



CHARTERED ACCOUNTANTS  
AUSTRALIA + NEW ZEALAND

5 February 2015

Manager  
Financial System Assessment Unit  
Financial System and Services Division  
The Treasury  
Langton Crescent  
PARKES  
ACT 2600

Via email: [CSEF@treasury.gov.au](mailto:CSEF@treasury.gov.au)

Dear Sir/Madam,

### **Crowd-sourced Equity Funding Discussion Paper**

Chartered Accountants Australia and New Zealand welcomes the opportunity to provide a submission to Treasury on the Crowd-sourced Equity Funding (CSEF) Discussion Paper (Discussion Paper). Our key points are below and Appendix A provides our detailed submission including responses to the questions. Appendix B includes more information about Chartered Accountants Australia and New Zealand.

#### **Key points**

- We support the introduction of CSEF regulatory structure as a means of increasing Australia's competitiveness and providing an environment where new companies can grow and stay in Australia. It is important that such reforms are implemented quickly as Australia is already significantly behind other similar nations, including New Zealand.
- We consider education of investors to be critical to the success of the CSEF regime. They need to be provided with adequate information to understand CSEF and the risks attached to that form of investment.
- Overall we support the introduction of the CAMAC model. However, we do not support the creation of a new category of exempt public company. We consider that CSEF issuers can be incorporated within the existing regulatory and reporting frameworks. We also recommend changes be made to the investor limits suggested by CAMAC.

Chartered Accountants Australia and New Zealand

33 Erskine Street, Sydney NSW 2000,  
GPO Box 9985, Sydney NSW 2001, Australia  
T +61 2 9290 1344 F +61 2 9262 4841

[charteredaccountantsanz.com](http://charteredaccountantsanz.com)

Should you have any queries concerning the matters discussed above or wish to discuss them in further detail, please contact me via email at: [rob.ward@charteredaccountantsanz.com](mailto:rob.ward@charteredaccountantsanz.com); or telephone (612) 9290 5623 or Karen McWilliams via email at [karen.mcwilliams@charteredaccountantsanz.com](mailto:karen.mcwilliams@charteredaccountantsanz.com) or phone (612) 8078 5451.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Rob Ward', written in a cursive style.

**Rob Ward AM FCA**  
**Head of Leadership and Advocacy**

## **Appendix A**

### **General comments**

- We support the introduction of CSEF regulatory structure as a means of increasing Australia's competitiveness and providing an environment where new companies can grow and stay in Australia. It is important that such reforms are implemented quickly as Australia is already significantly behind other similar nations, including New Zealand.
- We consider education of investors to be critical to the success of the CSEF regime. They need to be provided with adequate information to understand CSEF and the risks attached to that form of investment.
- Overall we support the introduction of the CAMAC model. However, we do not support the creation of a new category of exempt public company. We consider that CSEF issuers can be incorporated within the existing regulatory and reporting frameworks. We also recommend changes be made to the investor limits suggested by CAMAC.
- We recommend that when the approach is finalised, that existing legislation is reviewed to ensure CSEF legislation will not have unintended consequences or be adversely impacted by other existing legislation.

### **Responses to questions**

**1. Is the main barrier to the use of CSEF in Australia a lack of a CSEF regulatory structure, or are there other barriers, such as a lack of sustainable investor demand?**

We consider that the lack of a CSEF regulatory structure in Australia is certainly a major barrier to its use. We support the view that CAMAC formed, which is that a regulatory regime for CSEF be developed.

**2. Do the existing mechanisms of the managed investment scheme regime and the small scale personal offer exemption sufficiently facilitate online offers of equity in small companies?**

No, this was considered as part of the CAMAC report.

**3. Other than the restrictions identified above in relation to limitations on proprietary companies, public company compliance requirements and disclosure, are there any other barriers to the use of CSEF in Australia?**

No specific comment.

**4. Should any CSEF regime focus on the financing needs of small businesses and start-ups only, or is there a broader fundraising role?**

We consider the focus of the CSEF regime should be on small businesses and start-ups who have difficulty raising capital through the existing regulatory structure. However, we see no need to restrict access to the regime to only these types of entities, but would not expect it to be made available to those who have already undertaken significant public fundraising through other means, such as 'disclosing entities' as defined in the Corporations Act.

