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Eighteen Sustainable Revenue Channels

As the great one, Wayne Gretzky, once said, “Always be skating to where you think the puck is going to land.” The same applies to building a business from the ground up. When sketching out a business model for any business you might be thinking about starting, always picture the most desirable end result. For example, in the case of recommender communities, your most desirable end result is users group meetings. These are known by their modern name, *industry trade shows*. They are huge moneymakers because their producers rent air inexpensively for a few days, and sublet it at very high prices. The air is space in a hotel for seminars, exhibitor space, reprints of seminar topics, souvenirs, and space for attendees, who pay entrance fees, to meet with other users, speak with exhibitors, and listen to and query speakers at the seminars.

If your recommender community attracts 5,000 members to its users group meeting, each of whom pays $300 to attend, and 50 corporate exhibitors, each of which pays $40,000 for their booths, and if you take a 10 percent slice of $200 per night for the hotel rooms, then before other revenue items, your users group meeting will generate $1.5 million in attendee fees, $2 million in exhibitor space revenue, $500,000 in sponsor fees, and $200,000 in a slice of the room rates, for a gross revenue of $4.2 million. Your costs will be less than $500,000. As the number of attendees grows over the years, all of your other revenue channels grow as well, but not your costs. To paraphrase Irving Berlin, "There's no business like the trade show business." Ask Sheldon Adelson, who sold Comdex for $2 billion.

The loyalty and camaraderie that the users group meeting will generate will embolden the members when they return to their homes and click on for more reviewing, ranking, and rating of their products and services categories. And the theater and evangelizing that can be accomplished at users group meetings can create the glue that keeps your recommender community growing and glowing. We will talk about time-tested theatrical techniques to build passion for the community in Chapter 2.

With that endgame in mind, let's turn our attention to the more propinquitous revenue channels to select—from the date of the launch forward. After all, it is near-term revenue that you are interested in, to make sure cash flow keeps coming in and outside venture capital is minimized. As James Bond said to Pussy Galore as he pulled her closer, "Nothing propinks like propinquity." And so it is with launching an online community: near-term cash flow. Thus, in reviewing the 18 revenue channels, select the ones for your community that bring in the cash the fastest.

I didn't just stumble onto these 18 revenue channels; I came up with them out of necessity. As an angel investor in online communities and mobile social networks (see my company's portfolio at www.sfcapital.com), my angel group frequently invests $300,000 to $500,000 of a community's start-up capital. Our angel group receives, let's say, 20 percent ownership, and the entrepreneurial team keeps 80 percent.

It is my task to avoid a follow-on round of venture capital, because if that happens, our angel group will be diluted to around

10 percent, and the entrepreneurial team will have its stake desiccated to around 40 percent before stock options. At the time of exit, for—pick a figure—$50 million, my personal 2 percent interest gets diluted down to 1 percent or $500,000 from $1 million. Not pleasant. In order to prevent dilution of this magnitude, I observed and conceived of a number of new revenue channels to quickly bring cash into online communities. That kind of defensive thinking also led me to flush out the mechanics of the review, rank, and recommend functions of online communities, which, as you know if you've come this far, is my favorite online community pain-solving modality.

Lets go into depth on each of the revenue channels, and then create a business model for a recommender community that shows in which month the cash comes in from each channel along with an explanation that persuades the payor to pay.

Subscription Fees

There is a price sensitivity about paying for services on the Internet, because it is itself a nonscarce resource. Accordingly, although your members may be able to pay a monthly fee, they may not be willing to pay. Monthly subscription fees can be charged after a year of operations and after the members see and believe that their membership has value—that they are getting value for their money. The amount of the monthly fee depends not only on the clout that your recommender community delivers, but on the topic it covers. A higher fee can be charged by health and financial services communities, because they are of huge concern to the people who are most likely to join them; that is, older people who want to maximize their retirement accounts and live longer, healthier lives. Beauty, sex, dating, legal services, and buying a home are worth quite a bit as well, but not as much as health and wealth. Fighting crime, cleaning up a community, electing honest politicians, eliminating title insurance, encouraging oil companies to invest in alternative energy, and making credit reports more accurate are probably worth a little less.

A graduate student in economics scratching her head to find a good topic for a Ph.D. thesis could do a better job of ranking the pain level of people issue by issue and country by country than I can. An examination of the gross profit margins of publicly held companies by industry provides considerable insight. The higher the gross profit margin, the more confused and murky the solution that the company is delivering. Certain industries have very few competitors, and thus have monopoly power, and that is the case with "embarrassment products" such as tampons and condoms, where it is very difficult to explain in print or television ads why product B is superior to product A. Or take the case of Fair Isaac Company, which has persuaded the credit rating agencies of the accuracy of their algorithms. Fair Isaac sports a gross profit margin of 63.3 percent, and credit rating agency Equifax Corp's is 59.3 percent—both high by anyone's ranking system. Other publicly held companies with exceptionally high gross profit margins are Johnson & Johnson at 70.9 percent, Merck at 76.6 percent, Novartis at 72.5 percent, Pfizer at 84.1 percent, and Bristol-Myers Squibb at 68.8 percent—all pharmaceutical companies. The correlation between the rapid formation of online communities seeking truthfulness about health care and the high gross profit margin of pharmaceutical companies is readily apparent. If you launch a recommender community in this field, and do it successfully, some of that huge gross profit margin will transfer over to the wealth of your community.

Tip Jar

When a member of your community does an outstanding job of reporting a material transgression by a corporation that, for instance, has been calling its product "green" or "organic" when it isn't, and the report leads to a downgraded recommendation by the votes of the members, the reporter should be rewarded with tips. A tip-jar window on the home page of your community that accepts credit card payments should be set up. Into that window will pour a number of $20 to $100 payments. Remember to set a minimum tip of $20 or so, in order to encourage members to dig deeply and thoroughly in their research, thus making the tips worthwhile. If 5,000 members each send $20 to the reporter, the aggregate payment will be $100,000. Of that amount, the reporter will receive 70 percent and your community 30 percent.

That ratio was set by OhMyNews, a Korean citizens' journalism community that invented the tip jar-method of payment. OhMyNews has an Alexa rating of 53,352 (see www.alexa.com, which ranks the popularity of web sites).

