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WMRE
Wealth Management Real Estate (formerly NREI)

The Guide to Real Estate Crowdfunding

Presented by Modiv and Wealth Management Real Estate

I've been active in the real estate capital markets for over 25 years and have had the privilege to touch all aspects of the industry to include residential, commercial, institutional, retail, public, private, main street and Wall Street. As my career evolved, I had the opportunity to work on billions of dollars of real estate deals and the honor of being involved with two REITs listing on the NYSE and even taking a publicly traded REIT private in an M&A deal.

In early 2018, I deliberately left the institutional space and went into the crowdfunding arena. I believed then, as I do now, that this exciting and emerging sector presents a tremendous opportunity to provide convenient, lower cost and easier access to commercial real estate for everyday investors. While the underlying premise is centuries old, using technology to enhance access to this valuable asset class presents new and exciting opportunities that traditional institutional asset managers have yet to embrace.

During this journey, I've seen the industry move from a niche capital raising segment to one that raised more than $15 billion dollars in 2020 with no signs of slowing. The industry has grown from financing small residential fix-and-flips projects to providing the majority of the equity needs for multi-million-dollar commercial real estate investment opportunities and helping real estate investment managers achieve even more size and scale.

But while real estate crowdfunding has grown in terms of size and acceptance, there are still many investors – both big and small – who have yet to fully understand what crowdfunding is, how it works and where the future might take us.

Because of that, we partnered with Wealth Management Real Estate to produce The Comprehensive Guide to Real Estate Crowdfunding. Our goal is for this to be an educational resource on the industry, to help explain why crowdfunding is so interesting in the evolution of real estate capital markets and where we think this industry could be headed in the years to come based upon what we've seen in the evolution of similar industries.

If you enjoy this overview, I encourage you to also watch the on-demand webinar we produced with WMRE earlier this year: The Emerging Role of Crowdfunding in CRE Investing. During the discussion, we were able to get into even more detail and insight on this exciting and evolving industry.

Investing is a journey. So whether you are new to real estate crowdfunding or are an experienced investor, I hope you find this guide useful as you navigate your own path towards fulfilling your investment goals.

Aaron Halfacre
Chief Executive Officer | Modiv Inc.
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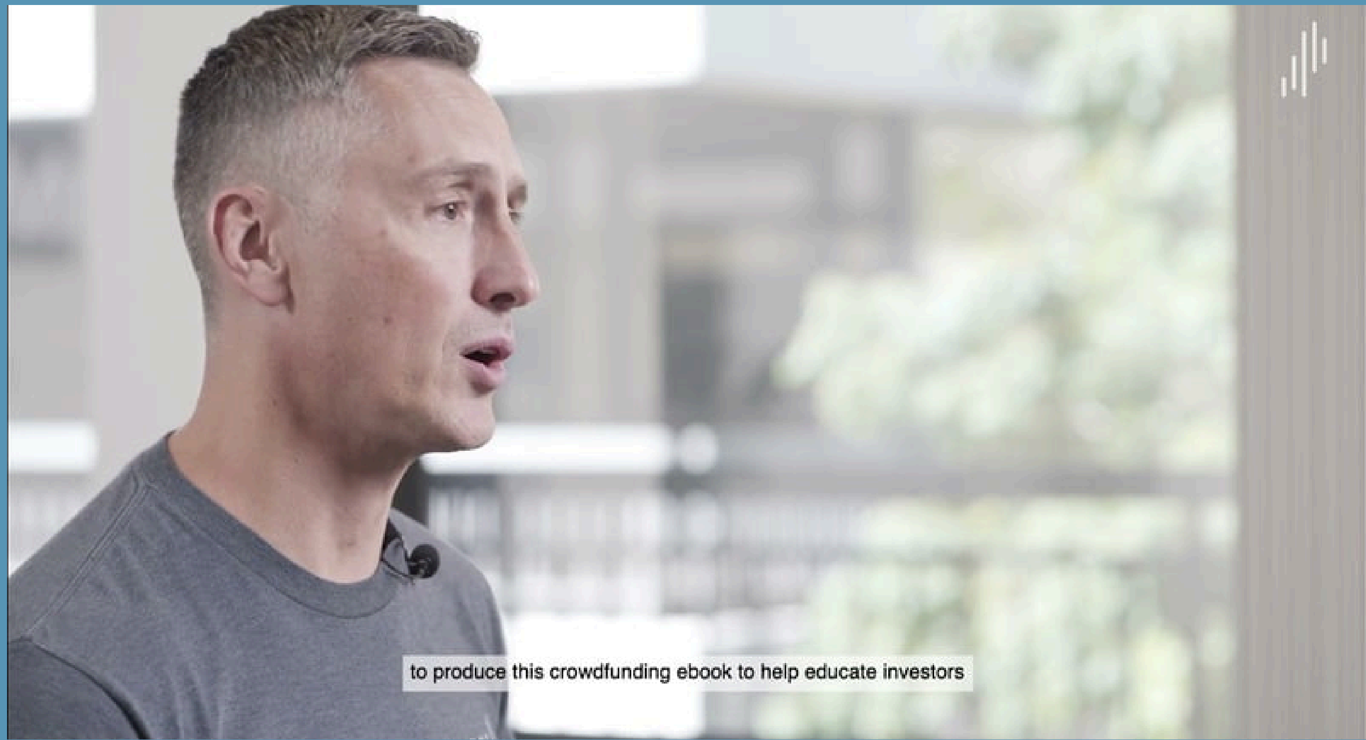

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What Is Crowdfundin g

The evolution of modern crowdfunding might surprise you

If someone asked if you've heard of crowdfunding, most likely you would nod your head and say yes. But what comes to mind and how each person interprets crowdfunding may be quite different.

When it comes to real estate crowdfunding, the term is really a misnomer. The concept of multiple people or a crowd coming together to fund a large capital project has been going on for centuries. In fact, the foundation for the Statue of Liberty was crowdfunded back in 1885, allowing it to stand in New York City as opposed to Baltimore, Boston, San Francisco or Philadelphia, which had all offered to pay for the statue's relocation.

What was missing then that people have come to expect from crowdfunding today is the technology component. So, a modern definition of crowdfunding is something along the lines of: economic funding by a large number of people, typically in smaller amounts, via a website or mobile app. Today, that definition could also be applied to Schwab, Vanguard, Fidelity and Robinhood – companies that are taking economic fundings in small amounts via technology. But, you probably don't think of those companies in terms of crowdfunding.

While technology has driven the growth of crowdfunding the past decade, along with new regulations, the Statue of Liberty campaign resembles modern crowdfunding in a number of ways:

- A large number of participants
- Relatively small dollar amount of each contribution
- Speed at which funding was raised
- Use of a single point of collection

Rewards-Based vs. Asset-Based Crowdfunding

Today, there are two primary types of crowdfunding: rewards-based and asset-based.

Does Not
Provide a Monetary Return

- Charitable causes
- New product inventions
- Artists and content creators

Designed To
Provide a Monetary Return*

- Businesses (debt & equity)
- Real Estate (debt & equity)
- Other/Niche (Art, Alcohol, Autos, Memorabilia, etc.)

Rewards-based crowdfunding encompasses platforms such as GoFundMe, Patreon, Kickstarter, and IndieGoGo. With rewards-based platforms, individuals can crowdfund businesses, new product ideas, charitable causes or their favorite YouTube personality.

In these scenarios, economic funding is provided but an economic reward is not returned. The contributor may receive a product, recognition or, in the case of a charitable cause, general goodwill. Typically, rewards-based crowdfunding is not designed as an investment with the prospect for potential returns.

On the other hand, asset-based crowdfunding is designed specifically for the contributor to make an investment and potentially earn a return on that investment. These types of crowdfund investing platforms were able to come about following the 2012 Jumpstart Our Business Startups (JOBS) Act.

The JOBS Act changed how investment capital could be raised by modifying rules originally put in place as part of the Securities Act of 1933. Title II of the JOBS Act allowed issuers, sponsors, syndicators and others who are raising capital from private investors to be able to advertise those private-investment opportunities to accredited investors under certain conditions.

A sampling of popular rewards-based and asset-based crowdfunding platforms.

Previously, Regulation D, Rule 506 restricted open solicitation and advertising of private investment opportunities, limiting sponsors' fundraising to only pre-existing relationships. Rule 506(c) created by the JOBS Act allows sponsors to solicit investment opportunities to accredited investors under certain conditions. In 2016, Title III of the JOBS Act – also known as Regulation Crowdfunding (Reg CF) – went into effect, permitting private early-stage companies to raise money online through an SEC-registered broker-dealer or a funding portal from non-accredited investors.

