



ALLENS ACCELERATE

CROWD-SOURCED EQUITY FUNDING – CAN YOU ACCESS IT?

In August this year, Treasury released a consultation paper seeking views on crowd-sourced equity funding (CSEF) for startups and small businesses. The paper sets out key changes for CSEF for public companies. But if you are a startup or a crowd-sourcing platform looking to engage with this source of funding, be aware that government policy has yet to fully develop regarding CSEF for private companies.

INTRODUCTION OF CSEF LEGISLATIVE FRAMEWORK

As part of the Federal Budget this year, former Treasurer Joe Hockey announced a number of measures focusing on startups and small businesses. This included introducing a legislative framework for crowd-sourced equity funding (you can read our in-depth analysis of the key budget measures in our previous [Client Update: Federal Budget 2015: Startups in the spotlight](#)).

On 4 August 2015, the Treasury released a consultation paper entitled 'Facilitating crowd-sourced equity funding and reducing compliance costs for small business'. The key focus of the paper is to announce the Commonwealth's policy framework for CSEF for public companies, which is intended to be developed into legislation and introduced into Parliament later this year. The paper also sought industry comment on a potential CSEF framework for private companies; submissions closed on 31 August 2015. Given the focus on public companies, it is unclear at this point how CSEF policies would apply to private companies once they are implemented as legislation.

BIG COMPANIES NEED NOT APPLY

For public companies, only small public companies who have not raised funds under an existing public offer arrangement will be able to use CSEF.

GROWTH TO BE ENCOURAGED

For private companies, the limit on the number of non-employee shareholders to 50 members places restrictions on the amount of funding that can be raised through CSEF (which consists of many shareholders with very small equity stakes). The paper suggests increasing this limit to 100 members for all private companies, or alternatively raising the limit just for private companies that use CSEF. However, this increase may be accompanied by a conversion period, whereby the private company must gradually convert to a public company over five years, which includes increasing disclosure requirements.

Restrictions on 'small scale offerings' could also be reduced, to allow for more investment from personal offers within a 12-month period.

FUNDRAISING CAPS PUT IN PLACE

Public companies will be limited to raising up to \$5 million through CSEF in a 12-month period, subject to the following limitation: 'Mum and Dad' investors will be limited to investing up to \$10,000 per offer in a 12-month period and \$25,000 in aggregate CSEF investment in a 12 month period.

Private companies may be limited to raising \$1 million through CSEF in a 12-month period, to reflect the more limited investor pool compared with public companies.

REDUCING COMPLIANCE COSTS AND DISCLOSURE

Public companies raising capital through CSEF will face fewer compliance costs than other public companies, such as exemptions from disclosing entity rules and the requirement to hold an annual general meeting. These exemptions will be available for up to five years, provided that the company does not exceed a \$5 million annual turnover and gross assets thresholds.

GREATER RISK AND REPORTING REQUIREMENTS

Both the issuing public companies and crowd-funding platforms will be required to provide mandatory risk warnings to investors, and investors will be required to sign a risk acknowledgement statement. Investors will also have a five-day 'cooling off period' to withdraw after accepting an offer.

For private companies, reporting requirements for small private companies using CSEF may be gradually aligned with that of large proprietary companies over five years. Private companies may also be required to convert to a public company five years after their initial CSEF capital raising or after exceeding annual turnover and gross assets of \$5 million.

THE FUTURE OF CSEF FOR PRIVATE COMPANIES

Private companies currently enjoy fewer corporate compliance obligations than their public counterparts, particularly in terms of disclosure. However, there are still many restrictions on how they can raise capital. The Treasury paper suggests a number of potential changes to facilitate how private companies can seek funding from retail investors, such as through crowd-funding platforms like VentureCrowd. While early industry reaction has welcomed the proposed measures for both public and private companies, keep in mind that there are doubts as to whether the changes go far enough to support practically a wider use of CSEF by startups.

THE NEW ZEALAND POSITION

In contrast with Australia's fledgling steps into legislating CSEF, New Zealand's *Financial Markets Conduct Act 2013* (NZ) and *Financial Markets Conduct Regulations 2014* (NZ), which contain specific provisions for CSEF, came into force on 1 December 2014.

The New Zealand regime contrasts with the current suggested Australian approach in a number of ways. Under the New Zealand regime:

- any incorporated entity (both private and public companies) may raise capital through CSEF;
- issuers are limited to raising NZ\$2 million through CSEF in any 12-month period;
- any entity that provides a 'crowd funding service', such as PledgeMe and Snowball Effect in New Zealand, must register for an ECF licence and meet certain eligibility criteria, which includes having appropriate policies for managing the risk of fraud, and fair dealing and adequate disclosure arrangements;
- disclosure obligations fall on the service provider of the CSEF platform, which includes making a statutory warning statement available, and the service provider must obtain written confirmation from each investor that the investor understands the risks involved; and
- caps on investors are recommendations only, and investors may exceed the caps, unless an investment limit is imposed by the issuer of the CSEF.

As Communications Minister, Prime Minister Malcolm Turnbull expressed his approval of the New Zealand approach, and suggested that his preferred approach would be to adopt the New Zealand regime in full. Given Mr Turnbull's recent ascension, we may see conformity with the New Zealand legislation take more prominence as part of the discussion around CSEF in Australia.

We will be keeping a close eye on any potential legislation released regarding CSEF. Stay tuned for future updates in this area by the Allens Accelerate team.

Visit our [Allens Accelerate](#) page to find out more about our practice for startups and emerging companies.

MEET THE TEAM

If you would like to learn more about crowd-sourced equity funding issues facing startups, get in touch with our team.

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ALLENS ACCELERATE

Allens Accelerate is a practice committed to working with startups and emerging companies to help them get on their way. Contact our team for more information.



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INTRODUCING THE A-SUITE

We know that legal issues are the last thing you want to focus on at the early stages of your startup venture. That's why we've developed a set of high-quality legal solutions specific to startups – called the A-Suite – to help you get your company up and running without a significant outlay of time or money.

The A-Suite is being made available on a free and open access basis to startups.

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