



6 March 2024

Miss Lynn Kelly
Commonwealth Treasury
Treasury Building
Langton Crescent
Parkes ACT 2600

Via email: [REDACTED]

Dear Miss Kelly,

Wilson Asset Management is proud of its long track record of making a difference as an advocate for retail investors.

We believe all shareholders should be treated equitably when investing in the Australian equity market.

However, *Corporations Act 2001 (Cth)* regulations regarding corporate disclosure, the issuance of new securities, and the sophisticated investor test are perpetuating the unequal treatment of retail shareholders and allowing the wealthy to profit at the expense of small investors.

I'm writing to bring these iniquities to your attention – and propose two regulatory changes that could help level the playing field between large and small investors:

1. Replace the sophisticated investor test that discriminates between investors according to their wealth with **a new test of financial literacy**.
2. Adopt changes that **allow all shareholders to participate in placement equity raisings** by ASX-listed companies, ensuring fairness to small shareholders and recognising the effectiveness of the ASX continuous disclosure rules and encourage companies to value equity from all shareholders versus unfairly excluding smaller retail shareholders.

Summary

Wilson Asset Management is an investment management company owned and operated in Australia that manages almost \$5 billion on behalf of 130,000 shareholders.

We are devoted to defending the rights of retail investors and want to highlight the unjust treatment of small shareholders in relation to equity capital raisings in listed markets, and the unsuitability in this modern era of the sophisticated investor test that categorises people by wealth.



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Specifically, we propose reform to the sophisticated investor test that uses wealth as a proxy for financial literacy and has allowed millions of Australians to inadvertently qualify for accreditation.

We propose regulators develop a financial literacy test that can accurately assess an investor's capability to understand and engage with financial opportunities, thereby protecting those truly at risk while not arbitrarily excluding others based on wealth alone.

Further, we note that restricting certain capital raisings to people that meet the sophisticated investor test has the unintended consequence of barring retail investors from accessing discounted equity capital raisings in listed markets and, in many cases, dilutes their ownership in the company.

This disadvantage is most notable when we see wholesale investors on-selling shares to retail investors. Provided the issuing company has been listed for at least three months, wholesale and sophisticated investors that participate in a capital raising may immediately on-sell those shares to retail investors on-market.

Investors who are considered "unsophisticated" are locked out of certain capital raisings but can buy these same shares on the market the very next day, usually at the detriment to them and the advantage of the so-called "sophisticated" shareholders.

This has the perverse outcome that retail investors are considered to need the protection of disclosure when they subscribe to buy shares directly from a company, but need no such protection when they buy those same shares on-market.

Instead, we propose removing the requirement for an investor to qualify as sophisticated in order to participate in capital raisings by ASX-listed companies conducted without disclosure.

Sophisticated investor rules are not equitable

The distinction between retail and wholesale investors is a part of the laws governing corporate disclosure set out in s708 of the Corporations Act and accompanying regulations and ASIC instruments.

Companies are required to issue shares under a prospectus unless the issue falls within a specific exemption. One exemption is when companies issue shares to wholesale investors – a class that includes sophisticated investors, professional investors, and financial services licensees.

Investors that are not sophisticated, professional, or licensees are defined as retail investors, and can only access certain new share issuances when a company issues a prospectus.

The underlying policy rationale is that an investor sophisticated enough to be able to assess the risks and merits of an investment does not need the protection of a disclosure document.

We understand the definition of 'sophisticated investor' is now under review by the government.

Current regulations define a sophisticated investor as having assets of \$2.5 million or annual income of \$250,000. ASIC has recommended raising these thresholds in line with inflation, potentially to as high as \$4.5 million or \$450,000.¹

In our view, the use of wealth as a crude tool to judge investment sophistication is an anachronism in modern Australia.

It is also out of date – in 2002, less than 2 per cent of the population qualified as sophisticated. Today, more than 16 per cent of the population qualifies, partly due to rising house prices.

Unequal treatment of small shareholders

The arbitrary division of investors according to their wealth is also perpetuating the unfair treatment of retail investors.

Section 708 of the Corporations Act permits companies to make share issues without disclosure if they limit access to sophisticated and other wholesale investors. The ASX allows companies to issue up to 15 per cent of new equity on a non-pro rata basis each year.