In addition, Title IV of the JOBS Act directed the SEC to amend Regulation A to exempt companies from burdensome Securities Act registration requirements for certain offerings of up to $50 million (now $75 million). The SEC adopted final rules for implementing this directive by amending Regulation A in 2015. The amended Regulation A allows sponsors to advertise generally to the public and allows non-accredited investors to invest in companies that are not publicly traded as long as the offering is under $75 million and the sponsor files certain forms with the SEC.

Within asset-based crowdfunding, there's a wide spectrum of opportunities. Sites like MoneyMade.io provide comprehensive listings of various crowdfunding platforms, along with reviews and additional resources to help navigate the myriad of options available.

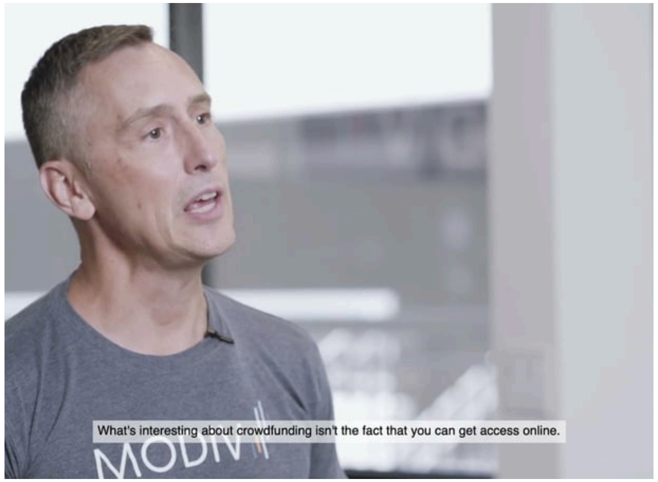
In general, asset-based crowdfunding can be broken down into three common types: businesses, niche markets and real estate.

Businesses: These are typically start-up businesses, oftentimes small and seeking venture equity or debt financing to fund their company, usually through Reg CF.

Venture Equity: Through venture equity crowdfunding, investors pool cash to fund start-ups and companies in their early stages in exchange for equity shares. Investors may be able to invest as little as $1,000 and have the potential for large returns if the company becomes successful. There are risks of course, including that shares may become worthless should the company fail and there is generally a long illiquid hold period from funding to a company's initial public offering (IPO) or other liquidity event (if either occurs at all).

Debt Financing: Often called "crowdlending," this crowdfunded loan operates similarly to a traditional loan, where money is borrowed and repaid with interest to the pool of individuals that provided the capital for the loan. The crowdfunding platform acts as a middleman to collect capital to fund the loan and later disperses loan payments with interest to the participants. The risk spectrum of credit quality and repayment likelihood varies widely, just like with other types of lending.

Niche Markets: With niche market crowdfunding, an asset is bought at a certain price today and sold later, hopefully at a higher price. If a sponsor believes there's a potential return or way to generate income from it, they can package it as an investment vehicle and try to raise capital via a crowdfunding platform. This market encompasses everything from wine and bourbon to sports memorabilia, artwork and automobiles.



Real Estate: The last common type of crowdfunded investing is in real estate. Prior to the JOBS Act rule changes, many investors had limited access to real estate investments. Commercial real estate was often held through direct ownership, private funds or publicly traded REITs.

Direct ownership is often unattainable or unsuitable for many investors because of the high purchase price of commercial properties in addition to property management costs and other expenses related to directly managing a property.

Purchasing shares in private funds is typically only available to accredited investors and often requires a high minimum investment of $25,000 or more. Investments in publicly listed REITs are available to most investors. However, because these shares are publicly traded and most are considered mid-cap stocks, they tend to be added to numerous indices that might be traded by ETFs or hedge funds which can result in higher price volatility when compared to private real estate.

Real estate crowdfunding has increased access for the average individual investor, in part due to the use of technology, by presenting opportunities to invest in single properties or in a portfolio of assets via a crowdfunded REIT or fund, in some cases for $500 or less. While some crowdfunding platforms are open to non-accredited investors, many crowdfunding platforms limit access to accredited investors only with higher minimums.

“Technology is leveling the playing field by reducing costs and increasing access to the private real estate market,” explained Matt DiLallo, who covers REITs and crowdfunding for Millionacres. “That’s opening the door for nearly anyone to invest in this lucrative market that was once only available to well-connected ultrawealthy investors.”

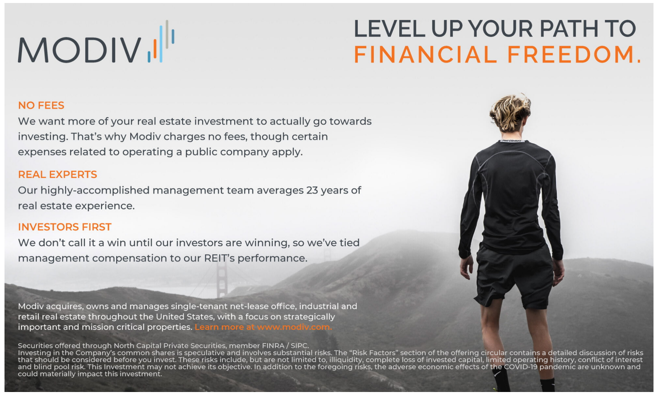
But investing via asset-based

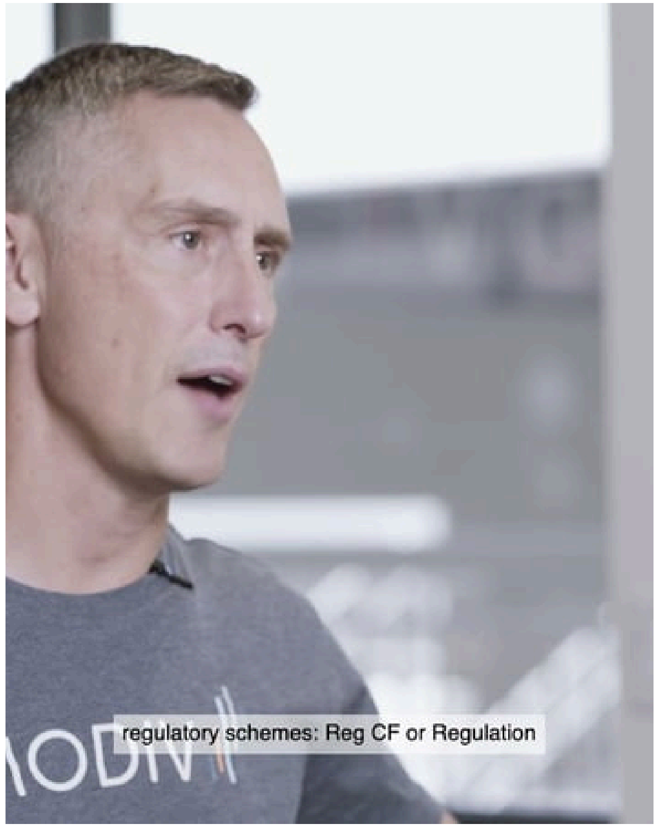
crowdfunding isn't without risk, of course. It's a relatively new industry without a track record of long-term performance. Investors may have to rely heavily on the management team to make diligent decisions while being locked in a potentially illiquid asset. And as with all investments, there are inherent risks that crowdfunded investment opportunities may fail and all the capital invested could be lost. Investors should seek out crowdfunding opportunities where there is meaningful real estate experience, risk management protocols, full financial disclosure and strong corporate governance as all of these attributes help protect invested capital.

To Sum It Up

If it wasn't for crowdfunding, the Statue of Liberty might have ended up as a landmark in another city. And if it wasn't for asset-based crowdfunding, the average investor might not have the same opportunity to potentially benefit from owning commercial real estate.

If you decide to allocate a portion of your investment portfolio to crowdfunded opportunities, make sure to do your due diligence and research the sponsor and the real estate they are managing or planning to invest in. And as always, work with a certified financial professional to help you make prudent investment decisions.





Deeper Dive into Investment Crowdfunding

Crowdfunding platforms provide a gateway to private real estate investments

Crowdfunding has "democratized" real estate investing. That is the catch phrase frequently used to describe how crowdfunding has leveled the playing field for the average Joe and Jane. Investment properties that were once only accessible to large institutions and the ultra-wealthy are now within easy reach of the average retail investor.