**5. Do you consider that, compared to existing public company compliance costs, the exempt public company structure is necessary to facilitate CSEF in Australia?**

We do not support the introduction of a new form of entity in Australia. This would add unnecessary complexity. We consider that the existing regulatory and reporting frameworks can be amended to facilitate CSEF in Australia.

- Firstly, we suggest that CSEF is included as a further exemption to the requirement to produce a prospectus, as is the case for small-scale personal offers and professional, sophisticated or experienced investors. This would include the \$2m in a 12 month period restriction and refer to the need to provide a simplified disclosure statement in place of the prospectus.
- Secondly, S111 of the Corporations Act be reviewed to accommodate the needs of CSEF issuers such that they would be classified as non-disclosing entities. The key areas we consider require attention would be:
  - S111AF to determine whether or not the disclosure statement does or does not meet the definition of a prospectus within the Act.
  - S111AF(1)(d) and S111AG(1)(c),(2)(d) to determine how the number of shareholders for the purposes of determining a disclosing entity should be adapted, if necessary, to deal with the 'crowd' from a CSEF issue.

These amendments would enable most CSEF issuers to be classified as public companies that are non-disclosing entities. As a non-disclosing entity, the issuer would be exempt from continuous disclosure, interim reporting and remuneration disclosures. The remaining Corporations Act requirements for public companies around the audit of financial statements and holding an AGM would be considered reasonable given the number of shareholders involved. An AGM is also important to give CSEF investors a voice.

If the CSEF issuer is a non-disclosing entity and their shares are not traded in a public market, they may also be able to apply Tier 2 reporting requirements in preparing general purpose financial statements. This would enable the issuer to prepare less complex financial statements than entities that have 'public accountability' as defined in accounting standards. We consider that CSEF investors would most likely be reliant on general purpose financial statements for information that will be useful to them for making and evaluating decisions about the allocation of resources, so we consider general purpose Tier 2 reporting requirements to be the minimum level appropriate in any CSEF regime.

We suggest that consideration be given to facilitating some of these amendments via a class order exemption where possible to enable the CSEF regime to be amended easily in the future once it has become more established.

We note that CAMAC's model proposes giving additional exemptions from the requirements of a public company compared to our proposal above. We consider it important to strike an appropriate balance between investor protection and compliance requirements. CAMAC's model provides exemptions from the requirement for financial statements to be audited and holding an AGM in particular. We consider these important processes to protect retail investors and provide them with the ability to communicate with the issuer. However, we note that to balance their proposed exemptions, CAMAC recommended very low investment limits for investors. As our response to question 10 explains, we would support higher investment limits for investors as these may be needed to help start the CSEF market. However these should be appropriately balanced with the slightly higher compliance requirements noted here.

**6. To what extent would the requirement for CSEF issuers to be a public company, including an exempt public company, and the associated compliance costs limit the attractiveness of CSEF for small businesses and start-ups?**

We do not have access to information to determine the extent to which becoming a public company would limit the attractiveness of CSEF for small businesses and start-ups. However, we note that if they do not wish to become a public company, there are other options open to them such as the small scale personal offers.

Further, small-cap junior mining and exploration companies in Australia share some of the cash-flow characteristics associated with CSEF start-ups but are often structured as listed public companies. So although small with simple structures and operations, they are subject to disclosing entity compliance requirements. If the CSEF regime was structured such that issuers were classified as non-disclosing entities, the compliance burden would be less.

Public company financial reporting and auditing requirements would also enable businesses to develop good financial processes and controls as well as its financial history, which would be invaluable for future funding requirements such as IPO or venture capital.

**7. Compared to the status quo, are there risks that companies will use the exempt public company structure for regulatory arbitrage, and do these risks outweigh the benefits of the structure in facilitating CSEF?**

As noted above, we do not support the introduction of the exempt public company structure. By adapting the existing framework, CSEF issuers should be able to be accommodated with limited risk of companies structuring to avoid unfavourable regulatory outcomes.

Further, we note CAMAC's report included important checks in relation to phoenix companies and recommend these are adopted.

**8. Do you consider that the proposed caps and thresholds related to issuers are set at an appropriate level? Should any of the caps be aligned to be consistent with each other, and if so, which ones and at what level?**

Both models propose a maximum of \$2m to be raised in a 12 month period. We consider this a reasonable level and it is supported by the detailed CAMAC review. We recommend specific advice be given regarding what 12 month period is referred to, ie this calendar year, financial year or a rolling 12 month period. We note CAMAC's report refers to 'any 12 month period'.