Reputation Management Fee

The members will want a continual flow of information on many factors affecting their community. Their loyalty to the community needs glue. The glue is the newsletter, along with the money they can earn in tip jars and their stock ownership in your community, about which more later. One of the main news items is naming or "outing" the corporations or enterprises that have attempted to place employees in the community who act as ordinary citizen members, but in fact are attempting to spread the biased gospel of their employer's product or service. There will also be defectors who hack into the community solely to throw it off of its mission and distract the members with gobbledygook. These perpetrators can be named in the community's weekly newsletter in a column entitled "Red Brigade." By reading the column, members will be warned not to share information with subversives. In the late 1940s and into the 1950s, the New York City Police Department formed the Red Squad, which was made up of police officers who searched for communists. The title was later changed several times to fit the mood of the city. It was named the Radical Squad for a while and then, for some reason, Public Relations.

If you choose "Red Brigade," and every other community founder chooses the same name, then an alert and prescient entrepreneur can launch redbrigade.com to gather the names of all defectors in all social networks and provide a useful service that all community owners will gladly pay for.

The point of the Red Brigade is to maintain the truthfulness of the conversations between members in your community. If someone pierces your community's mission as a place where concerned citizens can discuss their experiences with financial advisors (actually, salespersons) from the life insurance and annuity industry, and this intruder then makes sales pitches for Hartford Financial Group, she could destroy everything you are trying to build. Wikipedia has had a few instances of contributors spreading gross lies, and its "truth squad" had to be quickly assembled to vet the truthfulness of submissions. This could happen in your community; in fact, plan for it and make certain you admit people of the highest probity and rectitude.

There are several ways to investigate the backgrounds of both the Red Brigade truth squad members and new members who appear to be overtly pushing the products and services of a corporation as well as defectors and turnstile jumpers who join the community to disrupt it. One site is www.whois.sc, which will tell you the ownership of a web site. So, if I join your community with the e-mail address dsilver@excrutiatinglyupset.com, you can Google www.whois.sc and learn who owns the URL. This valuable repository does not charge for searches. Another site is www.backgroundspi.com, which does charge for searches. It will tell you if a person has a felony record.

The newsletter needs to contain more information for its members than just the reports of the Red Brigade. The members will want to know if their efforts are resulting in any changes to the industry or the governmental agency that they are trying to disrupt in order to improve its efficiencies. The members will want to know membership growth figures, average daily user figures, the community's Alexa rating, whether any major media have reported on its achievements, means by which they may purchase stock in the community, and what the stock price is worth week by week. The newsletter should also report outstanding pieces of research and the tip-jar value of the reports as well as newsworthy stories about the industry or the governmental agency being disrupted and made more efficient.

The newsletter is a scarce resource within the community, and it is worth charging an admission price for it. If a member wants to enter and read the newsletter page on the community's web site, that is worth something. Five dollars a month, or $60 a year, is a reasonable fee. If you finish your first year with 25,000 members, and if 20,000 of them pay the monthly fee upfront, and get a $10 discount, your company will have earned $1 million. That is a lot of float for a start-up company, and it will obviate raising $1 million of venture capital and giving up some precious stock ownership.

Slice and Dice the Conversation

This revenue channel requires you to make the e-mail addresses of the members anonymous and ambiguous, using some technical services, which are doubtless purchasable online. The e-mail addresses need to be changed continually so that the member is never identified. If their pseudonymous e-mail names are not made anonymous, your community could die before it has much of a chance to live. Be paranoid about the critical aspect of executing your business model, because your competitors will be all over you like white on rice, not to mention the damaged member who will likely be irate.

Various departments of the companies or governmental agencies that members of your community will be talking about as well as rating and ranking will be extremely curious about the conversations that take place in your community. "Curiosity" is probably an understatement. A better phrase is "seriously concerned," because the people who want to know how their product and service is being discussed, ranked, and rated by the wisdom of crowds could have their jobs on the line.

Brett Hurt, CEO of BazaarVoice.com, which manages Wal-Mart's online community said, "Wal-Mart is particularly interested in the negative reviews of members, such as which boom box cover scratches the most, and they react quickly to correct the problem they hear about."

Let's say that your recommender community is designed to rate and rank the credit rating process from credit card issuing companies, to the rating agencies that gather data from them, to Fair Isaac Corp, which gathers the data from the rating agencies and compiles the FICO scores of millions of Americans. The community is formed, and the members contribute their stories of the speed at which the credit card companies issue a 30-days-late or a 60-days-late report to the credit rating agencies. Let's say that the credit card—issuing companies are named Ajax, Bozo, Chumbly, Darth, and Ebo. The members report that Ajax always calls first, as soon as the member is 10 days past 30 days late, and asks for a payment and warns the cardholder that she will be reported only if she becomes 60 days late. They report that Bozo calls only 20 percent of its cardholders and reports the delinquent cardholders for being 30 days late if they become 45 days late. The members report that Chumbly calls 10 percent of its 30-days-delinquent cardholders and asks for a payment, and warns the 10 percent that they will be reported for being 30 days late if they go 40 days late. The members report that Darth does not call at all, but only reports cardholders who are 60 days late. And the members report that Ebo does not call at all and reports cardholders who are 30 days late. Ebo is going to see a sudden rash of customer flight.

One 30-day-late report to the credit reporting agencies results in a FICO score of 770 dropping to 735. For the cardholder who seeks to borrow $500,000 to buy a house, a decline in a FICO score of 5 percent could mean that the borrower will pay 1 percent more in interest, which in this example is $150,000 over 30 years.

The members rank the credit card issuing companies. Ajax gets 90 percent approval from the members; three-fourths of the members report that they are going to tear up their Ebo cards and two-thirds of the members say they are going to cut their Darth cards in half. Bozo and Chumbly cardholders say they plan to work their balances down to $100 and refrain from using the cards.