Crowdfunding rules introduced as part of the Jumpstart our Business Startups (JOBS) Act unleashed a wave of online real estate crowdfunding platforms that are raising capital from both accredited and non-accredited investors. Those platforms serve as financial intermediaries that connect sponsors looking for equity or debt financing for a real estate acquisition, development or redevelopment project and individuals who want to invest directly in commercial real estate. They leverage technology to bring more efficiency to capital raising by automating and streamlining processes related to communications, financial reporting, disbursement of funds and other functions.

Real estate is an alternative asset class that offers benefits, such as attractive risk-adjusted returns, portfolio diversification and a hedge against inflation. Another key quality that is drawing investors is the fact that privately held real estate has a very low correlation to the stock market, meaning that it helps to stabilize investment portfolios during periods of extreme volatility. Institutional investors and high net worth individuals have long embraced the advantages of commercial real estate investing. The strong demand for real estate is evident in investment sales activity that is once again exceeding pre-pandemic levels. Transaction volume reached $251.5 billion during the first half of 2021, according to Real Capital.

However, individuals who wanted to buy real estate have historically bumped into a variety of obstacles. Chief among them being the cost. Even starting out with a relatively small property, such as a single family rental house, requires a sizable cash down payment. The real estate crowdfunding marketplace offers direct investment opportunities in privately held real estate with as little as a few hundred dollars. Crowdfunding also gives individuals the opportunity to invest in commercial real estate without having to do the heavy lifting of managing properties.

Crowdfunding Offers Diverse Opportunities

Real estate crowdfunding platforms provide a variety of options with offerings across different property types, geographic markets and risk profiles. Offerings range from “fix and flip” homes to institutional quality assets such as trophy office buildings, apartments, shopping centers and industrial warehouses. Investors also can place capital in equity or debt investments and at different points in the “capital stack.”

The “capital stack” refers to the different layers of financing that go into funding real estate that include both debt and equity. Although sponsors can buy a property with all cash, many use debt to stretch their cash and buy high quality or large properties, or even multiple properties. Buying commercial real estate is not unlike buying a home. A homebuyer that wants to buy a $300,000 home may have to put down a 10% down payment – $30,000 – and take out a $280,000 loan to finance the rest of the purchase.

Now consider a sponsor who wants to buy a $3 million apartment building. A typical mortgage lender might provide a loan at 70% of the property value – $2.1 million. The sponsor plans to put in $100,000 in his own equity. That leaves $800,000 in that capital stack to fill. The sponsor decides to raise $400,000 in additional equity from investors and fill the remaining $400,000 gap with a junior mezzanine loan. Real estate crowdfunding firms have emerged as “disruptors” in every part of the capital stack. They raise money from investors to meet each of those different capital needs – senior loans, mezzanine loans, preferred equity and equity. Each offering is structured with different risk-adjusted returns depending on the type of financing. The senior loan is typically the lowest risk as it is backed by the underlying property as collateral on the loan and thus usually has the lowest return. Equity investors have the highest position in the capital stack, meaning they are paid after all of the debt is repaid, which equates to the higher risk and a higher return.

As you can see from above, even when purchasing a relatively small sized apartment building, it becomes nearly impossible for a small investor to do so alone. Taking it one step further, when you consider the purchase of a $30 million industrial warehouse with a high-quality tenant, you are typically only able to obtain a loan for 50-55% of the property value - meaning that as much as $15 million of cash equity is needed to purchase the property. Closing costs alone can run tens of thousands of dollars. Crowdfunding provides an accessibility solution to the individual investor that was non-existent in decades past.

Crowdfunding Firms Adopt Different Models

Real estate crowdfunding is not "one-size-fits-all". Crowdfunding firms have adopted different models that include both direct and indirect structures. In the direct

Syndicators

- Two-sided marketplace
- Transaction volume driven
- Fee & agency considerations

CROWDSTREET
REALCROWD

Hybrid

- FoF structure for syndicated deals
- Best/worst of both models
- Fee & agency considerations

EQUITYMULTIPLE
REALTYMOGUL

Asset Aggregators

- Own title to assets typically in a REIT
- Fees vary widely
- External vs internal management considerations

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investing model, the crowdfunding firm serves as the intermediary that facilitates capital raising between real estate sponsors and investors. Investors invest directly with the individual real estate firm or sponsor and not with the crowdfunding firm. Investors who choose a crowdfunding firm that uses an indirect investing model typically participating via a special purpose vehicle (SPV) that is created by the crowdfunding firm.

The evolution of the real estate crowdfunding sector has resulted in more specialization and diversification. Crowdfunding platforms also have continued to expand with different structures that include single property offerings, funds and private REITs. Crowdfunding platforms also have become more specialized. For example, PeerStreet is one online marketplace that specializes in offering investment opportunities in private real estate loans. RealtyMogul is another group that has expanded its platform by offering public, non-traded REITs.

Real estate crowdfunding is still a relatively young sector that has existed for less than a decade, and crowdfunding firms continue to innovate and test new ideas. For example, Fundrise recently announced that it was making key changes to its Starter Portfolio, which it developed for individuals who are new to investing. Notably, Fundrise has reduced the minimum investment amount on its Starter Portfolio to just $10. Fundrise CEO Ben Miller said in a blog post that: "Our goal is to provide a tailored experience for investors of all net worths and experience levels, whether you're making your first investment ever or investing tens, thousands, or millions of dollars." Such low hurdles once again speaks to the continued efforts crowdfunding firms are making to truly "democratize" access to private real estate investing for all individuals and introduce real estate to a new audience of investors.

Single Asset LLCs

Reg D

K-1

Closed End, liquidity upon sale

Value-Add and Opportunistic

High leverage is common

Blind Pool Funds

- Reg D
- K-1
- Closed End, limited liquidity
- Core, Value-Add and Opportunistic
- Property fees and fund fees

REITs

- Reg A+ and Reg D
- 1099-DIV
- Typically Core, but also Value-Ad
- Most are externally managed
- Fees and liquidity vary widely

History / Continued Evolution of Modern RE Crowdfunding

Crowdfunding continues to gain a bigger foothold as a legitimate capital source in the commercial real estate market. According to Real Estate Crowdfunding Unleashed, crowdfunded transactions in the real estate industry more than doubled in 2020 from $7 billion in 2019 to $15 billion in 2020. Real estate crowdfunding is poised for even more growth ahead thanks to a fresh round of rule modifications from the SEC that went into effect in March 2021.

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Traditionally, raising equity to fund real estate deals was very much a relationship business. Sponsors and syndicators courted potential investors wherever they could find them, whether that was in the boardroom the golf course, or the country club. Oftentimes, they were looking for a small group of "big fish" who were willing to write equally big checks. Building that network of high net worth investors took finesse – and a lot of time and resources. Crowdfunding has been a game changer for real estate sponsors as it moves fundraising that was occurring off-line to online platforms. Sponsors can raise large amounts of capital from "the crowd", including investors both big and small, faster and more efficiently. In addition, sponsors no longer have to rely only on networking in their own back yard team, but now they can raise capital from investors anywhere in the world.

Crowdfunding is a powerful combination of technology and SEC rule changes that emerged from the Jumpstart Our Business Startups Act or JOBS Act of 2012. It was introduced by the Obama Administration to encourage funding of small businesses and stimulate the economy following the Great Recession. The JOBS Act dramatically changed the way groups could raise investment capital by modifying rules originally put in place nearly 90 years ago as part of the Securities Act of 1933. Specifically, Title II of the JOBS Act allowed issuers, sponsors, syndicators and others who are raising capital from private investors to be able to advertise those private-investment opportunities to accredited investors under certain conditions.

In the past, Regulation D, Rule 506 placed restrictions on open solicitation and advertising of private investment opportunities. Sponsors had to limit fundraising to only pre-existing relationships. The new Rule 506(c) created by the JOBS Act allows sponsors and syndicators to solicit or advertise investment opportunities to accredited investors under certain conditions. In 2016, Title III of the JOBS Act – also known as Regulation Crowdfunding (Reg CF) – went into effect that permits private early-stage companies to raise money online through an SEC-registered broker-dealer or a funding portal from non-accredited investors with a max limit of $1.07 million.