As noted above, we do not support the adoption of a new exempt public company status and have not therefore commented on the related caps proposed for this model.

We do not consider it necessary to restrict CSEF eligibility to only certain companies with simple structure and cap of \$10m capital. The \$10m cap appears to be an arbitrary figure and is not linked to existing frameworks. We recommend that the existing framework and the key considerations noted in our response to question 6 above be used to restrict eligibility to only non-disclosing entities, ie once the issuer becomes a disclosing entity or if the proposed issue would make them a disclosing entity, they cannot use CSEF.

**9. Do CAMAC's recommendations in relation to intermediary remuneration and investing in issuers present a significant barrier to intermediaries entering the CSEF market, or to companies seeking to raise relatively small amounts of funds using CSEF?**

We note that an appropriate balance needs to be struck between ensuring the commercial viability of the intermediaries and protection of investors from conflicts of interest. We support the requirements in the CAMAC model around intermediaries as we consider they represent an appropriate level of independence for the intermediary.

If intermediaries were to be permitted to invest in the issuer, this would need to be clearly disclosed to prospective investors. Further, conditions would need to be in place to ensure all issuers offered by the intermediary have equal representation to prospective investors to avoid any potential bias. However, we do not see a situation where intermediaries lending to investors or providing financial advice could be deemed appropriate.

**10. Do the proposed investor caps adequately balance protecting investors and limiting investor choice, including maintaining investor confidence in CSEF and therefore its sustainability as a fundraising model?**

We support the inclusion of investor caps. However we note that a \$2m issue and an investor cap of \$2,500 per issuer would result in a minimum of 800 shareholders. This would seem a very large 'crowd'. We consider the choice of any cap to be relatively arbitrary but recommend further information is sought around existing CSEF experience, both overseas such as New Zealand and via the wholesale market in Australia.

We recommend consideration be given to a dual cap, where the lower value would apply. One cap would represent a percentage of the equity sought, this would provide the minimum 'crowd' permitted. The second would be an absolute limit on the funds invested for an individual retail investor in a specific equity issue. For example, the cap could be the lower of 20% of funds to be raised (so a minimum 'crowd' of 5) or \$20,000. Therefore, if the issue was \$50,000 in total, the 20% would apply limiting investments to \$10,000 per retail investor. If the issue was \$500,000, the \$20,000 cap would apply.

We note that the restrictions of CSEF investment per investor in a 12 month period could not be policed without a significant administrative burden on issuers, investors and intermediaries. CAMAC acknowledged this and proposed a self-certification requirement. However, we consider that the inclusion of statements within the risk acknowledgment that are signed by the investor would be more appropriate. For example, these might include, in addition to the suggestions within the CAMAC report:

- Acknowledgement of the higher level of risk associated with CSEF investments, the likely failure of start-up companies, that the value can go up and down and CSEF investment are relatively illiquid, making disposal of the investment potentially a difficult process.
- That the recommended annual level of investment in CSEF issues is \$x and that financial advice has been sought if needed for investments in excess of these levels
- That the value of the CSEF investment has been considered with reference to their total CSEF investment and their whole investment portfolio and they consider it appropriately balanced.

We support the proposal by CAMAC that each statement be signed off individually by the investor, rather than as a whole to ensure appropriate consideration is given to each one.

**11. Are there any other elements of CAMAC's proposed model that result in an imbalance between facilitating the use of CSEF by issuers and maintaining an appropriate level of investor protection, or any other elements that should be included?**

The CAMAC model proposes a single category of ordinary shares. There is a risk that investors could misunderstand whether the equity they are purchasing has voting rights or not. It is therefore very important that there is clarity in the disclosure from the issuer around which existing and new share classes have voting rights.

**12. Do you consider it is important that the Australian and New Zealand CSEF models are aligned? If so, is it necessary for this to be achieved through the implementation of similar CSEF frameworks, or would it be more appropriate for CSEF to be considered under the Trans-Tasman mutual recognition framework?**

We consider alignment of the CSEF models is important as part of the single economic market and to ensure issuers do not see one country as preferential over the other. However, alignment does not mean they need to be identical. Further, as the regulatory and reporting structures differ between Australia and New Zealand, it would not be possible to use the same model.