The conversations that lead up to the rankings of the card issuers can be sliced and diced into reports that can be sold to the banks and card-issuing companies for $100,000 apiece, or your community can offer Ebo a special deal: for instance, "We won't report the results of our members' ranking of Ebo against its competitors for a special price of $10 million." The $10 million can be distributed 70/30 among the members, with the members receiving the larger slice. *Ah,* oligopsony power at its finest. Call it hush money, but Ebo has the staff to have held focus groups, and it didn't. Now it must pay because the wisdom of crowds has spoken. The price charged Darth could be as high as the one charged Ebo, and for the same reasons. *Ah,* the wisdom of Willy Loman's wife: "Attention must be paid."

Port the Community to Mobile Phones

Mobile social networks have a distinct advantage over online communities: When people send voice messages, text messages, or documents from one mobile phone or personal digital assistant (PDA) to another, they are charged by the carrier for the minutes of connect time, and the receiving mobile phone user is charged 10 cents per message. Your community will be generating content, and the minutes that are earned by Verizon, AT&T Mobile, Sprint, T-Mobile, or Bell Canada, or any other mobile carrier, are the reason the call was made. Thus, the mobile carriers are willing to share some of their minute charges with the owners of content. Of course, you have to get your community's content onto the decks of the wireless carriers, and that means negotiating directly with the carriers or going through an aggregator such as Wireless Developer Agency, Lansing, MI, which is under contract to a number of the wireless carriers to select the best content to go onto their decks. Games are very popular and they are typically selected to fill the top positions on the decks. Recommender social networks will soon replace games because of their enormous value-add.

This change will occur for several rational reasons. As the population of web users ages, the people spending more and more time on the Web begin spending less time on games and more time on serious issues; so time is in your favor. Second, the published ratings, rankings, and recommendations of your community could be interesting content that members are likely to want to share with a friend as she walks into a Toyota dealership to see what the automobile recommender community thinks about the new Camry, or to share with a friend who is about to select a law firm to represent her in a contract dispute to see what the attorney recommender community thinks about the law firms in her town.

By sending out ratings, rankings, and surveys to nonmembers—an activity that you should encourage—you are broadening your outreach to new members, and the cost of bringing in new members is borne by current members.

In the near future, RFID chips will be embedded in consumer products, and they will transmit information gathered by the recommender communities and distributed to the vendors to be transferred into the transmitter chip. A consumer with a mobile phone that acts as a receiver for the RFID transmitter chip will be able to read the ratings, rankings, and recommendations right off the packages and not have to request the information from a member of the community that gathers the data on that particular line of products. When the RFID chip revolution comes around, the strongest recommender communities will be able to force the vendors to embed the ratings, rankings, and recommendations of their members onto their packages. They won't have a choice, if the oligopsony power of the successful recommender communities becomes as enormous as I believe it will. (By the way, I know about the RFID chip because the first iteration of it on the consumer level, the EZ Pass, was discovered at the Venture Capital Club of New Mexico, and the inventor, Gary Seawright, a Los Alamos, NM pharmacologist, raised some of his angel capital at the club.)

The revenue channel in the form of payments from mobile phone companies could become significant—but perhaps, not for a year or 18 months. Your community needs to gain traction first and foremost. But, when you are ready to sit down with the carriers and negotiate a slice of the pie, you can expect to receive around 50 percent of the charges they earn on the minutes used to carry your community's content. Payments are made every 90 days like clockwork, and because they are so regular, accounts receivable financing can be raised from specialty lenders who like telecom receivables, and you can borrow on the future payments and thus avoid taking in venture capital. A typical advance rate on telecom accounts receivable is 85 percent, and the interest rate you are likely to pay is in the range of prime plus 1 to prime plus 2 percent. And if the lenders ask you for your personal guarantee, tell them the meeting is over. I don't believe in them for early-stage, entrepreneurial companies. Use this phrase to negotiate away the personal guarantee request: "All my net worth is tied up in the company, and you know that; so why would you want to hold the same collateral twice—the receivable and my guarantee to pay you if the receivable isn't collected?" It is double dipping, and once again I repeat: Do not give your personal guarantee to a loan backed up by contractual receivables from the nation's wireless carriers. They're good for the money.

Accounts receivable lenders that like telecom receivables are Bridge Bank, Marquette, Capital Source, Capital Temp Funds, and Rosenthal & Rosenthal, among others.

The sale of synthetic currency to your members is an additional revenue channel. To get there, you will need to grow your membership to somewhere around SecondLife's size. They have close to 8 million members and 1.5 million average daily users. SecondLife has an Alexa ranking of 2,957, way up there.

Kudos

This revenue channel is similar to the tip jar but also borrows on the notion of the "unexpected reward." People love to be acknowledged, and when a member performs a certain act of brilliance that benefits all of the other members, she can be rewarded by the community management with a bag of synthetic currency and the membership can be encouraged to pay her as well. As this isn't real money, and she can spend it only within the community and with designated vendors and retailers, it is limited; but nonetheless, it is physical, it shines like gold coins, and it brings a sense of pride and accomplishment. When I attended one of the earliest meetings of Kentucky Fried Chicken franchisees back in the 1970s, I noticed that the franchisees wore string ties held together with metallic images of the Colonel. For outstanding achievement, the franchisees' Colonel tie-holder was gold. For not-so-outstanding achievement, the franchisees sported silver Colonel tie-holders. And if your franchise had not done so well, you had to hold your tie together with a paper clip or a rubber band.

Insurance companies and mutual fund marketing companies give kudos at their annual national and regional meetings. For outstanding sales in the Pacific Northwest Region, for instance, the winner is announced and he trots up to the brightly lit podium through a wall of high-fiving hands and shouts to receive an engraved pen set and the embrace of the head of sales and his blonde assistant. Multilevel marketing companies use kudos as a form of reward for outstanding sales. Mary Kay Cosmetics uses pink Cadillacs.

My point of differentiation is to have the community members do some of the rewarding. It's more meaningful, and they have to buy the synthetic currency from the community owner, which means you pick up another revenue channel.

Users Group Meetings

The ultimate goal of your recommender community is the annual users group meeting. Any member can come, as long as he pays for his air fare, his room and board, and an admission fee. Your money will come from selling exhibitor booths. I don't recommend your permitting booth rental to the companies whose products and services your community rates, ranks, and recommends. But there is a whole host of manufacturers and services providers who want to meet your members. The largest group of potential exhibitor booth renters is the computer and software industry, closely followed by the telecom industry, the travel industry (eco travel), food, media, publishing (relevant books), and furniture (media centers for the home). You will see in the business models that follow how to set up and run a successful users group meeting with a highly positive cash flow.

