

Crowdfunding as an alternative for credit for young people

Finansowanie społecznościowe jako alternatywa kredytu dla osób młodych

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Abstract. The article treats about practical aspects of crowdfunding. The institution is described on an example of young people who start their first small agricultural business. Some statistical data regarding the quantity of small farms are also shown. Crowdfunding is shown as an relatively easy alternative for credit. Crowdfunding allows farmers to collect money from other people or entities who will also participate in the co-financed project. There are four types of crowdfunding, which depend on the way of participation of co-financiers in the project. The publication shows among others crowdfunding examples in context of small agricultural holding sand some tips how it can be used in practice. The aim of the article is to show a new and legally acceptable form of financing small farms, and above all to indicate a further level for research, which should contribute to the development of crowdfunding in Poland, also in the area of agriculture.

Keywords: creditworthiness • finance • small agricultural business • innovation • legal regulations

Streszczenie. W artykule omówiono praktyczne aspekty crowdfundingu. Instytucja została opisana na przykładzie młodych ludzi, którzy rozpoczynają swoją pierwszą małą działalność rolniczą. Pokazano również wybrane dane statystyczne dotyczące ilości małych gospodarstw rolnych. Finansowanie społecznościowe ukazano jako stosunkowo łatwą alternatywę dla kredytu. Finansowanie społecznościowe pozwala rolnikom zbierać pieniądze od innych osób lub podmiotów, które również będą uczestniczyć w współfinansowanym projekcie. Istnieją cztery rodzaje finansowania społecznościowego, które zależą od sposobu uczestnictwa współfinansujących w projekcie. Publikacja pokazuje między innymi przykłady finansowania społecznościowego w kontekście małych gospodarstw rolnych, oraz wskazówki jak crowdfunding można wykorzystać w praktyce. Celem artykułu jest ukazanie nowej i legalnie dopuszczalnej formy finansowania małych gospodarstw rolnych, a przede wszystkim wskazanie dalszej płaszczyzny do

badań, które przyczynić się powinny do rozwoju crowdfundingu w Polsce, także w obszarze rolnictwa.

Słowa kluczowe: zdolność kredytowa • finanse • drobny przemysł rolniczy • innowacje • regulacje prawne

Introduction

In the introduction of this article there should be defined what a small farm means. Small farms have always been a cornerstone of agricultural activity in the EU. There is no fixed definition as to what constitutes a “small” or a “large” farm. In addition, there is no fixed definition as to when a small farm is rather a subsistence household producing food for its own consumption and is thus not an economic unit (*Small and large farms...*, 2018, p. 2). There is also no single definition of a small farm in Polish law Horonowski and Kryszak (2016, p. 92) say that the diversity of tools used to determine what could be understood as a small agricultural holding, is evidenced by the fact that the definition is determined in an economic and agricultural nomenclature in an ambiguous way. Dudzińska and Kocur-Bera (2013, p. 28) notice that the definition of a small agricultural holding depends on size of the land (area), and varies depending economic and social analyzes. However, the concept used is variously understood depending on the purpose of the analyzes and the country. Thus, we have in Poland different number of small agricultural holdings depending on the criterion of their separation.

The definition can be reconstructed from the text of the document titled “Rural Development Program 2014–2020”. In simplified terms small agricultural holding or small farm is a farm which owner – runs agricultural activity on the territory of the Republic of Poland for commercial purposes, is the holder of an independent or dependent farm within the meaning of the Civil Code, the area of agricultural land is at least 1 ha, has agricultural holding with an economic size of less than 10,000 Euro (the number of such farms in Poland is estimated at 1 019 267) (see: Ministerstwo Rolnictwa..., 2016, pp. 1, 2). Small farms are a place of work for over 75% of the full-time employed in the entire agriculture. In the case of Poland, over 40% of farmers declare that the majority of production from a farm is designated for household purposes (Ministerstwo Rolnictwa..., 17.06.2016, p. 3). It’s worth emphasizing that small agricultural holdings are very important sector of Polish economy. However, according to statistical data, the number of small farms in Poland is falling and will continue to decrease. But as we can find out from the documents of polish Ministry of Agriculture and Rural Development (such as reply of 25/09/2017 to the interpellation of September 4, 2017, number 15008 by Deputy Jarosław Sochajko and Deputy Norbert Kaczmarczyk regarding the effectiveness of agricultural holdings, SAR.an.058.1.2017, p. 10) – the goal of the government is primarily to protect and develop family farms. It should be remembered that according to the principle expressed in art. 23 of the Constitution of the Republic of Poland, the basis of the state’s agricultural system is the family farm.