Reg A+ Further Expands Crowdfunding

The majority of crowdfunding platforms started out using the Reg D structure that allows companies to market offerings to accredited investors. The introduction of Reg A+ under Title IV rules allows companies to use this structure to market to both accredited and non-accredited investors. In addition, while Regulation A provided a longstanding exemption from registration that permits unregistered public offerings of up to $5 million of securities in any 12-month period, Reg A+ expanded those limits to allow offerings of up to $50 million of securities within a 12-month period.

Regulation A+ rules also provide for two tiers of offerings:

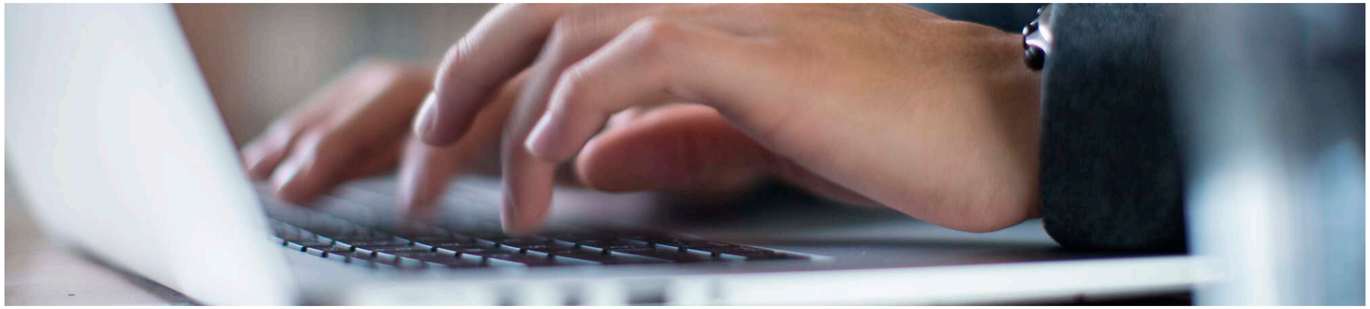
- Tier 1, for offerings of securities of up to $20 million in a 12-month period, with not more than $6 million in offers by selling security-holders that are affiliates of the issuer. Tier 1 offerings will be subject to federal and state registration and qualification requirements, and issuers may take advantage of the coordinated review program developed by the North American Securities Administrators Association (NASAA).
- Tier 2, for offerings of securities of up to $50 million in a 12-month period, with not

more than $15 million in offers by selling security-holders that are affiliates of the issuer. Both Tiers are subject to certain basic requirements while Tier 2 offerings are also subject to additional disclosure and ongoing reporting requirements. The final rules also provide for the preemption of state securities law registration and qualification requirements for securities offered or sold to “qualified purchasers” in Tier 2 offerings.

Rules Continue to Evolve

Rules pertaining to crowdfunding have continued to evolve. In November, the SEC voted to approve some key modifications to both Reg CF and Reg A+ that are expected to drive more growth for real estate crowdfunding. The SEC increased the Reg A+ Tier 2 offering limit from $50 million to $75 million; and also increased the Reg A+ Tier 2 secondary sales limit from $15 million to $22.5 million.

Critics have long said that the original offering limit on Reg CF was too low as it was cumbersome and expensive for small companies to raise a relatively small amount of money. The latest SEC rule change raises the offering limit from $1.07 million to $5 million, removes investment limits for accredited investors and uses the greater of annual income or net worth when calculating the investment limits for non-accredited investors. Further, some industry participants believe increased offering limits for Reg CF and Reg A+ are better solutions than lowering the standard of the SEC’s accredited investor definition as Reg D investments, limited to accredited investors, can oftentimes be considered higher-risk and less liquid investments.



The broad view from the real estate crowdfunding industry is that the latest round of changes will further accelerate growth of the real estate crowdfunding market on both sides of the table – those raising capital and those people who want to invest in crowdfunded real estate offerings. For sponsors, crowdfunding also has provided a tool for not only raising needed capital, but it also has created a way to interact and engage with investors that they could not reach in the past. That allows them to access a much larger audience, and ultimately, an opportunity to grow the investor base exponentially.

A Variety of Real Estate Crowdfunding Opportunities

What it is and how it works.

Despite its recent popularity, the funding of real estate by a crowd of smaller investors technically isn't new – it's been around for centuries. The pedestal upon which the Statue of Liberty stands might be the most famous example of real estate crowdfunding, and it all happened without any technology (except a printing press, which is actually machinery and not technology).

In 1884, when the American Committee for the Statue of Liberty ran out of funds for the Statue's pedestal, Joseph Pulitzer (yes, the namesake of the Pulitzer Prize) urged the American public to donate money toward it. He made the appeal through his newspaper, New York World, and within six months, he'd raised a whopping $100,000 in donations – most $1 or less. About 125,000 people contributed to the pedestal's completion, and Pulitzer published the name of each person who contributed.

If not for real estate crowdfunding, the Statue of Liberty would never have been installed on Liberty Island in New York Harbor. But the investment model fell out of the public eye for most of the 20th century and the early 21st century due to the Securities Act of 1933.

The federal government, in an effort to prevent unsophisticated investors from speculative investments, made it illegal to publicly solicit investors for any type of investment including real estate, says Adam Gower, Ph.D., an acknowledged expert in crowdfunding and the author of Real Estate Crowdfunding Unleashed.

Real estate investment firms could raise money only from people with whom they had a personal relationship, and as a result, real estate investing became the playground of the "country club set". Everyday folk were mostly excluded from investing in real estate deals. (That's why so many crowdfunding players today say they're "democratizing" real estate investing by making it accessible to everyone.)

After Congress passed the 2012 Jumpstart Our Business Startups (JOBS) Act, crowdfunding came roaring back, particularly real estate crowdfunding. Now, accredited and non-accredited investors have an opportunity to build wealth from the world's oldest asset class.

Exploring Ownership Structures

Single-Asset LLC – Both private and institutional investors acquire commercial real estate in single-asset LLCs. It's the most common ownership structure. In this type of structure, the LLC holds only one property, an office building or an apartment community, for example. Each single-asset LLC could be composed of multiple members, e.g. the owners or sponsors behind the deals.

Multi-Asset/Mini-Fund LLC – This type of structure owns several properties, and similar to a single-asset LLC, a multi-asset LLC can have a single member or multiple members. Often mini-fund LLCs target a singular type of property or a specific region, e.g. single-tenant net-lease or industrial facilities in Texas.

Blind Pool/Blind Fund – A blind pool, also known as a "blank check offering", is an investment structure that lacks specific identifiable assets but rather utilizes a broad strategy or stated investment goal for the funds whereby the manager targets a certain type of investment. In this situation, investors aren't investing in particular properties on day one. Rather, they have to trust that the management team will execute on its strategy and is capable of finding properties to acquire. Typically, investors choose to put funds into the blind pools based on the name recognition or the reputation of the management team of the company or investment firm managing the blind pool. Blind pools are often used by private REITs to raise money. As the investment money is deployed in assets and eventually, once fully deployed, is no longer consider a blind pool.

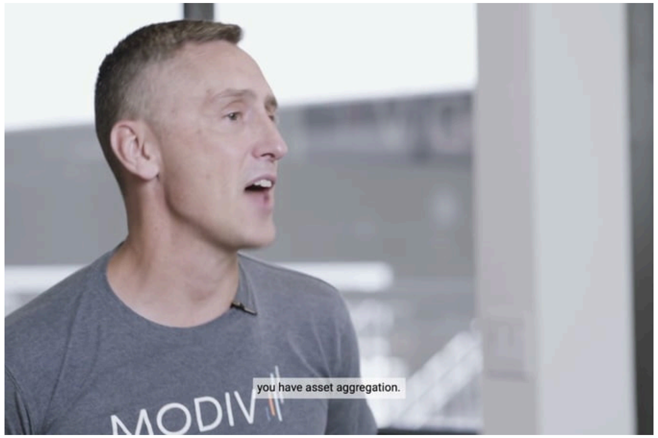
Non-Traded REIT – Publicly-traded REITs and non-traded REITs are similar in many ways. They both provide investors with access to real estate investments with potential tax benefits, and they both must be registered with the Securities and Exchange Commission and make regular, periodic regulatory filings. They both are subject to the same IRS requirements that include returning at least 90 percent of taxable income to shareholders. The biggest difference is that non-traded REITs are not listed on a stock exchange, which can limit the ability for investors to trade in and out of them but are also not subject to public-market price volatility. Non-traded REIT liquidity events often involve merging with an existing publicly-traded REIT, listing on a public exchange, or being acquired by

Real estate owners and investors typically refer to the four major "food groups" of commercial property: **office, industrial, retail, and multifamily**. And even within those segments, there's a lot of variation.

another entity. Many REITs have specific investment strategies and already own a substantial amount of properties, while newer REITs tend to look similar to blind pool funds.

