Manager

Financial Innovation and Payments Unit

Financial System

The Treasury

Langton Crescent

PARKES ACT 2600

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

6 June 2017

Dear Committee,

**Re: Extending Crowd-sourced Equity Funding (CSEF) to Proprietary Companies**

My name is Georgia Parletta and I am studying Bachelor of Law and Legal Practice (Honours) at Flinders University. I am currently completing my honours dissertation on CSEF in Australia. Specifically, I have explored its facilitation under the *Corporations Act (2001)* (Cth) before the legislative amendments, the impact of the *Corporations Amendment (Crowd-Sourced Funding) Act (2017)* (Cth) (the Amended Act) and the subsequent proposals of the *Draft Corporations Amendment (Crowd-Sourced Funding For Proprietary Companies) Bill (2017)* (Cth) (the Draft Bill). I have also considered the approaches adopted in other jurisdictions, allowing me to make recommendations for a successful Australian framework. My submission is therefore based on the research I have undertaken in relation to my honours dissertation.

**1 Extension to Proprietary Companies**

Extending the Australian CSEF framework to proprietary companies is paramount to its success, as the required conversion to public company status under the current framework is overly burdensome for small companies. This is due to the associated governance and disclosure requirements, of which the temporary concessions do not provide sufficient relief. It will therefore likely deter small companies from pursuing CSEF which would prevent Australia from harnessing its true potential. In making such an extension however, a balance between issuer access to funding and investor protection must be maintained, especially as an extension to proprietary companies interferes with their longstanding closely-held nature.

**2 Tiered Approach and Relaxed Reporting Requirements**

The Draft Bill and the Amendment Act fail to accommodate the vastly different needs of CSEF companies of varying sizes. For example, larger companies will likely pursue CSEF for business growth, seeking to raise larger amounts but with the resources to absorb the compliance costs of increased reporting requirements. Smaller start-up companies however, will likely have limited resources to meet onerous reporting requirements but, initially, will not seek significant capital. The regulatory requirements imposed on issuers must therefore be proportionate to their fundraising targets, which can best be accommodated through an adaptation of the United States’ tiered approach. Imposing audit requirements on issuers that raise over $1 million is also considered disproportionate to the amount such companies are seeking to raise. This would likely deter small companies with the most to gain from CSEF. It is therefore recommended that the fundraising amount requiring auditing be increased.

Reducing the reporting obligations for smaller companies through a tiered model is appropriate, as it deceases compliance costs for issuers but does not interfere with investor protection or access to information. This is because such protection is maintained through stringent intermediary regulation. In addition, the unique investor-issuer communication portal of an intermediary platform facilitates investor-driven disclosure, allowing investors to request information that is important to their assessment of whether to pledge without the need for more traditional issuer disclosure.

**3 Restrictions on Secondary CSEF Markets**

The Draft Bill excludes shareholders that have purchased or have been transferred CSEF securities through secondary trading from the definition of CSEF shareholders, meaning they will be included under the proprietary company 50-non-employee shareholder cap. This interferes with the on-sale of CSEF securities, reducing the prospect of profiting from an investment and subsequently discouraging contributions in small companies. It also contradicts the provisions of the Amended Act, which relax the Australian Market Licencing framework to accommodate secondary CSEF markets and subsequently increase the already low liquidity of CSEF securities. The removal of this provision is therefore recommended.

**4 Two-Director Requirement for Proprietary Companies**

The two-director requirement imposed on proprietary companies engaging in CSEF is considered arbitrary and should be removed, as it is merely administrative in nature, without affording additional investor protection. There is therefore no incentive to prevent sole director companies from pursuing CSEF, which may be the format of many start-ups.

Should you have any questions about my recommendations or require any additional details about my research, please contact me via email or via telephone.

Yours faithfully,

Georgia Parletta