

HENRY DAVIS YORK

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Financial System and Services Division
The Treasury
Langton Crescent
PARKES ACT 2600
ATTENTION General Manager

Dear Treasury

Consultation Paper: Facilitating crowd-sourced equity funding and reducing compliance costs for small businesses

Henry Davis York is grateful for the opportunity to comment on the Treasury Consultation Paper *Facilitating crowd-sourced equity funding and reducing compliance costs for small businesses*. Our submission is set out in the attachment to this letter.

We would be happy to elaborate on our comments and provide Treasury with any further assistance on this subject.

Yours faithfully
Henry Davis York



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Consultation Paper: Facilitating crowd-sourced equity funding and reducing compliance costs for small businesses

Submission

1 Background

- 1.1 On 4 August 2015, Treasury released its consultation paper outlining the Federal Government's proposed crowd-sourced equity funding (CSEF) framework.
- 1.2 Treasury's consultation paper reflects the commitment to CSEF made in the 2015-16 Federal budget. As part of the *Growing Jobs and Small Business* package, the Government confirmed its intention to introduce a legislative framework to facilitate CSEF. This follows on from developments in relation to CSEF which have been gathering momentum over the past year. Different CSEF framework options have been explored in the Corporations and Markets Advisory Committee's report (May 2014), the Financial System Inquiry (FSI) final report (November 2014) and Treasury's discussion paper (December 2014) as well as a variety of industry publications.
- 1.3 We note that regulatory impediments to the development of CSEF solutions in Australia include that proprietary companies are not permitted to have more than 50 non-employee shareholders and face prohibitions (subject to limited exceptions) on making public offers of equity. These impediments mean that proprietary companies cannot access the large numbers of investors which would typically be targeted under a CSEF offering.
- 1.4 Although operating as a public company may avoid some of these impediments, this company form may not be appropriate for small businesses who are looking to avoid the associated costs and compliance requirements such as reporting and corporate governance. In addition, while public companies can offer shares to the public (outside exemptions such as sophisticated, professional investor or small scale offers), the work involved in preparing the requisite disclosure documents for these offers can be expensive and time-consuming.

2 Submission

- 2.1 While we welcome the legislative outline proposed in Treasury's consultation paper, the draft legislation and accompanying legislative and regulatory guidance will need to acknowledge the potential complexities which issuers and intermediaries will face in navigating the framework in order to realise its full potential. In addition, we submit that the CSEF framework should be extended to include proprietary companies from the outset in order to provide maximum utility for small business.
- 2.2 On the basis of the outline framework for public companies set out in the Consultation Paper, we make the following observations and comments:
 - (a) The role of the intermediary will need to be carefully identified in the legislation so it is not exposed to unviable levels of commercial risk, including exposure to claims if investments in the underlying issuer lead to investor loss.

- (b) Intermediaries will be obliged to monitor compliance with the proposed investment caps for retail investors. It would be helpful to provide guidance in the legislation or accompanying explanatory memorandum as to the limits on this monitoring obligation.
- (c) It would be helpful for the legislation to provide clear timeframes for the obligation on issuers to ensure compliance with the public company exemption requirements, which are based around annual turnover and asset thresholds.
- (d) Guidance should be provided to assist prospective intermediaries with assessing the Australian financial services licensing implications arising from providing the service. We note that new entrants will need to assess whether to make an application or rely on exemptions from licensing. Existing operators may be able to rely on a current licence or may need to seek a variation. It may be that the Australian Securities and Investments Commission (**ASIC**) has a role in providing such guidance.
- (e) A clear exemption for intermediaries from market licensing requirements under the Corporations Act 2001 would provide clarity as to the broader licensing requirements attached to acting in this capacity.
- (f) ASIC guidance to assist issuers and intermediaries with decisions in relation to designing the tailored CSEF disclosure document and other information would be helpful. We note that issuers and intermediaries will need to consider how such disclosures may be made suitable for the digital environment but also compliant with financial services laws more generally. In addition, they will need to consider adjacent legal requirements for engaging with individual investors such as privacy laws and anti-money laundering rules.
- (g) We note that the current framework does not cater for non-voting shares. The result is that issuers may need to consider the likelihood of investor activism. The small lot allocation contemplated by a CSEF program should mitigate against large block shareholdings which could be leveraged to convene meetings and exercise control. However, unless a non-voting or economic interest only option emerges through the draft legislation, the framework appears likely to provide investors with voting rights through the issue of ordinary shares.

Please contact Jon Ireland, Partner if you wish to discuss any aspect of this submission.

Henry Davis York

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