Predictably, companies have flocked to take advantage of these exemptions to avoid the enormous cost and effort of preparing a prospectus. Instead, capital raisings are commonly conducted exclusively for wholesale and sophisticated investors, locking out retail shareholders.

As capital raisings are typically conducted at a discount to prevailing market prices, retail shareholders are significantly disadvantaged when their sophisticated and wholesale counterparts get the chance to buy more shares at a price lower than the market rate.

Offering wealthier shareholders discounted shares is patently unfair.

When retail shareholders are excluded from a capital raise, their percentage of ownership in a company decreases, meaning they end up with fewer votes and are entitled to a smaller share of the company's future dividends because their stake has been diluted.

In the past 4 years, over 500 ASX-listed companies have raised over \$160 billion at significant discounts to market prices.

Reframing the sophisticated investor test to be fair to all

Wilson Asset Management is classified as a wholesale investor and thus benefits from the existing rules. In fact, we regularly participate in capital raisings on behalf of our 130,000 shareholders – accessing opportunities that most of them would not be able to seize independently.

¹ <https://treasury.gov.au/sites/default/files/2023-11/c2023-404702-asic.pdf>



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However, we do not believe that wealth is a sensible proxy for financial literacy, or that an individual that inherits money or sells a business becomes sophisticated enough to understand investment risk.

There are some simple reforms the government can make to make the playing field fair for all Australians.

Replacing the wealth requirement with a financial literacy test would allow regulators to better distinguish between investors experienced enough to understand investment risk and those who should continue to benefit from safeguards.

Screening investors by knowledge and experience would help avoid wealthy, but inexperienced, people undertaking investments without a full understanding of potential risks. And it would allow experienced investors of lesser means to participate in wholesale investment schemes.

Allowing fair access to ASX capital raisings

All investors should be allowed to access capital raisings conducted via the placement of securities by ASX-listed companies.

The argument for restricting retail shareholders' access to such capital raisings is founded on a belief that a higher standard of disclosure provides a degree of protection when assessing whether to invest.

However, the risk is limited when a company is listed on the ASX.

The Corporations Act requires listed companies to disclose material price sensitive information on a timely basis. The ASX has detailed and well-enforced rules on disclosure that require companies to immediately notify "any information ... that a reasonable person would expect to have a material effect on the price or value of the entity's securities".²

Australia's robust continuous disclosure regime is already acknowledged in s708AA of the Corporations Act which allows companies to conduct rights issues to all shareholders without having to prepare a prospectus. Rights issues are a form of capital raising in which existing shareholders are given the right, but not the obligation, to purchase additional shares from a company at a specified price. ASIC also acknowledges the efficacy of continuous disclosure in class order relief that allows companies to offer \$30,000 worth of shares per shareholder per year without disclosure.

The policy reasoning behind this is that the continuous disclosure regime ensures all relevant information is available to all investors.

² <https://www.asx.com.au/documents/rules/Chapter03.pdf>

New Zealand reforms offer a model for Australia to follow

New Zealand has long enshrined in law the right for all shareholders to participate in any offer of securities in a class already traded on the New Zealand Stock Exchange without requiring a prospectus to be issued.

The basis for that reform was NZ's strong continuous disclosure rules that mean new disclosure documents are redundant.

The same holds true in Australia – the ASX is a world-leading securities exchange with equally robust continuous disclosure obligations.

Conclusion

Wilson Asset Management believes all shareholders should be treated fairly – regardless of their wealth.

We have a long track record of standing up for the rights of small shareholders.

Favouring the affluent at the expense of everyday Australians contradicts the very principles our nation was built on.

Reforming laws governing capital raisings and refining exemptions for sophisticated investors is critically important to levelling the playing field for all Australians.

I would welcome the opportunity to meet with you to discuss these matters alongside Wilson Asset Management's Chief Financial Officer, Jesse Hamilton, and Head of Corporate Affairs and Marketing, Samantha Philp. I will ask my Executive Assistant, Helen Wood, to follow up with your office to propose a time.

In the meantime, if you have any questions, please contact any of us on (02) 9247 6755, Jesse on 0401 944 807 or Samantha on 0410 696 730.

Yours sincerely,

Geoff Wilson AO
Chairman and Chief Investment Officer
Wilson Asset Management