In the EU many small farms are characterised by the fact that farm holders may struggle to make a living. A characteristic of very small farms is that they are often subsistence households Very small and small farms (in economic terms) are often

unable to provide a viable income for farmers and their families. As such, they are often run either as part-time operations, in conjunction with other gainful activities, or to supplement pensions; these small farms are typically characterised by a high share of family labour (*Small and large farms...*, 2018, pp. 25, 44).

According to EUROSTAT document *Small and large farms in the EU – statistics from the farm structure survey* (p. 140) small and very small farms as defined as below:

Small and very small farms

- 1) By economic size based on standard output in euro:
 - Very small farms: < EUR 2 000
 - Small farms: EUR 2 000 – < EUR 8 000
- 2) By economic size based on standard output in euro, grouped into quintiles: In order to compare the relative weight of the agricultural holdings in each country, farms were sorted from smallest to largest by their economic size and then divided into five groups (quintiles):
 - the smallest farms, defined as those with the lowest levels of economic output who together cumulatively account for 20 % of the total standard output;
- 3) By physical size based on utilised agricultural area in hectares:
 - Very small farms: < 2 hectares;
 - Small farms: 2 hectares – < 20 hectares

According to EUROSTAT Bogacz (2017) notice, that in the European Union small farms account for over 80% of farms. Currently in Poland, 2% of farms have 1 ha or less land. Units within the range of 1–2 ha account for 18% of all farms. Most are farms with an area of 2–4.99 ha – 32.2%. Less than 23% of farms have 5 to 10 ha. In the range of 10–15 ha, there is just over 10%, and from 15 to 20 ha, over 5%. Farms with an area of over 20 ha total make less than 10% of Polish agriculture – the Central Statistical Office (GUS) divided them into units with an area of 20–29.9 ha (there are more than 7%) and more than 50 ha, of which there are only over 2%.

As has been said above, the number of small farms in Poland is falling. This tendency may change slowly towards the rebound and slow growth of new specialized small ecological and innovative farms. Probably the structure of small farms will change from low-income mini-farms, which are run by older farmers, to specialized self-employment sources for younger people. They will certainly need additional financial support at the beginning of their activities. The main source of external financial resources for young farmers are banks and credit unions, but there are also alternative methods of acquiring financial resources – like crowdfunding. Crowdfunding is a relatively new tool that makes it possible to finance a variety of investments, resigning from the relationship with the bank. It is particularly useful when the investor does not have creditworthiness, but has a promising and innovative idea. In this case, the idea itself is a guarantee of the success of the project. Crowdfunding institution, like startups, becomes particularly popular among young entrepreneurial people. Significant group of such people are young (potential) farmers, who are either people who have moved from town to country, or are the next generation of settled farmers (whose families originates from the

countryside). It is worth stressing that a noticeable new social tendency or kind of trend among some groups of young city dwellers, is their relocation from urban to rural areas.

A move from a rural to an urban area was mostly driven by economic and employment reasons, but education-related reasons such as moving for your own or other's education were also important factors. In contrast, when people chose to move from an urban residence to a rural residence, it was also frequently environmental factors prompting the move, such as not being satisfied with previous lifestyle (*Urban and rural dwellers'...*, 16.06.2018). A contemporary tendency is to move away from industrialization towards pro-ecological attitudes. This trend strongly indicates Alvin Toffler, in his book "The Third Wave". He emphasizes that the modern world is moving away from industrialization towards pro-ecological attitudes. "Third Wave civilization" is coherent and workable in both ecological and economic terms, it could be made more decent and democratic than previous "Second Wave civilization," which was based on industry (see: Toffler, 1981).

For example the population of the English countryside will increase by more than half-a-million in the next decade as more people choose to leave cities and settle in rural areas, official figures have found. (*Countryside population...*, 15.06.2018). According to surveys, the rural population will increase by 6 per cent by 2025, leading to a major boom in England's countryside economy. The most recently available figures also show that tens of thousands of people every year are choosing to leave urban areas for the countryside. Many of the people choosing to live in the countryside will also open small businesses (*Countryside population...*, 15.06.2018). A report by the Department for the Environment, Food and Rural Affairs in United Kingdom found that: "It can be expected to drive increased spend and economic activity in rural areas, not least as those relocating to rural areas tend to be relatively wealthier" and: "There is also evidence that people moving to rural areas are more likely to start a business than those already there, helping to drive up economic activity and potentially productivity." The Environment Secretary, said: "People are more likely to start up a business in a rural area than in an urban area. There's a myth out there that innovation happens in cities, that it happens in major towns. In fact, we're seeing lots of innovation, lots of exports, new technology startups, in rural areas" (*Countryside population...*, 15.06.2018).