You may have noticed that my orbital summary of the revenue channels in their evection through all possible galaxies of cash flow did not include affiliate ad networks, advertorials, setting up a not-for-profit, team building products, facilities management, or branding fees. I haven't forgotten these stars and planets. They are quite novel and little used, but they may become the most important revenue channels that you will use in solving the pain that consumer products and service producers are feeling as TV viewership declines and web usership and online purchasing rises. Exhibit 1.1 shows the magnitude of the pain that your online community may heal.

As the population of TV viewers ages, and this applies to print media and radio as well, consumer brand advertisers must reach out to web users and online purchasers. Alas, the latter group, raised on the fundamental belief that the Internet is free, click through the ads for the most part. The dilemma for consumer brand advertisers is to find a way to reach web users and online purchasers to present their messages and to introduce new brands in a manner that produces documentable sales. Recommender online communities can achieve that for them. Recommender online communities can heal that pain. Here are some of the newest revenue channels cocooning in the business plan drafts of entrepreneurs.

Sponsorships: All of us have seen the "powered by . . ." sponsorships on the home pages of many web sites. For instance, CNNMoney.com is "powered by . . ." Cisco. The sponsor has paid for the right to have its name front and center on the home page

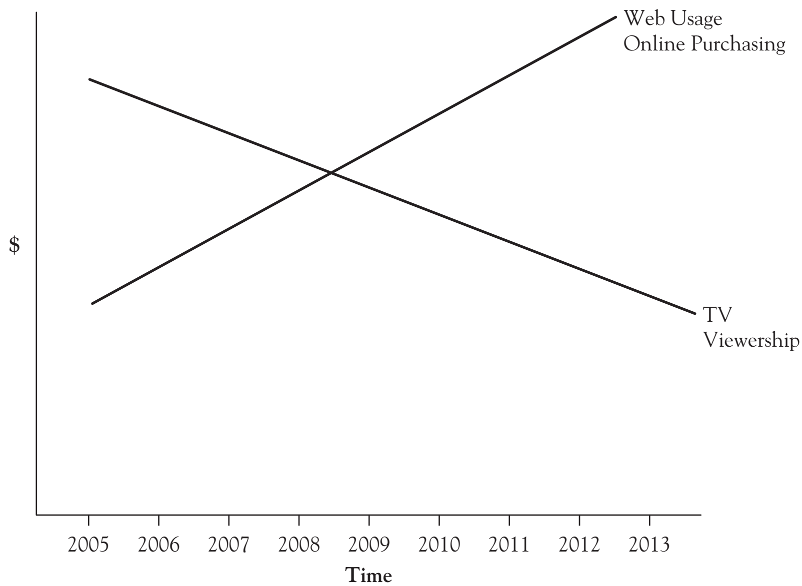

EXHIBIT 1.1 The Pain-Healing Opportunity

of CNNMoney.com, a popular business and financial news web portal. When you launch your recommender social network, call on some corporate giants whose products are not going to be the subject of reviews and ratings in your community, and sell them "powered by . . ." links on your home page. Share your business plan with them, and make sure they understand that at times your members may be outspoken about issues that concern them, and that this could mean speaking negatively about industry companies or government agencies. Several politically agnostic candidates for sponsorships are makers of computer equipment, chips, software, mobile phones, cabling, printers, printer cartridges, and other stuff that enables the Internet to operate. Intel Corp., American Micro Devices, Cisco Systems, Hewlett-Packard, IBM, Epson, and Dell come immediately to mind. Charge them as much as the market will bear, and explain that you plan to port your community to mobile phones and to television, and each time it is ported, the names on the home page that power the community will be seen by many more viewers than just those who have joined the community. If you can collect $60,000 a year per "powered by . . ." slot that you sell, that is a terrific accomplishment for a start-up. Take the money and say thank you. You've just sold something to support a community that hasn't even launched.

The J.D. Powers Business Model

This business model is known as the "validation business," and *wow!* Is it ever a barn burner. There are very few companies in the business of giving out awards to companies for being the best at this or that, and so the barriers to entry are low. J.D. Powers owns and operates call centers, where young people call consumers and ask their opinions of cars, trucks, and other consumer products. J.D. Powers charges the members of the industries it surveys. Oprah Winfrey has validation power and can do wonders for novels. She flew out to Santa Fe in 2007 with her camera crew to interview the publicity-shy Cormac McCarthy, who would not go to Chicago, to discuss his terrific novel, *The Road*. Ms. Winfrey spent a morning with Mr. McCarthy at the Santa Fe Institute, a think tank that studies chaos theory in its many forms, from race relations to getting tenants out of a 50-story building when a fire is reported on one of the floors and there are only four exit doors. In typical Winfrey style, she stayed for lunch and listened to the latest in chaos theory and presented the Institute with a Winfrey-size check. Another validator is *Good Housekeeping* magazine, with its well-known "Seal of Approval."

A recommender community would find it difficult to compete with Oprah Winfrey in the book rating and recommending field, because she is a beloved public figure. But, all of the other marketplaces are available—financial services, legal services, communications, regional offices of the Internal Revenue Service, computers, insurance and annuities, colleges and graduate schools, credit card companies, commercial banks, pharmaceutical companies, regulatory agencies, and the like. And your recommender community will be able to generate its data from raw data: that is, the actual words of the members of the community. J.D. Powers doesn't collect data that way. Its call center personnel write down what they hear, and there can be errors in transmission. Angieslist.com, yelp.com, cityvoter.com, and others are well on their way to becoming great recommender communities in some of these markets.

Who is the payor for validating information? Members of the industry being studied. It's a little like the *Who's Who in America* business, the so-called *vanity business*. You can get your name in *Who's Who in America*, but if you're not a celebrity, you have to pay for the insertion. The validation business works the same way. You take a couple of people with strong voices and good scripts and put them on the phone to the CEOs of the companies your recommender community studies. Your people ask the CEOs if they would like to see a report on how their such-and-such products were rated against the competition, with a million voters (or however many members you have at the time). They may resist at first; but, then you tell them that the ratings and rankings report will be sent to CNN, Bloomberg, MSNBC, the *Wall Street Journal*, the *New York Times*, the *Financial Times* . . . and by then they have gotten out their checkbooks.