Reviewing the Spectrum of Asset Types

Ask anyone in the commercial real estate industry, and they'll tell you that assets come in a lot of flavors. After all, commercial property is where we live (apartments), work (office buildings and industrial warehouses) and play (shopping centers, restaurants, and hotels).



Real estate owners and investors typically refer to the four major "food groups" of commercial property: office, industrial, retail, and multifamily. And even within those segments, there's a lot of variation. For example, office buildings are differentiated by their location – suburban or CBD (central business district, also known as downtown) – and their design – high-rises/skyscrapers versus low-rise, campus-style buildings.

Beyond the four major food groups, there are several other categories of commercial property that are more specialized:

- Hospitality – motels, hotels, and resorts
- Student housing – purpose-built properties to house college students, either on or off-campus
- Data centers - buildings specifically designed to house internet servers or specially cloud-based data storage facilities
- Healthcare – acute-care facilities, medical office buildings (MOBs), clinics, and seniors housing (assisted living facilities, nursing homes, etc)
- Self-storage - buildings in a wide variety of shapes and sizes designed to store personal property holdings, oftentimes from individuals who no longer have the space in their primary residence
- Government – office buildings, prisons, and courthouses

The next time you're out and about, take a look around – commercial property surrounds us, almost everywhere we are. Even income-producing timberland and farmland are considered commercial property.

Understanding Different Business Models

Third-Party Syndications – When investors come together and pool their money to buy or develop real estate, it's called a syndicate. Real estate syndications make it possible for investors to participate in assets that they wouldn't otherwise be able to afford if they were investing individually.

Fund-of-Funds – There's little mystery here because the name gives it all away. A fund-of-funds is a fund that, you guessed it, invests in other funds, typically mutual or hedge funds. A fund-of-funds usually charges a management fee to its investors while often typically incurring an underlying fee of the fund they are investing in - giving rise to their "double layer of fees".

Externally-Managed REITs – The very first REITs were structured as externally-managed REITs. In this management structure, an external, third party manages the REIT's portfolio of assets. Proponents of this structure contend that it's a simpler and more efficient structure that gives REITs access to sophisticated technology and operational process, as well as experienced executives. Critics point to the past known conflicts of interest and the high fees associated with third-party management.

Internally-Managed REITs – Over time, at the urging of Wall Street, most U.S. REITs have evolved from externally-managed structures to internally-managed. In this structure, an in-house team manages the REIT's portfolio of assets. Many experts say this structure is more investor friendly and appealing to shareholders because an in-house team is committed and focused on only one portfolio instead of many.

If It Quacks Like a Duck...

Is real estate crowdfunding proptech or fintech or something else entirely?

There's a big debate occurring in the real estate investment space right now – people just can't agree on what real estate crowdfunding is.

Is it proptech? Is it fintech? Or is it just plain ol' real estate?

Because technology, specifically the Internet, has generated so much excitement around crowdfunding and made real estate investing more accessible by expanding its reach, many real estate experts say real estate crowdfunding is either proptech or fintech or both.

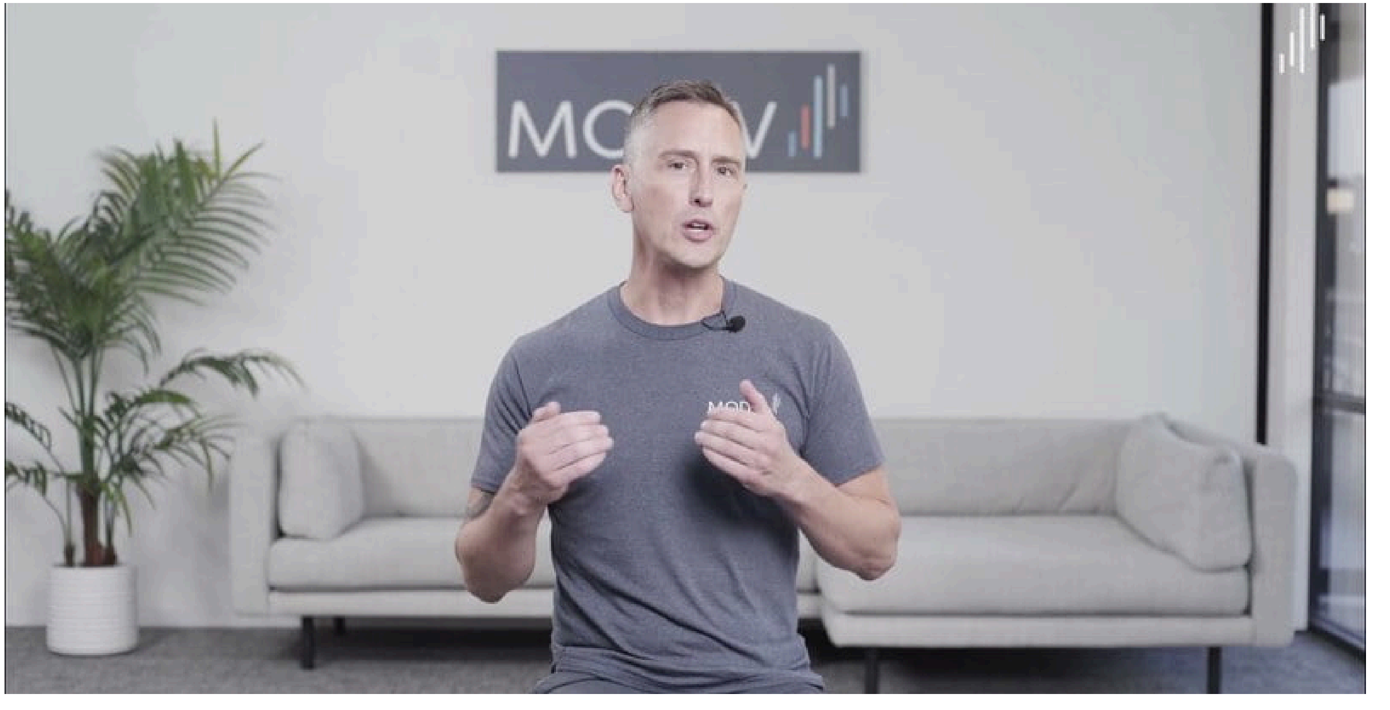
Others, meanwhile, contend that technology is enables real estate crowdfunding activities, which would still occur without technology, albeit slower and less efficiently.

The Pitch for Proptech vs the Facts on Fintech

It's a challenge to say definitively that real estate crowdfunding is proptech because a huge swath of the real estate industry, both residential and commercial, have a hard time explaining what proptech is.

By and large, proptech investors – venture capitalists and the like – have a different definition of proptech than those who develop it or use it. For proptech investors to consider something proptech, it must be new and it must either 1) streamline an existing real estate-related process or 2) disrupt an entire segment of the industry.

Real estate crowdfunding platforms that serve as digital marketplaces are still relatively new. They have an enablement component – they make it easier for sponsors to share offering information and



for investors to evaluate different opportunities. By those metrics, real estate crowdfunding platforms are proptech.

But what about the sponsors who use crowdfunding to finance their investment strategies? Are those sponsor firms/ companies actually proptech companies? Sponsors or syndicators aren't new, and neither is pitching deals to investors. Pooling money from multiple sources isn't new either.

Prior to the internet and property-focused tech marketplaces, investment firms and managers spent most of their time meeting potential investors in person, pitching deals over informal lunches and formal presentations.

In the absence of crowdfunding platforms, though, real estate sponsors would likely find other ways to get the word out. Some enterprising soul would probably eventually wrap a bus in an offering circular.

As for fintech, the official definition is: the integration of technology into offerings by financial services companies in order to improve their use and delivery to consumers.

The question that must be answered: Is a real estate investment firm also a financial services company? Though there are some exceptions, namely private equity firms that invest in real estate debt and provide loans, most real estate professionals would say a financial services firm is a bank, not a real estate sponsor, syndicator, or REIT.

With the power of technology, real estate crowdfunding has the potential **to reach anyone**, as long as they have access to the internet. It doesn't matter if they're located in Manhattan or Manhattan, Kansas.

Technology's Undisputed Role in Crowdfunding

Real estate crowdfunding can happen without technology. The donations that Joseph Pulitzer raised to pay for the pedestal for the Statue of Liberty is proof of that.

