

FTC Eyes Kickstarter Campaigns for Consumer Protection

Intellectual Property Alert

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Most Kickstarter projects never reach the funding threshold, so funders never pay anything into the venture. However, as shown by recent enforcement action, agencies such as the FTC (Federal Trade Commission) have become interested in the 37% that do receive funding. Those using crowdfunding platforms should take note and renew their attention to the FTC's rules on deceptive trade practices.

Sometimes fraud is obvious. On June 10, 2015, the FTC settled a claim against a company and its CEO, requiring the return of over \$122,000 of funders' money. Money that was intended to fund development of a board game titled "The Doom That Came to Atlantic City" went instead to the CEO's personal expenses and to costs of another project. Unfortunately, there is still no happy ending for the funders; the judgment is currently suspended due to an inability to pay.

While this may have been a clear case of misuse of funds, other misrepresentations in a campaign, while not outright fraud, may still rise to the level of an unfair or deceptive trade practice. The FTC does not have data on how common such practices are on crowdfunding sites, but thinks it is a matter of concern.

Sponsors are eager to sell their campaigns, to get people interested and to generate excitement, among other reasons. But when the description does not openly discuss risks, it can lead to unmet expectations and, worse, a potentially deceptive campaign.

It's one thing when the CEO puts money in his or her own pocket, and quite another when the project experiences commercial failure. Unhappy funders have been promised a "special party," which turned out to be a low-attendance event. Others have been promised products that are delivered after long delays, or are of a much lower quality than expected. Is this deceptive, or merely one of the many businesses that never get off the ground?

In any event, claims should be expected to arise from crowdfunding gone bad.

How to deal with it? When launching a campaign, sponsors should be as open and honest as possible about the risks associated with the project. For example, if a company's founders are first-time entrepreneurs without experience in the particular space, perhaps that should be disclosed. If success relies on external factors, those should be identified and discussed. The clearer and more open a company is about the risks of the campaign, the safer it will

be from allegations or claims like the one recently brought by the FTC.

Kickstarter and other crowdfunding sites have been clear that they do not and cannot guarantee creators' work. Earlier this year, Kickstarter responded to one funder, "Kickstarter itself cannot force the creator to fulfill rewards, offer refunds, or communicate with backers (though we encourage them to do so). In this case, we cannot force the creator to fulfill the reward that the backer has specified."

As Jessica Rich, director of the FTC's Bureau of Consumer Protection, put it, "Many consumers enjoy the opportunity to take part in the development of a product or service through crowdfunding, and they generally know there's some uncertainty involved in helping start something new. But consumers should be able to trust their money will actually be spent on the project they funded."

Lawyers at McCarter & English, LLP routinely advise clients on the law of marketing, the law of crowdfunding, and other issues of interest to start-ups and emerging growth companies, and continue to monitor the space for updates in this rapidly evolving area of the law. We give our thanks to summer associate Cristián Ossa for his assistance with this client alert.