Synthetic Currency

I am all about synthetic currencies for recommender communities. I believe it is a differentiator and adds something of a design feature to the process of persuading large corporations and governmental agencies to do the right thing. We know they can do things right, but they need to be persuaded to do the right thing, to borrow Peter Drucker's definition of judgment. The community members should vote on what these judgment calls should be. But some are obvious. Many consumer products companies trade with countries whose judicial systems are oppressive to women. These countries may be banned by the federal government, but the corporations trans-ship to them anyhow through Qatar or Bahrain.

Many manufacturers of consumer products make components for their products in coal-fired plants, and we know that coal is a major carbon emitter. Many consumer products are shipped to warehouses via trucks that burn regular rather than biodiesel fuels. There are various software programs that reduce the number of truck deliveries, hence carbon footprints, such as pallet optimizers and load balancers, sold by Cape Systems and others, but very few vendors use them. Pharmaceutical companies with their 70 and 80 percent gross profit margins could take a 1 percent hit to their margins by dropping the price of drugs that could be distributed by the Gates Foundation and other NGOs to sick people in poverty-stricken countries in Africa.

The synthetic currency can be awarded by the community in the form of kudos to its members to form committees within the community to work on these projects. Or, as is done at SecondLife, which sells Linden Dollars to its members for trading within the community for land purchases, and used in multiplayer games to purchase higher status and weapons, your community can sell synthetic currency to its members, which can then be recommended to the vendors in the industry in which the community is focused as a form of payment for their products. How about the "carbon footprint reducer" kudos, or "carbfoot" dollars spendable on Johnson & Johnson products sold at Walgreens, if Johnson & Johnson energetically agrees to pallet optimize and load balance? A web application company will have to be launched to act as a currency exchange for your community's currency and the synthetic currency of other communities. And the story gets better. If retailers carry the products sold to them by vendors in the industry your community studies, you can recommend that the retailers accept payment in your community's synthetic currency. There is currently an online currency exchange company, called IGE, which exchanges synthetic for real currency; but, clearly others need to be formed to handle the increased volume. Allcom Corp. is creating an online currency exchange company. You can do it in house, and earn the spread. Operating a currency exchange business within your social network is yet another revenue channel.

Affiliate Ad Networks

This revenue channel requires that you build your online community to run on the Web and be concomitantly portable to television. On the six o'clock evening news, and again at ten o'clock, for many of the nation's local TV stations, there is not enough news, and a three- to five-minute story tucked in between sports and weather would delight the producers. The idea isn't new. These stories are called "infomercials" or "advertorials." These are stories that are produced to look like news, but in fact are informative stories about something that could be of interest to the viewers, such as a visit to a vineyard. For certain kinds of social networks, what's going on in the conversations of the members could easily take up five minutes and provide wonderful stories for the viewers.

If your community is one that was organized to bring back the Ozzie-and-Harriet neighborhoods of 1950s, as is Groundswellmedia.com, a Los Angeles, CA, social network, replete with efforts to encourage volunteerism, clean up vacant lots so children can play there safely, discourage rampant development of strip centers, paint crosswalks, and cooperate in other efforts, the get-togethers can be videoed and uploaded into TV infomercials.

Suppose your community gathers the carbon footprint reductions (and increases) of America's major industrial companies and creates a scoring system such as the Dow Jones Industrial Average for stocks. The conversations of the members who gather the data can make an interesting infomercial.

Who pays and who gets paid? The "powered by . . ." sponsors pay the TV stations, since their logos will be on the screen for the full five minutes. For video ads, the going CPM, or cost per thousand sets of eyeballs tuned to the station, is $30 to $70. If the local TV station in Sacramento has 600,000 viewers for its six o'clock news, the sponsors would pay $18,000, from which the community would slice off a 15 percent advertising agency fee, or $2,700. If the community has six sponsors, and all six want to have their logo seen by Sacramentans, the TV station will take in $108,000 less the fee to the community of $16,200.

But one market a business does not make. As Cecil B. DeMille supposedly said when filming the *Life of Christ* in the 1930s, "What do you mean only 12 disciples? I need thousands." The same with infomercials. You will need thousands of local TV stations to turn the Affiliate Ad Network into a serious revenue channel. If your community's story is sold to 100 local TV stations each week for 20 weeks, it will make $3,440,000. And the event can be reproduced quarterly, with new material. Your community will earn 15 percent of that, the typical ad agency fee.

Plus, your community will engage with people who may not have heard of it, and a number of them may join to find out for themselves how much fun your group of collaborators has been having.

A Boon to Local Retailers

Now that you have brought millions of dollars to the local TV station, let's see what you can do for local retailers, and this means newspapers and magazines as well. Let's call your community seriousgardeners.com, and the nucleating issue of the community is to share information about what soil additives, fertilizers, and plants flourish best under what conditions, what geographies, and with what kind of care. In northern New Mexico, we are plagued by grasshoppers, and most of us who garden would give our eye teeth to learn how to get rid of the leaf chewers.

Seriousgardeners.com reviews, ranks, and recommends soil additives for tomato and lettuce plants, and announces the winning additive. Let's call the winning soil additive "Tomato and Lettuce Growth Helper," and let's name its manufacturer Helen of Soil. The community makes stickers available on its web site called "Approved by" stickers and these can be plucked off by garden supply stores around the country and affixed to every package of Helen of Soil. An invoice then gets mailed to Helen of Soil asking for a redemption fee of 10 cents a package for using seriousgardeners.com's "Approved by" sticker to promote their product. Helen of Soil will have to agree to this program, but why wouldn't they? Their marketing department didn't have to lift a finger; the wisdom of crowds is better than any focus group they could have engaged. Once again, for designing, developing, and implementing the program, the community earns an advertising agency fee of

15 cents, or a penny and a half per package. If a million packages bear the "Approved by" sticker, that's $15,000 to the community.

