, at 228 (CA Technologies); Alexandra Cheney, *AIDS-Crusader Biopic to Debut After Years of Changing Hands*, WALL ST. J., Oct. 28, 2013 (Dallas Buyer’s Club); MANNING, *supra* note 45, at 227 (40 Acres and a Mule); see also, e.g.,

Recent federal legislation, however, excludes teenagers from this important avenue of early stage financing. Recall that in the 1970s, American society came to a consensus that the age of legal adulthood for purposes of contractual capacity, among other things, should be eighteen.⁴⁹ Nevertheless, Congress enacted the federal Credit CARD Act of 2009,⁵⁰ one section of which reinstates—for credit card contracts—the ancient common-law rule that those under twenty-one are infants lacking capacity to contract.⁵¹ Indeed, the CARD Act's prohibition is even harsher than the common-law rule, at least in one sense: under the common law, a contract with an infant is merely voidable by the infant;⁵² the CARD Act renders a credit card contract with an infant void, even if she would have preferred to abide by it.⁵³

The net effect is that teenage entrepreneurs are legally prohibited from financing their startups using credit cards, which, as stated above, is among the most common sources of seed-stage capital. By categorically withholding credit cards from teenagers, the CARD Act seriously impedes their ability to start up a business, in direct contradiction of the strong public policy favoring entrepreneurship.

III. TEENAGE CROWDFUNDING

Part II just showed that the CARD Act cordoned off an important source of early-stage financing from teenage entrepreneurs, namely credit cards. However, as this Part will show, sometimes what the federal government takes with one hand, it gives right back with the other. Just a few years after the CARD Act, Congress authorized the “crowdfunding” of securities in the JOBS Act of 2012. This new

SCOTT, *supra* note 46, at 2 (“*The Blair Witch Project*, a film that grossed more than \$250 million, was funded almost exclusively with credit card debt”); Miguel Helft, *For Start-Ups, Web Success on the Cheap*, N.Y. TIMES, Nov. 9, 2006, at C1 (reporting that Meebo, a successful web-based start-up company, was initially financed with the founders’ credit cards); *see generally* MANNING, *supra* note 45, at 238-56 (collecting stories of start-up companies financed with credit cards).

49. *See supra* Part II.A.

50. *See* Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009, Pub. L. No. 111-24, § 301, 123 Stat. 1734, 1748.

51. *Id.* (“PROHIBITION ON ISSUANCE—No credit card may be issued to, or open end consumer credit plan established by or on behalf of, a consumer who has not attained the age of 21”).

52. *See supra* Part II.A.

53. *See* CARD Act § 301. There are two important exceptions to the CARD Act’s ban on credit cards for those under twenty-one. First, a person under twenty-one years old may contract for a credit card if someone else, twenty-one years or older, cosigns and accepts joint liability for the infant’s credit card debts. H.R. 627, 111th Cong. (enacted). Second, an infant may obtain a credit card if she demonstrates “independent means of repaying” her debt. *Id.* The upshot is that independently wealthy teenagers, or those whose parents are willing and able to accept joint liability, will still be able to obtain a credit card, but poor and middle-income applicants may not.

method of selling securities to the public can substitute for, and perhaps even supersede, credit cards and other sources of early stage funding for teenage entrepreneurs.

Subpart A of this Part describes securities crowdfunding in general.⁵⁴ Subpart B claims that this novel financing technique is particularly well suited for teenage entrepreneurs.

A. Securities Crowdfunding in General

Securities crowdfunding is a new idea that builds off of the earlier concept of “crowdsourcing.” *Crowdsourcing* is where the public—the “crowd”—is invited to contribute to an online project without compensation.⁵⁵ Wikipedia is a famous example of an Internet-based encyclopedia, in which many workers, each adding just a bit, collectively created a powerful resource.⁵⁶ *Crowdfunding* differs from crowdsourcing, in that the crowd is asked to contribute money rather than labor.⁵⁷ To date, most crowdfunding projects have been in the form of “reward” crowdfunding where, in return for capital, the funding participants receive the fruits of the project, such as a book, CD, or video game. Websites such as Kickstarter have been doing reward crowdfunding for the past five years, during which time it has quickly grown into a \$1.5 billion market.⁵⁸

Securities crowdfunding takes the concept one step further. Funding participants receive a security, such as a share of stock, a bond, or any other investment contract. For example, in exchange for an investment of \$100, each investor might receive a share in a rock band’s profits from their upcoming tour, which is itself financed through these investments. Until the passage of recent federal legislation as discussed immediately below, however, crowdfunding securities in this way would violate the Securities Act of 1933 as an unregistered public offering. The law allows a person to solicit investments from the public if all that is promised is a CD or concert tickets, as in the case of reward crowdfunding. But in order to sell securities to the public, the Securities Act generally mandates that you first register the securities with the Securities and Exchange Commission (SEC), otherwise the securities will be cancelled and the money returned.