However, with the power of technology, real estate crowdfunding has the potential to reach anyone, as long as they have access to the internet. It doesn't matter if they're located in Manhattan or Manhattan, Kansas.

Moreover, the technology offerings available today make it easier than for fund administrators to not only manage their assets, but also handle back-end reporting functions such as collecting the investment dollars, issuing dividend distributions and preparing K-1 forms.

Investor portals can provide more transparency and visibility to investors and make it easier for administrators to communicate with them.

Though no brawls have occurred as the real estate industry endeavors to define crowdfunding, one can only hope that this conundrum can be solved soon.

Your Real Estate Crowdfunding Checklist

Keep these important considerations in mind when evaluating an investment opportunity.

With numerous crowdfunding options available for real estate investing – and new players regularly entering the space – it can be challenging to determine what your best options may be. We've created this checklist to help you navigate through the marketing talk and identify key items for consideration when researching opportunities and conducting your own due diligence.

Fee Structures

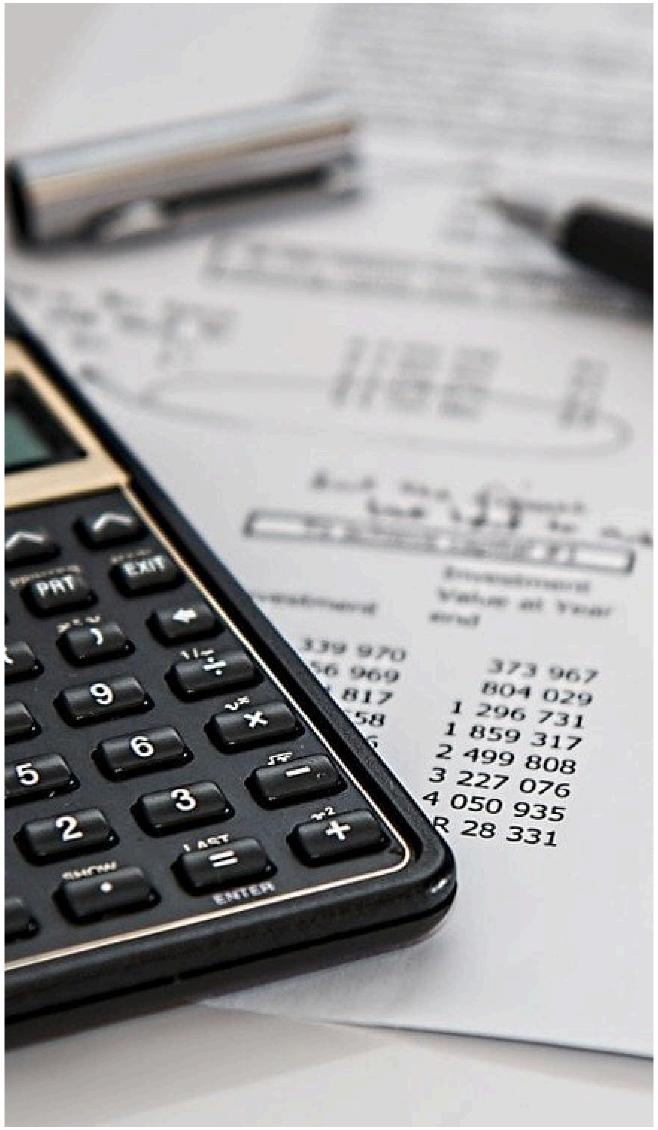
External advisory fees, management fees, performance fees, acquisition fees, development fees—the list goes on and on while margins of return potentially decrease. It's important to understand not only how many different fees a particular platform has, but why those fees are being levied.

It goes without saying that acquiring, owning, managing and operating commercial real estate has inherent costs, particularly as it relates to brokerage and due diligence. However, many sponsors burden an offering with additional fees to increase the revenue and profit to the sponsor—such as a disposition fee charged when a property is sold or an acquisition fee when it is acquired—possibly misaligning incentives between sponsors and investors.

It is incumbent on the platform sponsor to structure their business model so that it focuses on the profit realized by increasing the value of its portfolio—not by charging fees. It's imperative to look for a crowdfunding platform that is transparent about its fee/expense structure and ideally has a sponsor focused on reducing costs across its portfolio, acquisition activities and marketing efforts in order to pass along those savings to the investor.

Most crowdfunding platforms seek maximum fees vs. striving for minimal costs.

- Internally or externally managed
- Impact of placement or syndication fees on potential returns
- Impact of transactional fees on potential returns (i.e., acquisition, financing, disposition)
- Impact of ongoing fees (i.e., asset management, property management, promoted interests)
- G&A expenses within reasonable range
- Sponsor compensation



Real Estate Profile

Many real estate crowdfunding platforms provide access to individual properties, while others provide access to a REIT or fund comprising many properties. Some crowdfunding platforms focus on specific sectors of commercial real estate. Others have a broader perspective. Investors need to pick the one that fits their risk profile. It's important to consider a real estate portfolio that is balanced and has tenants that need the buildings they are in for mission-critical functions.
The type of property, class, location, credit rating and tenant(s) of the individual property or portfolio should all be considered, as well as how much leverage is being used to fund the project or acquisition.

Crowdfunding can provide individual investors with access to quality commercial real estate. Armed with the above checklist, investors can be better informed and prepared to understand how to wisely choose the most effective and efficient investment platform that fits their needs and goals.

Determining whether a professionally managed portfolio of many properties or individual property investments better fits your risk profile is an important consideration.

- Property type(s)
- Investment strategy (i.e., core, core-plus, value add, opportunistic)
- Single tenant vs. multi-tenant
- Geography
- Diversification
- Leverage

Corporate Governance & Transparency

It's important to look for a crowdfunding sponsor that adheres to certain corporate governance best practices, including: registering as a Maryland corporation or Delaware LLC; having a best-in-class board of directors and senior executive team to manage the enterprise; consistent and regular public filings, reports and communications for full transparency; use of a qualified independent external auditor; and formal adoption of compliance policies and procedures.

Investing in real estate through crowdfunding, like any other form of real estate investing, isn't without risk. Many of the real estate crowdfunding opportunities do not offer any liquidity, provide very little transparency and not all of the sponsors have the pedigree that seasoned real estate investors have come to expect. Very few business models check all of the boxes.

- Registered as a Maryland corporation or Delaware LLC
- Independent board of directors
- Documented investment committee procedures
- Compliance standards for capital raising, reporting and communications (including a code of business conduct and ethics)
- Audited public filings with SEC
- Ability to provide for liquidity
- Regular investor communications including earnings calls

Risk Awareness & Management

Many crowdfunding platforms are notorious for presenting very optimistic projected returns produced by certain engineered "models," i.e., financial spreadsheets that create expectations for a certain rate of return on the real estate property being marketed. If those platforms were subject to FINRA, like nearly all other financial products being offered in the market, they would not be permitted to use these metrics due to the inherent subjectivity and speculation involved in creating the models.

> Many of the real estate crowdfunding opportunities **do not offer any liquidity**, **provide very little transparency** and not all of the sponsors **have the pedigree** that seasoned real estate investors have.

All projected returns, often delivered as an internal rate of return (IRR) or equity multiple, are based on many subjective future variables. Those variables include: What will the property be worth later? How much income might the property generate? What is the financing rate? What is the discount rate? How much leverage is being used and is it appropriate? What condition will the markets be in at the targeted exit period? What will it cost to operate the property? What is the vacancy rate? How much will rents increase or decrease? What is the assumed rent growth? What is the assumed sales price? How long will it be held? The reality is that with any investment, the future is unknown and sponsors tend to use assumptions based on a best case scenario designed to make their investment opportunity look more attractive.

Given that this is a relatively new industry and there are a variety of investment vehicles offered, real estate crowdfunding as an industry does not yet offer a long-term performance track record. Investors may have to rely heavily on the management team to make diligent decisions while being locked into a relatively illiquid asset. And as with all investments, there are inherent risks that crowdfunding companies or the individual investments they offer may fail and all capital invested will be lost.

Pay close attention to the overall strategy of the platform, its leadership, and portfolio/product structure to help guide your decision.

Institutional-grade processes have not been broadly adopted across the industry.

- Sponsor experience
- Realistic target returns
- Defined holding periods
- Documented property due diligence processes
- Real estate acumen and experience of management team
- FINRA registration
- Risk profile of investment and risk management protocols used by manager

Crowdfunding can provide individual investors with access to quality commercial real estate. Armed with the above checklist, investors can be better informed and prepared to understand how to wisely choose the most effective and efficient investment platform that fits their needs and goals.