If this process is repeated with 30 different gardening products, that's $450,000 in the cash register of seriousgardeners.com. What about newspaper ads and magazines? Helen of Soil can't use the "Approved by" sticker on ads in these print publications because they are the property of seriousgardeners.com. But Helen of Soil has measured in blind tests that the "Approved by" sticker sells 25 percent more bags of its soil additives in stores that bear the sticker than in stores that do not. Helen of Soil would be a fool not to pay the newspapers and magazines a premium for carrying the "Approved by" sticker, with seriousgardeners.com arranging to put itself in the middle and collect its ad agency fee of 15 percent.

Setting Up a Not-for-Profit

Online communities should set up not-for-profits in buddy-cars running alongside the main community, where grant money can be raised, and the grant money used to solve the pain of people voted on by the community. Contributors should be provided with links on the not-for-profit's web site. If the community is devoted to investors seeking to collaborate on investment techniques used by others, the gifts of the not-for-profit could go to associations that assist teenagers in learning about wealth creation, saving money, and the multiplier effect of investing.

Here's how not-for-profits work. First, Google "grants," and you'll find grants of all sorts. You can assign an eager employee to comb through them to find grants that apply to the issues in your online community. He then writes a number of grant applications. Some are awarded to your community, and some are not. A guild or foundation is formed under Internal Revenue Service Code

Section 501-C3, which grants the foundation not-for-profit status. The funds you take in from the grantors must be spent in the year you receive the money. A modest management fee of 10 percent of the funds can be paid to your community for managing the foundation. If you take in $200,000, the community will earn $20,000.

The foundation will need a board of directors to decide to whom the grant money should be given. The ideal recipients will be those people who might benefit the most in a related field. Using seriousgardeners.com as an example, the grant money can be spent on inner-city gardens, for instance. Naturally, you will want to post placards or small notices in the inner-city gardens that say "Funds Provided by Seriousgardeners.com." It could bring in more members.

Prepaid Credit Cards

The members will be paying for various things on the community, and you might consider creating a prepaid credit card in affiliation with Visa or MasterCard to send to the members when they sign up. The card will bear the name of the community, and it can be used outside the community for purchases, just like a normal credit card. As an accredited issuer of a prepaid credit card you will make money several ways. For instance, with each purchase, Visa will charge 3.5 percent on average, and kick back roughly a third of that to you. You can charge a set-up fee—after all, cards cost about $6 to produce—an annual management fee and a loading fee. If the member accesses her cash from an ATM, there is a fee of a dollar and a half, sometimes more, and the company that owns the ATM will send you approximately one-third of what it earns per use.

The prepaid credit card is also a loyalty builder. When it is used in public, nonmembers will see it and may ask the member about its name, and that could lead to a conversation about the things that the community does. Tip-jar payments can be made with the credit card, and members can buy kudos with it, or if they have collected a lot of kudos, and want to cash in, they can do so more easily with a community credit card.

Some communities have products. For instance, CollarFree.com, a community for clothing designers, sells back to the members the item of clothing that the members voted as best design each month. Designers can make $5,000 to $10,000 a month, and the members are delighted to wear something unique and best in its class.

In your social network, you can ask the members to design community-related products and have the members vote on the best. You can mass-produce them, and you can open a store in your community and sell the tee shirts, hats, bracelets, key chains, and the like that the members vote on—emblazoned with the community's logo. The products can be paid for with the community's credit card.

Another revenue channel to consider using with the credit card is to persuade merchants to give your members discounts when they purchase something using the prepaid credit card. The community can earn a slice of the discount as a fee for setting up the discount programs. That brings the total to six separate revenue channels with the prepaid credit card.

Build-in All 18 Revenue Channels: You now have 18 of the best revenue channels to build into your community. If you work with an outside firm to build and maintain your community, such as OneSite or Pluck, hand them this book and tell them you want all 18. They include the following:

Users group meetings
Subscription fees
Tip jar

Reputation management fees
Slice and dice the conversations
Port the community to mobile phones
The J.D. Powers business model
Synthetic currency/foreign exchange operation
Kudos
Sponsorships/ "Powered by. . ."
Affiliate ad networks
Setting up a not-for-profit
Prepaid credit cards—six separate cash flow channels

I'm going to give you another revenue channel: *branding*. It is massively disruptive and hugely profitable. Look for it in Chapter 6.

For now, a summary of the conversation is needed. I will do that by building a business model of a recommender online community that I call creditefficiencies.com.

Creditefficiencies.com: The Business Model

The heavy lifting in creating a business model is the list of assumptions behind the projections to the monthly cash flow statement. These have to be done granularly and updated continually because events change. Otherwise they are of little value. In what follows, I have created a list of assumptions to the three-year cash flow statement projections, and the cash flow statement projections themselves, to a recommender community. Where the three following conditions exist, a social network will likely thrive: *isolation* of the people most affected or at risk because they have no one to discuss the *complexity* of the issues with (and there are few things as complex as the fees charged by credit card issuers and the scoring of one's credit rating); and *regulation* (and as we know, the U.S. Congress was recently lobbied by the credit card industry to have the federal bankruptcy laws changed to benefit the lenders). I have chosen the credit card, credit reporting, and credit rating industries because of the opacity of the players and the consumers' need to know, plus the three-legged stool—*isolation*, *complexity*, and *regulation*. It could be a very successful social network. I call my community www.creditefficiencies.com.

The primary objective of creditefficiencies.com is to force the credit card issuers, the credit rating agencies, and Fair Isaac Corp. to *behave*—in the words of Max as he faced the wild things in his bedroom in Maurice Sendak's legendary children's book, *Where the Wild Things Are*: "be still." In my opinion, and that of just about everyone I have spoken with and every article I've read on the subject, there is a serious disconnect. I believe the most thorough thesis is "Illuminating the Obscure Model Called Fair Isaac," by Francisco Garcia, Anderson School of Management, UCLA, October 2006. The credit card issuers want us to use their cards as much as possible because they make their money only when we use them. They would like us to be a little bit late in paying our monthly bills and to exceed our borrowing limits so that they can charge us late and overlimit fees. But when that happens, they report our transgressions to the credit reporting agencies that pass along the negative information to Fair Isaac Corp. (FICO), which lowers our credit scores by (I understand this to be true) a significant percent per transgression.