54. See also Schwartz, *supra* note 5, at 1459–77.

55. See <http://en.wikipedia.org/wiki/Crowdsourcing>.

56. See <http://en.wikipedia.org/wiki/Wikipedia>.

57. Schwartz, *supra* note 5, at 1459.

58. See generally C. Steven Bradford, *Crowdfunding and the Federal Securities Laws*, 2012 COLUM. BUS. L. REV. 1, 16-17 (2012) (describing Kickstarter and IndieGoGo as the “leading reward/pre-purchase crowdfunding sites”); KICKSTARTER, *Kickstarter Stats*, <https://www.kickstarter.com/help/stats> (\$1.3 billion pledged to Kickstarter projects alone as of August 25, 2014).

That is, unless the offering is made under an “exemption” found in the Securities Act. “Exempt” offerings are exactly what they sound like: offerings of securities without prior registration. Two important and long-standing exemptions are the private placement exemption, where one sells securities only to family and friends, and the accredited investor exemption, where one sells securities solely to wealthy people (millionaires).⁵⁹ The federal CROWDFUND Act added a new exemption for crowdfunded securities to this list,⁶⁰ pending the promulgation of regulations by the SEC.⁶¹

The CROWDFUND Act includes a number of limitations on the crowdfunding of securities, including the following: companies may not raise more than \$1 million annually via crowdfunding,⁶² investors may only invest a maximum of 5% of their annual income or net worth in all crowdfunded securities each year;⁶³ crowdfunding transactions must be consummated between an intermediary broker dealer or “funding portal”; and issuers may not advertise to the public directly.⁶⁴

Crowdfunding issuers—that is, companies that engage in crowdfunding securities—must provide some basic disclosures to the public, including: (a) the name, address, and website of the company; (b) the names of directors, officers, and substantial investors; (c) a description of the business and the anticipated business plan; and (d) a description of the issuer’s financial condition.⁶⁵ Issuers must also provide a description of the purpose and intended use of the proceeds, the target offering amount,⁶⁶ the price of the securities to be offered, and a description of the ownership and capital structure of the issuer.⁶⁷ Finally, following a crowdfunding round, an issuer must annually file

59. 15 U.S.C. §§ 77d(a)(2), (5).

60. 15 U.S.C. § 77d-1(c)(1)(A). The CROWDFUND Act is Title III of the broader “JOBS Act” which President Obama signed into law in April 2012.

61. *See supra* note 5.

62. Jumpstart Our Business Startups Act, H.R. 3606, 112th Cong. § 302 (2d Sess. 2012) (codified at 15 U.S.C. § 77d(a)(6)(A)).

63. *Id.* (codified at 15 U.S.C. § 77d(a)(6)(B)(i)). Wealthy investors can invest up to 10%. § 302 (codified at 15 U.S.C. § 77d(a)(6)(B)(ii)).

64. *Id.* (codified at 15 U.S.C. § 77d(a)(6)(C)).

65. *Id.* (codified at 15 U.S.C. § 77d-1(b)(1)). The disclosure requirements concerning the financial condition of the issuer vary depending on the size of the offering. Offerings under \$100,000 or less must provide income tax returns for the last fiscal year and unaudited financial statements certified as accurate by the principle executive officer. For offerings between \$100,000 and \$500,000, financial statements reviewed by an independent public accountant are required. For offerings between \$500,000 and the maximum of \$1 million, audited financial statements are required. *Id.* (codified at 15 U.S.C. §§ 77d-1(b)(1)(D)(i)-(iii)).

66. Issuers must also announce the deadline to reach their target amount as well as regular updates regarding the progress of the issuer meeting its target amount. If the issuer fails to reach the goal, the whole transaction is cancelled.

67. *Id.* (codified at 15 U.S.C. §§ 77d-1(b)(1)(E)-(H)).

with the SEC and make available to investors financial statements and a report on the results of operations.⁶⁸

Issuers are prohibited from advertising the offering themselves, and any solicitation of the offering must go through the registered funding portal.⁶⁹ Crowdfunded securities cannot be transferred or sold by investors for one year after the date of purchase, unless being transferred to the issuer, as part of an offering registered by the SEC, or to an accredited investor or family member.⁷⁰ The CROWDFUND Act authorizes civil actions for fraud against issuers, directors, and officers.⁷¹ Finally, the Act expressly pre-empts state Blue Sky laws, effectively prohibiting states from adding additional reporting requirements for crowdfunded securities.⁷²

B. Crowdfunding for Teenage Entrepreneurs

With other sources of financing out of reach for aspiring teenage entrepreneurs,⁷³ securities crowdfunding represents a potentially exciting new source of business capital for teenage-led startup companies. Thanks to the CROWDFUND Act, teenagers who are not allowed to hold a credit card will soon be able to tap the national public market to finance their entrepreneurial dreams.