The Future of Crowdfundin g

As has been noted throughout The Comprehensive Guide to Real Estate Crowdfunding, crowdfunding has developed into a successful capital raising source in the commercial real estate industry. Research from GowerCrowd has shown that real estate crowdfunding transactions increased from $7 billion in 2019 to $15 billion in 2020 – tremendous growth for an industry less than a decade in the making and demonstrates the demand for real estate as an asset class among individual investors.

So, as the real estate crowdfunding market begins to mature, what might we expect in the future? Let's start by looking at common real estate crowdfunding business models and then draw some parallels to the financial services industry that evolved quickly following the deregulation of stock commissions in the mid 1970s, which paved the way for how we buy and sell public securities today.

Digital Syndicators, Asset Aggregators and Hybrids

Real estate crowdfunding has two basic business models, but the lines are beginning to blur between the two and there are certainly variations. On one side of the spectrum, there is digital syndication. In this scenario, a company creates a two-sided marketplace. The platform sponsor is soliciting real estate sponsors – people who need to raise capital – and also marketing to investors to raise capital.

Examples of these types of crowdfunding companies are CrowdStreet and RealCrowd. Typically, in this scenario, the crowdfunding sponsor collects a fee for "digitally syndicating" the investment offering. The practice of someone acting as an intermediary to find investors for someone else's project has been around for hundreds of years, but it has now gotten easier thanks to technology. Though digital syndication is relatively new, the act of syndicating real estate deals is

age old. The syndicator in either context is a financial intermediary who collects a fee but may not be around for the life of the investment.

At the other end of the crowdfunding spectrum lies asset aggregation. With this business model, the crowdfunding sponsor raises capital and buys assets that are owned by the platform and/or platform's sponsor, typically structured as a fund or a REIT. The platform sponsor sources and acquires real estate assets in the open market and raises capital from investors to help fund the cost of purchasing the properties. In this business model the real estate crowdfunding platform is taking title to the underlying assets and intends to manage the assets for the life of the hold period.

All of these approaches can have pluses and minuses, so be sure to conduct your own **due diligence** to best understand which approach is most suited for your **investing strategy**.

Examples of these types of crowdfunding companies are Modiv and FundRise. But there are differences in how they can be structured. For example, when you invest in Modiv, you own Modiv, meaning all of the real estate and the fintech crowdfunding platform. The employees work for the platform – not a third-party, external manager – which may help keep incentives aligned.

When you invest in FundRise, you own the real estate (the fund), but fees are paid to the external manager. The investor doesn't actually own FundRise (the company) and the employees work for FundRise, not for the fund, which acts as the external manager.

Hybrid business models attempt to blend syndication and asset aggregation - resulting in the best and worst of both models. This business model typically matches investors to third party sponsors (syndication) but do so via a fund they create to retain assets under management (aggregation). While this business offer may offer the greatest range of selection, the vehicles they use are effectively fund of funds which can be subject to double layers of fees. Hybrid crowdfunding platform examples include RealtyMogul and EquityMultiple.

All of these approaches can have pluses and minuses, so be sure to conduct your own due diligence to best understand which approach is most suited for your investing strategy. Keep in mind that any investment, including those in commercial real estate, a REIT or crowdfunding platform, is speculative and involves substantial risks, including illiquidity and complete loss of invested capital and there are no guarantees dividends will be paid.

The Evolution and Convergence of the Financial Services Industry May Provide Hint to the Future

When looking at the evolution of the financial services industry, there are a number of parallels to the crowdfunding industry.

Let's start with the May Day Act of 1975 which allowed the U.S. government to deregulate stock commissions. Prior to that, stock commissions were set at predetermined levels and the system was regulated, just like AT&T used to regulate the telecom industry and the Civil Aeronautics Board regulated airline prices.

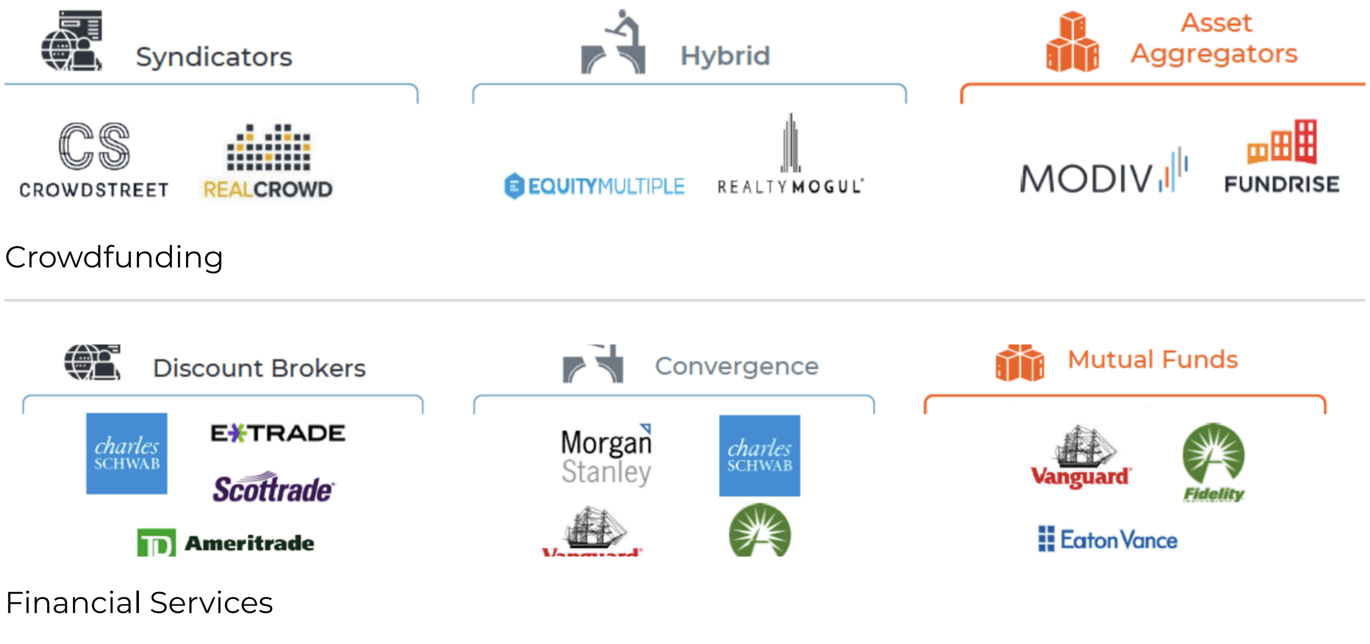
Shortly after the May Day Act, Charles Schwab started the Charles Schwab Company. Schwab was a discount brokerage offering trading at a lower cost. Around the same time, Merrill Lynch increased their stock commissions.

Many industry pundits believed that discount brokerage wouldn't be able to last. They argued that it was expensive to trade stocks, professionals were essential for trading and there were inherent costs and expenses that couldn't be reduced. They foretold the end of discount brokerage. Fast forward to today and their predictions obviously did not become reality. In fact, investors are now accustomed to paying zero commissions when buying and selling stocks. Investors can trade stocks easily with very little cost with the likes of Schwab, Vanguard, Fidelity and Robinhoood. The use of technology made this possible - driving down costs and increasing investor access - two qualities that we are witnessing in real estate crowdfunding today.

There was a plethora of discount brokerage shops that started in the late 70s, 80s and into the early 90s, not unlike what's happened in real estate crowdfunding. But what started happening? Some consolidated. Others went public or listed on a stock exchange. And then there was further consolidation. While there are fewer discount brokerages today, that business model is an industry standard and widely accepted.

There has also been a similar evolution in the mutual fund industry. John Bogle, the founder of Vanguard, started offering a no-load (i.e., commissions) mutual fund in the late 1970's. Prior to that, there were mutual funds where an investor might be paying 3% or more in upfront commissions (also known as front end loads), reducing the amount of the investor's dollars actually being invested.

Bogle turned that approach upside down. His approach was to remove the load charge and, instead, run his business cost-effectively so more of each investor's dollars were invested. Again, the pundits said this business model wouldn't work. And again, the pundits were wrong. Today, low- or no-load mutual fund structures, and their exchange traded fund (ETF) offspring, are the industry standard. In fact, you really have to go out of your way to pay a load on a mutual fund today.