Further, in the FICO algorithm, improvement in our credit scores occurs only when the credit balance in *all* of our credit cards is less than 35 percent of the authorized limit. In other words, the analysts at FICO have determined that if Sarah does not need more than $3,500 of a credit card with a $10,000 limit, she should have a significantly higher FICO score, other things being equal, than Emma, who needs $4,000 of a credit card with the same upper limit. Thus, the primary actors in the drama we know as building and maintaining a reputation for creditworthiness push us one way and pull us another, without working together or for our betterment, and without any clarity as to their objectives, but with considerable misinformation. It is the task of creditefficiencies.com to disrupt their business model and heal pain for credit-cardholders. The business model that we will build and execute has the following characteristics.

Rate, Review, and Recommend

As the founding entrepreneur of creditefficiencies.com, you will want to build your membership massively, to out the defectors and pretenders, and to report the transgressions of the corporations that make obscene profits, and whose top brass earn stratospheric salaries, as a result of not shooting straight with their customers.

To build members quickly, I recommend approaching the most important bloggers to report the news that creditefficiencies.com is up and running—you will need to launch a Web portal, of course, and install a dozen servers to handle the deluge of member sign-ups. Provide them with the PR blurb, which could be something like this: "If you have ever been treated unfairly by a credit card issuer or a credit reporting agency or if you believe your FICO score is too low, here is a new online community that is accepting members who will collaborate and work together to change the industry practices and business methods of credit card issuers and the credit rating and reporting industry."

Initially, the members should be permitted to join for free, except for a *reputation management* fee of $2 per month. This money will be used to find decoys and expose them in the community's newsletter. It will take some clever detective work to locate the decoys and wolves in sheep's underwear, but it can be done; and their names and the companies they work for should be published in the creditefficiencies.com newsletter and broadcast to conventional media. I discussed the method for outing wolves in sheep's clothing earlier in this chapter.

The second revenue source is the slicing and dicing of anonymized conversations regarding the credit card issuers, the credit reporting agencies, FICO, and some of the other alternative rating agencies. You can sell those ratings, rankings, and recommender reports to the members of the industry. Since they borrow so inexpensively—the prime rate is 4 1/2 percent, as I write this—and loan their money so dearly—19 percent plus penalty fees is not uncommon—they can afford a fairly steep price for the report; and it should be multiple-copy protected. If it is published in booklet form, be sure to squeeze the type toward the left side of the pages to prevent photocopying. A price of $10,000 per copy per month sounds about right.

Tip Jar

The newsletter needs stories. The stories that are submitted should be on point; such as one woman's fearless battles with Equifax to remove a dozen untrue statements about her in Equifax's credit report; or one man's year-long battle with TransUnion to remove false tax liens from his credit report; and a college students' story of receiving 30 unsolicited credit cards upon entering the university and his attempts to get rid of them. Readers who learn something from these stories should be encouraged to pay tips to the authors via the community's prepaid credit card with a $10 minimum established at the outset.

The community's owner-operator will keep 30 percent of the tip money and the happy author will receive 70 percent.

Given these three revenue sources, and assuming an exponential membership growth rate, as opposed to a linear one, after month six, see Exhibit 1.2 for the kind of monthly cash flow statement creditefficiencies.com generates:

EXHIBIT 1.2 Creditefficiencies.com 12-Month Cash Flow Statement Projections

($000s)

	Mo. 1	Mo. 2	Mo. 3	Mo. 4	Mo. 5	Mo. 6	Mo. 7	Mo. 8	Mo. 9	Mo. 10	Mo. 11	Mo. 12	Total Yr. 1
Cum. Members	5,000	7,500	1,000	12,500	15,000	20,000	40,000	60,000	89,000	120,000	160,000	200,000	200,000
Report Buyers	-	-	1	3	5	7	12	18	24	30	36	42	42
Revenues:													
Rep. Mang. Fees	10	15	20	25	30	40	80	120	160	240	320	400	1,460
Newsletter Sales	-	-	10	30	50	70	120	180	240	300	360	420	1,780
Tip Jar	-	-	-	2	2	3	4	8	12	16	24	32	103
Total Revenues	10	15	32	57	83	114	208	312	416	564	712	860	3,343
Optg. Expenses:													
Systems Engs.[a]	-	7	7	7	14	14	21	28	35	35	35	42	245
Newsletter Pubs.[b]	21	21	21	42	42	42	84	84	84	168	168	168	945
Marketing Mgmt.[c]	36	36	36	36	36	36	36	36	36	36	36	36	432
Purchase Servers	-	11	-	5	-	-	5	-	-	5	-	10	36
Travel, Telecom	-	2	3	4	5	6	7	8	9	10	11	12	77
Office Rent, Misc.	5	5	5	5	5	5	5	5	5	5	5	5	60
Professional	20	20	5	-	-	-	-	-	-	-	-	10	55
Unspecified	10	10	2	2	2	2	2	5	5	5	5	10	60
Total Optg. Expenses	112	102	85	104	105	118	163	174	180	290	276	294	1,863
Net Optg. Income	(102)	(87)	(53)	(47)	(22)	4	45	138	236	274	436	566	1,480

[a] There is one systems engineer for every four servers for every 20,000 members. A systems engineer is paid $72,000 a year plus benefits at 20 percent.

[b] There are initially three employees who gather data for the newsletter, doubling every six months, and paid the same as systems engineers. They also produce the reports.

[c] The founder and a marketing team run the Company at a cost of $10,000 per person/mo plus benefits at 20 percent.

In this set of just 12-month cash flow statement projections we learn several things. First, the cumulative cash loss is $311,000, which occurs for the first five months of operation, before break-even is reached. Since Murphy's Law applies to all start-ups, it is wise to raise several dollars more than the projected cumulative cash deficit. Raising $400,000 from family, friends, and angel investors would be the wise move.

We also learn that creditefficiencies.com builds cash profitability very fast. In months 6 through 12, it throws off $1.7 million in free cash flow, enough to expand into some interesting areas that are described in Chapter 5—enough to make multiple online community launches as described in Chapter 4.

