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Mr John Kluver  
Executive Director  
Corporations and Markets Advisory Committee  
GPO Box 3967  
SYDNEY NSW 2001

By email: [john.kluver@camac.gov.au](mailto:john.kluver@camac.gov.au)

Dear Mr Kluver,

### **Crowd sourced equity funding**

ASX is pleased to make a submission to the Committee's inquiry into crowd sourced equity funding (CSEF).

A range of studies over the years have concluded that many small and early stage start-up companies in Australia struggle to access the capital needed to enable them to develop and commercialise their ideas. This is a significant impediment to innovation industries in Australia.

Many of these companies are at a stage of development where they find it difficult to access bank financing and tap capital markets for debt and equity finance. While the venture capital sector (including angel investors) often fills this financing gap in other countries, this aspect of Australia's capital markets is less well developed.

This 'market failure' has prompted the Government to consider and implement a range of tax and other incentives to promote these industries. The results of those policy interventions have been mixed.

Encouraging new avenues for funding these innovative industries, which often have relatively modest capital needs, offers the prospect of facilitating a range of emerging technologies. If this initial funding yields positive results then the companies that gain traction in the market may also eventually graduate to public markets as their need to raise more substantial sums of capital increases.

Crowd sourced funding is still an emerging funding mechanism which, as the Committee's paper noted, has focused to date on raising small amounts of capital motivated more by philanthropic rationales than by prospective financial gains. As these funding mechanisms mature and move more into equity type investments, the role of the prospect of financial returns in driving the supply of funds from investors will increase. It is not clear how many potential issuers may be attracted to using crowd sourced finance.

The ability of CSEF to play a role in providing capital for early stage start-up companies and innovative industries in Australia will be driven by a combination of the:

- size and nature of the potential investor pool for making investments through such portals; and
- regulatory requirements for capital raising.



ASX acknowledges that the capital raising provisions of the Corporations Act were designed for more substantive capital raising activities and that the compliance costs associated with those requirements may be prohibitive for very small capital raisings through crowd funding portals. The Corporations Act provisions have a proper focus on providing an appropriate level of investor protection when issuers are seeking to raise capital given the risk associated with those investments. Striking a balance between investor protection concerns and encouraging a capital raising regime that can facilitate new, innovative funding mechanisms is an appropriate matter for the Government/ASIC to consider.

In the immediate future, developing a new self-contained statutory and compliance structure for such funding would not seem justified. However, in the longer term and as this form of capital raising becomes more widely used globally and locally, it will be important for Australia to put in place the appropriate statutory and compliance regime.

ASX also does not believe that offers under any CSEF arrangement should be restricted only to 'sophisticated' investors as this would appear to reduce the potential benefits that might be achieved by tapping non-traditional investors who may be attracted both to the types of issuers seeking to raise capital.

ASX is of the view that there is merit in considering measures that would provide relief for this type of fundraising activity – so long as such relief is effectively targeted and not allowed to undermine the broader fund raising provisions but reflects the nature of CSEF, that is, a large number of very small individual investments.

The paper notes that in other jurisdictions, where a policy decision has been made to support such targeted assistance, this has usually been accompanied by specific funding limitations to ring-fence the regulatory relief. For example, by limiting the total amount that a company could raise annually through such means.

This appears to be a sensible approach and one that could be adopted in Australia, requiring only relatively limited modifications to existing Corporations Act arrangements.

The option raised in the paper of liberalising the small scale personal offer exemption would appear to be an effective policy response. That is, increasing the number of investors may facilitate the sort of CSEF envisaged without undermining the general capital raising rules.

However, more careful consideration would need to be given to what may constitute a reasonable maximum funding limit that could be raised by an issuer under this relief. ASX notes that the existing maximum amount (\$2 million) allowed under the small scale exemption is not out of line with the approach taken in other jurisdictions that have specifically examined CSEF. That is, the US JOBS Act limits the proposed relief to an annual \$US1m and recent NZ legislation limits it to \$NZ2m.

It is also important that CSEF is subject to disclosure obligations which appropriately balance the needs of issuers and provide for informed investment decisions by investors. To help facilitate CSEF becoming a viable form of capital raising, it will be important to ensure that the disclosure obligations are no unduly burdensome and do not discourage participation from issuers.

The intermediaries that provide the platform between the issuers and the investors should be subject to an appropriate licensing arrangement to provide some minimum standard of protection to those issuers and investors participating in the marketplace. For example, it makes sense that there should also be some more generic disclosure of the risks of such funding mechanisms provided by the operator of the web portal.

The question of whether the licensing of an intermediary should be under an Australian Market Licence or an Australian Financial Services Licence, or even the creation of a new licence category (eg the US approach of a specialised licenced 'Funding Portal') is difficult to answer without knowledge of the precise nature of the services the operator is providing. The role the operators play in the intermediation of investors and issuers should determine what type of license they have and the regulatory obligations the operator should meet.

There are a number of overseas jurisdictions, where CSEF arrangements are more advanced, and where regulators are also looking closely at many of the questions raised in the CAMAC discussion paper. Australia should seek to learn from their experiences.

ASX would be happy to meet with CAMAC to discuss in more detail our perspectives on capital raising issues confronting companies in the micro-cap market segment of the market and particularly those in the early stage start-up stage and innovative industries.

If you would like to discuss our submission or arrange a meeting please contact: Gary Hobourn, Senior Economic Analyst, Regulatory and Public Policy (02 9227 0930 or [gary.hobourn@asx.com.au](mailto:gary.hobourn@asx.com.au))

Yours sincerely



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