Both models propose the limit of \$2m in 12 months. Further, our proposal to incorporate CSEF into the existing regulatory and reporting structure as a non-disclosing public company would result in similar financial reporting and auditing requirements for CSEF issuers in both jurisdictions. We consider this to represent an appropriate level of alignment.

**13. Do you consider that voluntary investor caps and requiring increased disclosure where investors contribute larger amounts of funds appropriately balances investor protection against investor choice and flexibility for issuers?**

Whilst this model has been adopted by New Zealand, we did not support this option during the consultation process there. We understand this was implemented as there were concerns that due to the small market, imposing caps might restrict some private individuals from investing larger sums and to stimulate the CSEF demand, these larger investments would be needed initially.

Australia has a larger market for CSEF and therefore we do not consider the same issues to exist. Further, we recommend a larger, dual cap for retail investors is implemented than that proposed by CAMAC.

**14. What level of direction should there be on the amount of disclosure required for different voluntary investor caps?**

As noted, we do not support voluntary investor caps. However, if they are implemented, we recommend that the amount of disclosure should be appropriate for the level of the investor cap. Where possible, these should be linked to existing frameworks or tiers. There should be clear direction on the amount of disclosure to avoid companies using any ambiguity to avoid disclosure.

**15 How likely is it that the obstacles to CSEF that exist under the status quo would drive potential issuers, intermediaries and investors to move to jurisdictions that have implemented CSEF regimes?**

A recent example of an issuer moving to New Zealand was cited in the press, therefore, it seems likely that this could continue to occur.

**16 What are the costs and benefits of each of the three options discussed in this consultation paper?**

The majority of the costs and benefits have been discussed in the paper and through the questions. CAMAC undertook an extensive review of the existing regime and CSEF structures in other jurisdictions to come up with their proposed structure. An appropriate balance needs to be struck between alignment with New Zealand, improvements to their model where appropriate and adaptation for the Australian environment.

**17 Are the estimated compliance costs for the CAMAC and New Zealand models presented in the appendix accurate?**

No specific comment.

**18 How many issuers, intermediaries and investors would be the expected take up online equity fundraising in Australia under the status quo, the CAMAC model and the New Zealand model?**

No specific comment.

**19 Are there particular elements of the New Zealand model that should be incorporated into the CAMAC model, or vice versa?**

We note that the New Zealand model has only been in place for 7 months and globally CSEF is still in its infancy. Our proposed amendments to the CAMAC model are included in our responses to the earlier questions. The New Zealand model cannot be directly adopted in Australia, due to the different reporting and regulatory structure.

We recommend that regardless of the model adopted in Australia, a review is recommended after 2 years to identify any changes that might be needed to ensure appropriate balance between protecting investors and enabling issuers is maintained.

**20 Are there particular elements of models implemented in other jurisdictions that would be desirable to incorporate into any final CSEF framework?**

No specific comment.

**21 Do the issues outlined in this consultation paper also apply to crowd-sourced debt funding? Is there value in extending a CSEF regime to debt products?**

The issue of debt has different risks attached compared to the issue of equity and would need to be considered in that light. In New Zealand, this is known as peer-to-peer lending and whilst it has a similar model to CSEF, it is a separate scheme. There is a similar licensing process in place but the operational infrastructure of the intermediary must be different – its systems and processes must be tailored to the specific risk profile.

We note that the interested parties for peer to peer lending may not be engaged in this consultation as it is focused on equity funding. Further CAMAC did not consider debt funding as part of their review, noting:

*Debt securities involve different investor expectations and have some important differences in regulatory arrangements, which would add further layers of complexity in the Australian context.*

We therefore recommend that this be considered as part of the post implementation review for a CSEF regime and as a separate discussion paper.

**22 To what extent would the frameworks for equity proposed in this discussion paper be consistent with debt products?**

No specific comment.

**23 Would any of the options discussed in this paper, or any other issues, impede the development of a secondary market for CSEF securities?**

If the equity issued under CSEF was actively traded, then the issuer would not be able to use the Tier 2 reporting requirements noted in our response to question 5. Additionally, the legislation would need to be reviewed and consideration given as to whether trading on a secondary market would make the issuer a disclosing entity.

## ***Appendix B***

### ***Chartered Accountants Australia and New Zealand***

Chartered Accountants Australia and New Zealand is made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over.

Members of Chartered Accountants Australia and New Zealand are known for professional integrity, principled judgement and financial discipline, and a forward-looking approach to business.

We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are members of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.