Industry Parallels

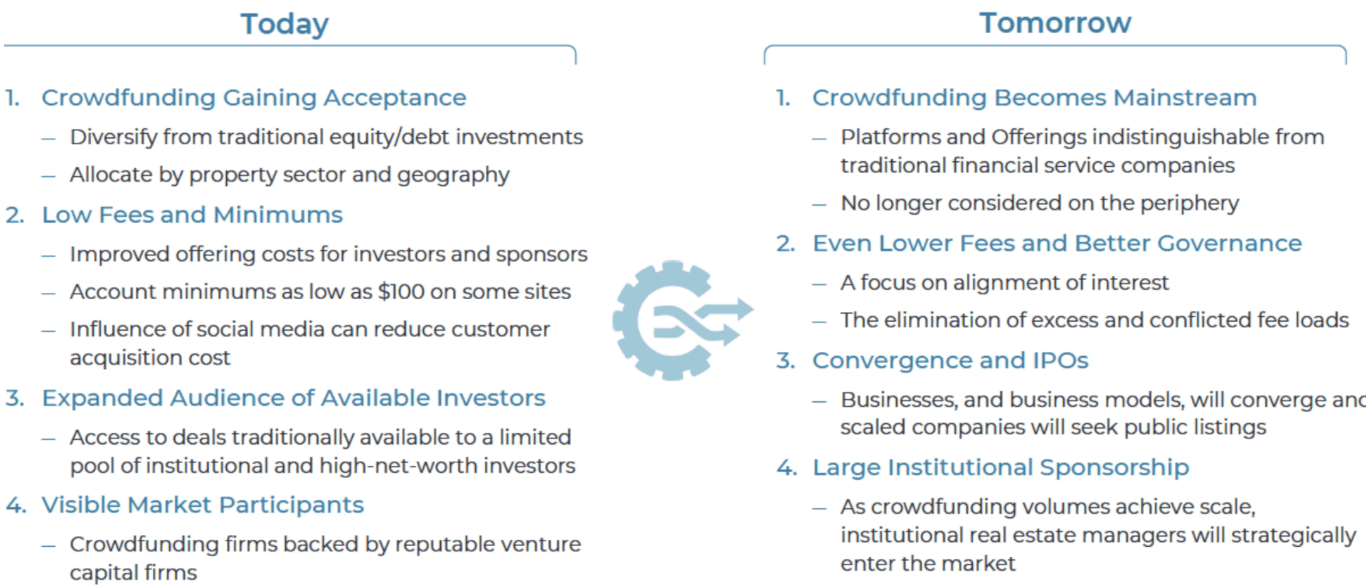
Why so much background on stock brokerage, mutual funds and financial services? Turns out, there are interesting parallels.

As a brokerage firm, Schwab started out as a syndicator, like CrowdStreet today. Vanguard was basically an aggregator, like Modiv is now.

Over the past 30-plus years, Charles Schwab began offering mutual funds and other financial products (i.e., asset aggregation). At the same time, Vanguard began offering brokerage services (i.e., syndication). Now you can use their platforms to invest in their products, buy other products or trade stocks. But when these companies started out, they were at opposite ends of the spectrum, and they were not readily accessible. There was a lot of competition and, ultimately, a lot of consolidation. What they provide today is considered mainstream: providing access to investments at a reasonable cost to millions of investors.

That storyline, or parallel path, is what's relevant to crowdfunding. Some industry experts believe that real estate crowdfunding today is following a similar path that discount brokerages and mutual fund companies took. That could result in different business models converging so that platforms will provide both asset aggregation and digital syndication. Competitors may start to consolidate and, eventually, some of them could become publicly traded companies - just like we witnessed in the financial services industry. Over time, accessing commercial real estate at a low cost could become just as acceptable as trading stocks with no commissions.

Tomorrow may very well see crowdfunding become even more mainstream. Mainstreaming could drive down fees and inspire better corporate governance that more closely mirrors what investors expect from mutual funds and stock brokerage accounts. As the line blurs between syndicators and aggregators, consolidation and the creation of larger, public companies becomes a possibility. And as we've seen in the non-listed REIT space, large institutions may seek to enter the market creating another channel to reach retail investors and grow their assets under management. It also provides more opportunities for individual investors. "I think the industry is heading towards more personalization," predicted Matt

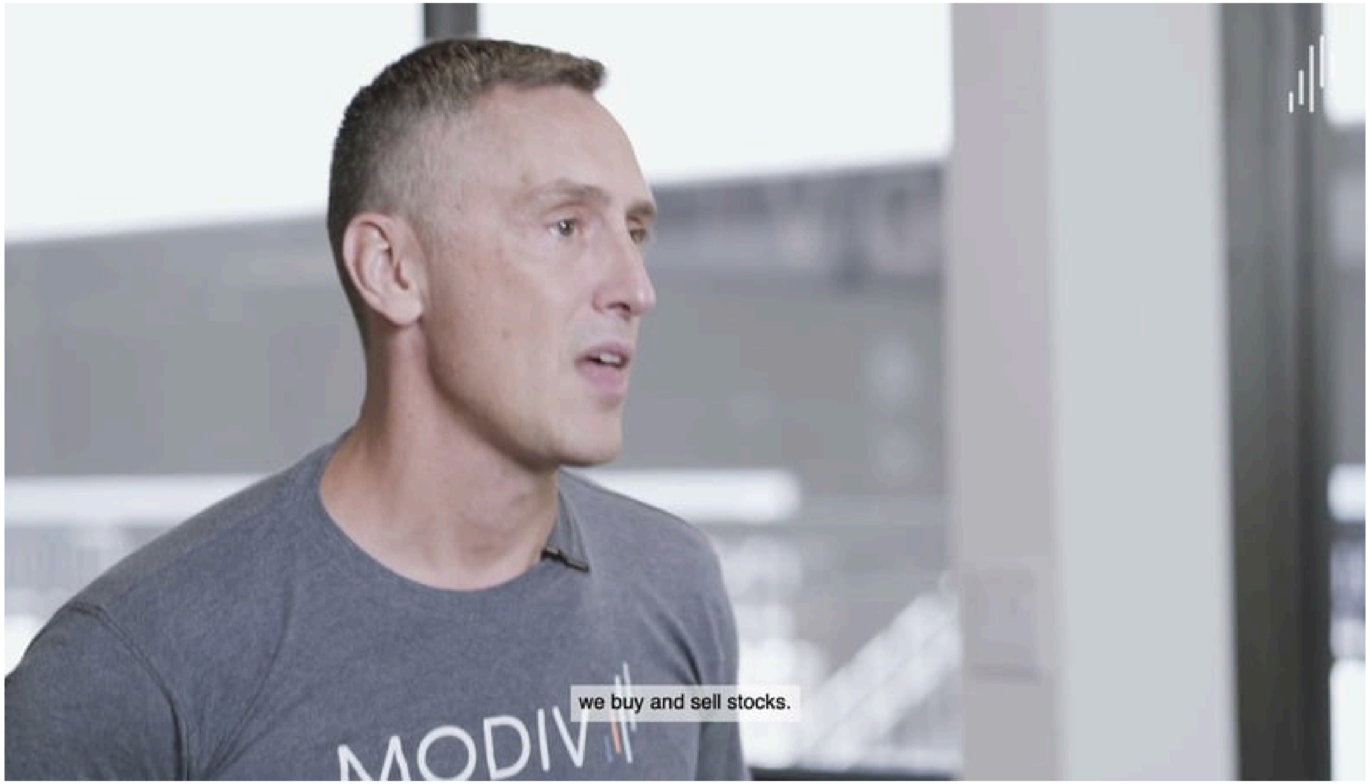


The Evolutions of Crowdfunding

DiLallo, who covers the real estate crowdfunding industry for Millionacres. “Eventually, anyone might be able to build a real estate portfolio that suits their tastes. For example, I personally think it would be exciting to buy stakes in vacation rentals in some of my favorite vacation spots or invest in a redevelopment project in my town. Crowdfunding could one day make this investment dream a reality for more people.”

Time Will Tell

Obviously, none of us has a crystal ball that will reveal what the future holds. With rapid growth, better access for investors and more sophisticated sponsors – as well as the parallels with financial services – the industry appears poised to come into its own. Whether that’s in five, 15 or 50 years, only time will tell. In the meantime, investors have the opportunity to enjoy the potential benefits that commercial real estate may provide, much easier and more cost effectively than just 10 years ago. That is something we can all be pleased with.



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