New inhabitants of rural areas very often want to lead a healthy, ecological life, but they also must maintain themselves and earn money for a living. Their main source of income is often agritourism or other activities that can be performed remotely, for example via the Internet (telework). Second group – farmers from generation to generation – are naturally engaged in farm management and agribusiness. Both of these groups, living in the countryside, will strive for the most favorable living conditions and a stable source of income. One of the most appropriate ways to achieve this seems to be running small family farms and agritourism.

In connection with the above remarks, the following hypothesis was made: small farms run by young people have the chance to transform the character of traditional small agricultural holdings or family farms into specialized, pro-ecological business ventures, at the beginning of their activity the basic source of financing increasingly will be crowdfunding, which is new institution whose use is permitted by applicable Polish and EU law.

Definition of crowdfunding and legal regulations

Crowdfunding is a relatively “young” form of financing that is developing fast in Europe. In Dictionaries it is defined: as practice of funding a project or venture by raising money from a large number of people who each contribute a relatively small amount, typically via the Internet (see: English Oxford Living Dictionary). Currently, we are observing social macro-phenomena consisting in turning towards the information society. Alvin Toffler says that for the so called “Third Wave civilization”, the most basic raw material of all – and one that can never be exhausted – is information. Information became more important than ever before: “Third Wave civilization” will rest on interactive, declassified media, feeding extremely diverse and often highly personalized imagery into and out of the mind stream of the society (see: Toffler, 1981).

The Internet is very important aspect of crowdfunding because project owners send an application to special online platform, which can pre-select projects and ideas, or publish the project/idea without pre-selection. Crowdfunding platform is the basic communication tool for beneficiary and crowd funder. The beneficiary should present to co-financing persons: project, its objectives, deadlines for achieving the objectives, benefits, crowdfunding plan, etc.

Gierczak (2016, p. 12) notice that in contrast to traditional financial intermediaries, crowdfunding platforms do not borrow, pool, and lend money on their own account. They focus on the matching of project initiators and backers by providing information about the projects and functionalities, e.g. for reducing the risks of the investment.

Cumming says that crowdfunding is an alternative way of financing projects, with a focus on small, entrepreneurial ventures. In simple terms, crowdfunding is the way of financing of a project or venture by a group of individuals instead of professional parties. In theory individuals already finance investments indirectly through their savings, since banks act as intermediaries between those who have and those who need money. In contrast, crowdfunding occurs without any intermediary: entrepreneurs “tap the crowd” by raising the money directly from individuals. More conceptually other authors (Belleflamme, Kleemann) extend the definition of crowdsourcing by describing crowdfunding as an “open call, essentially through Internet, for the provision of financial resources either in form of donation or in exchange for some form of reward and/or voting rights in order to support initiatives for specific purposes” (Cumming, 2012, pp. 370, 371). In this sense crowdfunding can become a viable fundraising method available to small entrepreneurial companies or project-based initiatives (Cumming, 2012, p. 389).

Most commonly used classifications of crowdfunding (also used by the EU Commission in its work), is classification which distinguishes between four categories of campaigns: 1) donation-based, in which people do not receive any reward for their contributions (although, depending on the project and the jurisdiction, they can be entitled to tax deductions); 2) reward-based, where people receive goods or services in exchange for their contributions; 3) lending-based, in which contributors receive interest payments in exchange for financing a project with an associated rate of return and maturity date; 4) equity-based, where people receive shares in the venture, in exchange for their contributions. The International Organization of Securities

Commissions (IOSCO) refers to the first two categories as “crowd sponsoring” and the latter two as “crowd investing” (*Crowdfunding in Europe...*, 19.06.2018, p. 1). Small scale or hobby farmers looking to raise smaller amounts of money might investigate donation-based crowdfunding. In donation-based crowdfunding, people who wish to support farm projects contribute money without much of a reward expectation besides the gratitude of the beneficiary or project creator. Farmers who need to raise more significant amounts of money to fund the launch or growth of their project may choose to pursue equity crowdfunding (*Crowdfunding for agriculture...*, 19.06.2018).

In most countries, as in Poland, crowdfunding is not regulated in detail by law, but there are some regulations regarding other legal institutions that are analogously applied to crowdfunding initiatives, secondly there are frames of regulation at the European level.