The cost of crowdfunding securities will be quite modest, especially when compared to a traditional initial public offering (IPO). Crowdfunding companies will be exempt from complying with the extensive securities laws and regulations, saving literally millions of dollars.⁷⁴ In addition, promoting a crowdfunded issue via the Internet will cost a fraction of what a traditional “road show” presently does. By avoiding physical meetings in hotel ballrooms, the cost of an online campaign will be relatively miniscule.

But even this modest cost of crowdfunding—\$5,000 to raise \$100,000, for example—will still be more than a teenage entrepreneur can afford at the outset. To some extent, this illustrates why the CROWDFUND Act does not completely solve the problem created by the CARD Act when it outlawed credit cards for teenagers. A credit card could come in handy to pay for these initial costs of

68. *Id.* (codified at 15 U.S.C. § 77d-1(b)(4)).

69. *Id.* (codified at 15 U.S.C. § 77d-1(b)(2)).

70. *Id.* (codified at 15 U.S.C. § 77d-1(e)).

71. *Id.* (codified at 15 U.S.C. §§ 77d-1(c)(1)(A), (c)(3)).

72. *Id.* (codified at 15 U.S.C. §§ 77r(a)(1)(A), (b)(4)(C)).

73. *See supra* Part II.B.

74. Stuart R. Cohn & Gregory C. Yadley, *Capital Offense: The SEC's Continuing Failure to Address Small Business Financing Concerns*, 4 N.Y.U. J.L. & BUS. 1, 10 (2007) (suggesting that \$20 million is the smallest IPO that makes sense given the costs).

crowdfunding.⁷⁵

In spite of these challenges, teenagers with promising business ideas should be able to find attorneys, accountants, and others who are willing to be paid out of the crowdfunding proceeds. So the cost should not unduly hinder the ability of teenage entrepreneurs to sell securities via crowdfunding. At the very least, securities crowdfunding is a promising new alternative for teenage entrepreneurs, considering that credit cards, bank loans, IPOs, and other sources are out of the question.⁷⁶

Teenagers are ideally positioned to take full advantage of the online marketplace that the CROWDFUND Act will create because crowdfunding will take place entirely on Internet portals,⁷⁷ and teens are well known to be facile with the Internet and other aspects of our online era. Teenagers use the Internet more than the rest of the population,⁷⁸ and they do so in creative ways. Take blogs for instance: Many older people continue to read and maintain blogs, but teenagers have largely abandoned them in recent years in favor of social networking (Facebook) and micro-blogging (Twitter).⁷⁹ This is just one instance of teenagers being on the cutting edge with respect to all things online.

In addition, the CROWDFUND Act requires businesses to post sensitive financial and business information on Internet portals.⁸⁰ This has the potential to make many business owners uncomfortable and is likely to discourage them from attempting to finance their company via crowdfunding. Teenagers, by contrast, are known to be quite willing to share a lot of personal information online, often with an eye toward how it will be received, and by whom.⁸¹ Similarly, teenagers will likely be more amenable than older people to posting business information on the Internet. In sum, there are ample reasons to expect that teenagers will be interested and proficient at raising business capital through securities crowdfunding.

75. This provides a further reason to repeal Section 301 of the CARD Act, in addition to those set forth in Schwartz, *supra* note 1, at 432 (“Section 301 should be repealed.”).

76. *See supra* Part II.B.

77. *See supra* Part III.A. Indeed, “CROWDFUND” stands for Capital Raising *Online* While Deterring Fraud and Unethical Non-Disclosure. Jumpstart Our Business Startups Act, H.R. 3606, 112th Cong. § 301 (2d Sess. 2012).

78. Amanda Lenhart, et al., *Social Media & Mobile Internet Use Among Teens and Young Adults* 4 (Pew Research Center Feb. 3, 2010) (reporting that 93% of teenagers go online, compared with 74% of all adults ages 18 and older).

79. *Id.* at 24 (Pew Research Center Feb. 3, 2010) (“Since 2006, blogging has dropped among teens and young adults while simultaneously rising among older adults.”).

80. *See supra* Part III.A.

81. Mary Madden, et al., *Teens, Social Media, and Privacy* 2–3, 63 (Pew Research Center Feb. 3, 2010) (“Teens are cognizant of their online reputations and take steps to curate the content and appearance of their social media presence.”).

IV. CONCLUSION

Teenage startups are in the public interest and should be encouraged, yet the federal CARD Act of 2009 eliminated credit card financing for many such companies, cutting off an important source of early-stage business capital for teenage entrepreneurs. Since then, however, Congress passed the CROWDFUND Act of 2012 which will allow teenagers to raise early-stage financing through Internet crowdfunding. Teens, being masters of the Internet, are well positioned to exploit this new opportunity, with the upshot being that securities crowdfunding may become an important way for youthful entrepreneurs to fund their business dreams.