Silver's Law Applies

For those of you who read *Smart Start-Ups*, I have a fondness for testing business models against formulae that I have used over the years as an angel investor. Assuming you have read *Smart Start-Ups,* I will test the model against the formulae. First, let's see what numeric value the creditefficiencies.com business model produces.

The principal test is whether the problem is a large one, and in this particular case it is not only large, but one of the largest ones in existence. There are 140 million holders of credit cards in the United States. Approximately 40 percent of the holders pay their balances in full every month, which brings down the market size to 84 million individuals. Eighty-four million concerned people is a large homogeneous market by any standards. The second test is the elegance of the solution, which refers to the nonduplicability or first-to-market of the solution and the uniqueness of its means of delivery. An online community that rates, reviews, and recommends credit card issuers and rating agencies can be started by many people; thus, the uniqueness of the means of delivering the solution to the problem will separate the winner from the losers. Third is the quality of the entrepreneurial team, and that is an open item. Executing this particular business model will require skill and guts, because credit cards are major profit centers for banks and the sole profit centers for nonbank issuers; and the issuers will not welcome this particular community with hugs and kisses. If you prefer softball to hardball, this Bud is not for you.

The next eight factors, which I call the *Demonstrable Economic Justification* factors, include the following:

1. *Existence of a Large Number of Receivers:* This opportunity speaks to the awareness of the problem by 84 million credit card holders and by people who want to know how to improve their FICO score. It would seem that every cardholder and potential home buyer would like to save money and have a higher credit rating. As a former commercial banker, I quote a Wall Street homily: "If one has to explain his credit worthiness it is presumed to be in doubt." Accordingly, good credit is something everyone wants because it is a mark of respect.
2. *Homogeneity of Receivers:* Will the consumers accept a standardized solution, or will it need to be customized? Most problems will be of a standard nature, but in the event of a requirement for a customized solution, the community will respond. A member with a problem comparable to one experienced by another member will find a helpful solution—worthy of a tip-jar payment—from the experienced member.
3. *Existence of Qualified Receivers:* Will there be a cost involved in finding new members? Yes, at first, because there will be distrust of any new solution to a problem involving something as private as credit. For instance, we know that people fear identity theft, and creditefficiencies.com may be perceived as a place where one's credit could be stolen. Thus, the community

may need a spokesperson, or a board of advisors composed of some of the top names in finance. Imagine the power of a Paul Volcker endorsement! That could cost a small percentage of ownership, but it would be equity well spent.

4. *Existence of Competent Providers:* The wisdom of crowds is going to be the solution provider, and the solutions they provide will be based on their experience in dealing with sudden increases in interest rates and having the credit reporting agencies remove false information. Only Equifax is a publicly held U. S. company, and therefore open to filing grievances within the judicial system and the New York Stock Exchange. TransUnion and Experian are conveniently based in foreign countries, and immune from conventional dispute resolution mechanisms.
5. *Absence of Institutional Barriers to Entry:* There is no regulatory authority that blocks the oligopsony power of online communities. The playground is perfectly level for creditefficiencies.com to build a reputable business at a relatively low cost.
6. *The "Hey, It Really Works" Factor:* You will need some early, documentable successes in order to make creditefficiencies.com gain traction in its early months. To do this, the community will need some experienced, battle-scarred members to guide some new, timid members through the process of taking their troubles with credit card companies and credit rating agencies and tossing their problems out to the wisdom of crowds to come up with battle plans. When the new members obtain roll-backs of fees and interest rate decreases, and especially when they get untrue statements removed from their credit reports, they can write stories for the community newsletter and possibly earn kudos points and tip-jar money for their journalistic efforts.

7. *Invisibility:* You will want to operate this community very quietly for several reasons. The formula could be adopted by a competitor. The enemy will want to regard you as a tiny blip on their radar. If the enemy thinks you are well-organized and well-funded, they could arm themselves before you are ready for the Battle of the Bulge. Do not talk to the press; operate out of cheap offices in an out-of-the-way location; and shred all paperwork at the end of the day. Always remember that you are attacking the most profitable departments of large banks, and they will do everything imaginable to crush you. Some of them book "Litigation" as a revenue line item!
8. *Optimum Price/Cost Factor:* The community's cost of goods sold will be borne largely by the community's members, except for the cost of servers and the salaries of systems engineers who write programs and maintain the servers. If you charge a reputation management fee going in of $2 per member per month, and if you persuade some of the leading blogs to bring in the members and build an initial base in the first few months of 10,000 average daily users, I would consider that a good start.

Bear in mind that creditefficiencies.com is a David v. Goliath community. You will need to arm David, the community, with slings and arrows, to add to his smooth stone and slingshot. You might consider doing an early disruptive event against one of the credit card issuers or credit rating agencies, in which a success is scored against them; then broadcast the news throughout the Internet with the goal of attracting a threat from the enemy to bring legal action. This is known as Little Richard's Law and its premise is that rock 'n' roll became even more popular in the 1960s when preachers spoke out against it from the pulpits and songs such as "Wake Up Little Susie," by the Everly Brothers, were banned in Massachusetts for being too suggestive. (For more on Little Richard's Law, see *Smart Startups*.)

You say that I preached about remaining invisible, but I was talking about bragging to the press and capturing the interest of the media about membership growth, capturing a major celebrity endorser, or talking about the size of your community. Little Richard's Law is all about getting under the skin of the industry you are trying to disrupt. It is the "irritation" business model: Attack a "brand," the "brand" sues, and your community is famous.

Strength will come to you by taking continual small but important steps that score wins for your members and losses for the opponents. Carefulness will trump creativity in the early days, and new capital will flow in from reputation management fees and tip-jar payments and from utilizing some of the glue factors described in Chapter 5. Initial angel capital of $400,000 or thereabouts should be sufficient to hire a staff of system engineers, build out the community's Web portal, and persuade bloggers to announce the formation of creditefficiencies.com. Your goal is to disrupt an industry that has obfuscated the tautology of their terms and conditions beyond comprehensibility and has thus taken advantage of consumers for dozens of years. You can heal pain for nearly 100 million people. The task is awesome, but the rewards can be very significant.