The European Commission (through a communication and two reports) and the European Parliament (through three resolutions) have taken an active interest in this form of financing. As a result, the Commission has conducted a study on the state of the European crowdfunding market. It found that, while crowdfunding is developing fast, but it is still concentrated in a few countries (the United Kingdom, France, Germany, Italy and the Netherlands), which have introduced tailored domestic regimes, and that it remains, for the time being, a national phenomenon with limited cross-border activity. The study therefore concluded that for the moment there is no strong case for EU-level policy intervention. Nonetheless, given the encouraging trends and the potential of crowdfunding to become a key source of financing for small enterprises over the long term, the Commission noted that it will maintain regular dialogue with European supervisory authorities, Member States and the crowdfunding sector to monitor and review its development (see: *Crowdfunding in Europe...*, 19.06.2018, p. 2).

The growth of the crowdfunding market will continue in the next years. The experts think that the global crowdfunding volume will rise up to US\$35 billion in 2020. The most significant growth is expected in profit-oriented models, such as equity-based and lending-based crowdfunding. For example – looking at the years ahead, the experts are convinced that crowdfunding in Germany will be able to continue to grow, in particular helping creative projects (97%), start-ups (87%) and young growth companies (92%) to raise money (Gierczak, 2016, p. 9).

As was said above, in addition to national legislation, crowdfunding can also be subject to EU legislation, depending on the business model used. The following EU regulations apply to crowdfunding:

- Directive 2000/31/EC on certain legal aspects of information society services, in particular electronic commerce, in the internal market (platforms charging money for successfully financed projects may engage in e-commerce),
- Directive 2006/114/EC concerning misleading and comparative advertising, which provides minimum harmonisation for misleading marketing practices in a business-to-business context;
- Directive 2005/29/EC concerning unfair business-to-consumer commercial practices in the internal market, which protects consumers against misleading and aggressive crowdfunding practices,

- Council Directive 93/13/EEC on unfair terms in consumer contracts, in case the standard terms and conditions used by crowdfunding operators contain unfair clauses,
- Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading,
- Directive 2007/64/EC on payment services in the internal market,
- Directive 2004/39/EC on markets in financial instruments,
- Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms,
- Directive 2011/61/EU on alternative investment fund managers,
- Directive 2008/48/EC on credit agreements for consumers,
- Directive 2002/65/EC concerning the distance marketing of consumer financial services,
- Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms;
- Regulation (EU) No 345/2013 on European venture capital funds,
- Regulation (EU) No 346/2013 on European social entrepreneurship funds (Crowdfunding in Europe..., 19.06.2018, p. 6).

All the above-mentioned regulations may be applicable to crowdfunding also in our country.

Crowdfunding as an alternative to credit

As Daniłowska (2014, p. 96) points out, banks are the main source of external financial resources for small and medium enterprises as well as for small farm holdings. However, raising funds is associated with the conviction of their administrators (banks) that at a given time and on certain conditions they will be returned along with the remuneration.

To get a credit or a loan debtor must have creditworthiness. Creditworthiness is defined by art. 70 of the Banking Law (The Act of 29 August 1997, Dz.U. 2018, item 1075), in line with this provision, creditworthiness is the ability to repay the loan taken together with interest on dates specified in the contract. The borrower is obliged to submit a) documents at the bank's request and b) information necessary to assess this ability. Moreover according to Art. 70. 3. of the Banking Law the borrower is obliged to enable the bank to undertake activities related to the assessment of the financial and economic situation and to control the use and repayment of the loan.

When assessing the creditworthiness of farmers, credit rating models based on the assumptions of Basel III are used. Small agricultural holdings are treated as a subsector of the sector of small and medium enterprises. The analyses, which Daniłowska (2014, p. 99) describes, showed that farmers' creditworthiness is much higher than individual entrepreneurs. This phenomenon stems from the fact that the farm is an

economic base for the existence of farmer's household and the farmer generally does his best to repay debt even at cost of consumption. The regular income subsidies under the CAP are the other reason. Moreover, the additional sanctions connected to repayment of the preferential credits discipline farmers who taken such credits.

However, the repayment of the loan requires effort and the amount repaid is often much higher than the amount borrowed from the bank. Therefore crowdfunding is a reasonable alternative for a credit or a loan. It does not require repayment, it does not generate interest, is therefore a cheaper solution, but it requires a good idea and should offer a specific benefit for the people that are co-financing the project in return. It is very important that the idea of a project funded by crowdfunding initiative somehow replaces the creditworthiness, but similarly to Art. 70.3 of Banking Law (like creditor/bank) the crowd-funder should have transparent information about the idea and the project (not only before starting, but also during the project implementation) to know whether the project is worth financing and whether it will bring the assumed profit.

Crowdfunding – opportunities in agriculture

Crowdfunding offers small agricultural holdings the opportunity to apply directly to investors in order to build up enough funding for their project. This means bypassing banks who may turn down funding applications for a whole host of reasons. It also means anyone can invest in a new business (Singleton, 2016).

As was said above crowdfunding is a kind of alternative to a credit or a loan. It not also can provide money, but what's even more important, through crowdfunding platform (for example Crowdfunder, Crowdcube, UKCFA, Kickstarter, GoFundMe) the project can be popularized, so farmer can easy find cooperation partners, discuss and improve the idea, set up a company or lead the venture, or on the basis of a civil law contract can lead so called share farming. There are special crowdfunding platforms for agriculture, for example: Harvest Returns (<https://www.harvestreturns.com/>). The Harvest Returns platform draws together investors interested in agriculture with a wide assortment of investment agriculture products. With as little as \$5,000, these investors are able to own interests in farms, timberland, or orchards in different parts of the world, each with their own risk/return profile.

As an example of successful crowdfunding project in agriculture can be given an innovative idea which led English young farmer (25 years old) Jack Stilwell to finding help and financial support from an unlikely source. He is known on social media through his "Get Jack Farming" campaign, which he set up during his fourth year at Harper Adams University (see: <https://hubbub.org/p/FarmerJack/>). He wanted to raise £4,000 to allow him to increase the size of his herd, but the obvious question was how to get the funds. The website he used was purely for people to donate if they had an interest in the project, with no equity given in return. His project entailed trying to build his own farm from scratch, starting with a traditional, homegrown British beef herd. He promoted his campaign in the farming press and across social media. Despite raising close to £5,000 through crowdfunding, farmer says the opportunities he

received as a result of the campaign have been more beneficial in the long-term than the financial gain. This has come in the form of two share farming agreements. Both sides of the contract have put a monetary value on what both parties were contributing, then they have split the overheads from the revenue. The surplus was divided between both sides (for more information see: Singleton, 2016). Another example can be beekiping industry – an Australian farmer for patented beehive design, has raised \$2M on the crowdfunding site Indiegogo (*Crowdfunding campaign...*, 19.06.2018, for more details see: The Flow Hive: a lesson in crowdfunding and IP protection, <https://www.ipaustralia.gov.au/tools-resources/case-studies/flow-hive-lesson-crowdfunding-and-ip-protection>). In turn on the Kickstarter platform we can find a project titled “Fresh Truck – Mobile Food Market”. Fresh Truck is a social business that operates a retrofitted school bus as a mobile farmers market, serving Boston neighborhoods with fresh, affordable fruits and vegetables (see: <https://www.kickstarter.com/projects/1530126668/fresh-truck-mobile-farmers-market>). There are many such examples having them in mind crowdfunding seems to be more available than we might think. In addition, it is a completely legal tool, despite the fact that there is no special law that regulates this institution. However, the crowdfunding project should be carefully thought out, and the investor should check what provisions – especially tax regulations – will apply in his or her case.

Conclusions

In conclusion, it must be stated again that crowdfunding is a reasonable alternative to credit. It does not require the disclosure of creditworthiness, which may be particularly difficult for young people who start their first activity – also of a farming nature. It's worth stressing that according to the Central Statistical Office (GUS), the most optimistic opinions about the economic situation in agriculture were expressed by young farmers (up to 35 years old) and people running a farm for no more than 5 years. Moreover satisfaction with the place of residence is in rural areas (80.6%) is slightly higher than in the city (78.4%).

This article confirm the hypothesis set out in the introduction that 1. small farms run by young people have the chance to transform the character of traditional small agricultural holdings or family farms into specialized, pro-ecological business ventures – it's the new social trend, that can be observed recently, 2. at the beginning of the activity of young farmers the basic source of financing increasingly will be crowdfunding, which is new institution whose use is permitted by applicable Polish and EU law. Crowdfunding is not regulated in a separate act, but appropriate national and EU regulations should be applied to it. It is a fully legal, innovative method of financing, that can also be applied to small agricultural initiatives – similarly to small enterprises and startups. There are many examples of successful financing of agricultural projects from this alternative source. In Poland crowdfunding is still little known and its potential is not used, but the possibilities which it offers are worth considering.

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Zaakceptowano do druku – Accepted for print: 22.10.2018

Do cytowania – For citation:

Frańczuk, M. (2018). Crowdfunding as an alternative for credit for young people [Finansowanie społecznościowe jako alternatywa kredytu dla osób młodych]. *Problemy Drobnych Gospodarstw Rolnych – Problems of Small Agricultural Holdings*, 3, 41–51. doi: <http://dx.doi.org/10.15576/PDGR/2018.3.41>