INSTITUTE OF
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Corporations Amendment (Crowd-Sourced Funding) Regulations 2018 Funding

Introduction

The Institute of Public Accountants (IPA) welcomes the opportunity to offer our 'Corporations Amendment (Crowd-Sourced Funding) Regulations 2018' submission and looks forward to working with the Government as it sets its economic agenda.

The IPA is one of the three professional accounting bodies in Australia, representing more than 35,000 members and studentsthroughout Australia and internationally. The IPA prides itself in not only representing the interests of accountants but also small business and their advisors.

The IPA's submission has been prepared with the assistance of Deakin University through its SME Research Partnership and its dedicated IPA-Deakin SME Research Centre

We look forward to discussing further and in more detail the IPA's recommendations with the Government and Treasury. Please address all further enquires to Tony Greco or Vicki Stylianou +61 3 8665 3100

Yours sincerely

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IPA Submission

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Corporations Amendment (Crowd-sourced Funding) Regulations 2018

The IPA I spleased to provide the following submissionIPA to the proposed Corporations Amendment (Crowd-sourced Funding) Regulations 2018. The submission has been developed in conjunction with the IPA-Deakin SME Research Centre.

Support for crowdfunding law objectives

It should be noted at the outset that the IPAIPA supports alternative methods of finance for small businesses. There is a great need for small business owners, irrespective of corporate structure, to access finance more readily. Organisations such as the G20 and OECD have noted that small business owners have used traditional sources of finance such as bank loans, overdrafts, credit lines and credit cards to enable them to start up or meet cash flow and investment needs in the past. Some forms of finance, however, may not be suitable for those businesses that operate in newer and faster growing industries. There may also be circumstances where substantial funds are required for specific projects, but finance may be difficult to obtain if there is an inability for a small business owner or their advisers to provide reliable revenue and profit forecasts for potential lenders. New financing methods are required in circumstances where traditional financial institutions are unlikely to provide readily available finance to new innovative and entrepreneurial businesses. Changes to Australian laws which allow crowdfunding to be permitted for proprietary companies are timely as well as necessary to broaden the available financing options.

Comment on regulations out on exposure

The *regulations,* subject to this consultation process, contain nothing that would cause the IPAIPA to object to them in the context of proprietary companies. However, there appears to have been no attempt to address more fundamental concerns the IPAIPA has raised in previous submissions, and this remains a matter of concern.

Concerns highlighted in previous submissions

The IPAIPA has highlighted a series of concerns in previous submissions that relate to the practical implementation of crowd funding laws to which no legislative response appears to have been reflected in the proposed Corporations Amendment (Crowd-sourced Funding) Regulations 2018. The concerns included but are not limited to the following:

- *Revenue and Asset threshold as at 'test time'*: The IPAIPA remains concerned about what is meant by 'test time' and whether a proprietary company that exceeds these thresholds is able to make use of the mechanism for further crowd-sourced offerings. There is also the question in principle: *why should a threshold restriction apply to a proprietary company?* These entities are for all intents and purposes *private* unless they exceed the threshold of 50 non-employee shareholders. A threshold for a capital offering of this sort in a private or proprietary company context is questionable given that the structure itself is one that has a limited ownership as defined under law. It would appear that these provisions were incorporated in the law for proprietary companies just by transferring them across from the public company-related provisions. This should be reconsidered in a subsequent draft of the legislation, given its inconsistency with the distinction between public and proprietary companies.
- *Cap on proprietary company shareholders*: The IPAIPA maintains that there is an absence of clarity about how the new laws impact on the various aspects of the 50 non-employee shareholder cap. Further clarity is required on these issues because the existing cap of 50 non-employee shareholders will not include shareholdings that arise from a CSF offer, in which case, first time acquirers of CSF shares will not trigger the current default provisions in the law requiring a proprietary company to convert to a public company. The IPA has no issue with these amendments as they relate to initial buyers of CSF shares. However, we are concerned with the amendments as they relate to secondary buyers, who lose the CSF status and are counted among the existing shareholding that is subject to the 50 non-employee shareholders cap. Our concerns for members of the IPA and their clients continue in this area. We are aware that there are many companies who have directly or through various inter-posed entities already reached the cap of 50 members or are close to it. Consider, for example, instances where a family firm with several families and their generations of offspring are shareholders and the family firm is verging on a membership of 50 non-employee shareholders. A sudden sell-off or transfer of shares by initial purchasers to secondary buyers might result in a breach of the cap thus resulting in a mandatory conversion to a public company. This in itself might bring with it unintended and undesirable consequences for the original 'private' group of shareholders. We believe that this area of the proposed laws needs further examination and consideration, particularly where it would be plausible, for at least the first 5-year period, to consider all acquirers, including secondary acquirers, as qualifying CSF shareholders, and thus not form part of the cap.
- *Status of shares held by CFS shareholders in a liquidation or administration*: It remains unclear how these shareholders are treated in the case of administration or liquidation under law. There would be great merit in the provision of greater clarity on the matters, so those contemplating such an investment in a proprietary company are able to do so understanding the risks bundled with such an investment.

The IPA would like to see these matters addressed explicitly in some form so that those undertaking crowd-sourced fund raising are able to get clarity. If the matters referred to above

are not able to be addressed in the law, it may be appropriate for the corporate regulator to issue regulatory guidance on crowd-sourced fund raising matters in the short-to-medium term.

Public documents on the ASIC web site

Stakeholders will naturally seek advice from the corporate regulator on the way in which these kinds of offerings should be made and how the rules should apply to the entities and the intermediaries involved. Educating company directors and potential investors is an important way to begin the process of implementing the new law. Educational and guidance materials appear to be lacking on the corporate regulator's web site in relation to the area of crowd-sourced funding. This is a shortcoming, even if it is temporary, because there may be companies thinking about such an offering without access to the regulator's view on how a proprietary company should proceed with a crowd-sourced share offer.

The ASIC web site does not have documents that specifically address the proprietary company element of the crowd-sourced funding issues. Documents currently online only deal with the public company side of the equation, following the implementation of that law. The areas covered by the corporate regulator on the 'topic specific' page[1] include:

- Access to principal Act and Regulations that cover the area of crowd-sourced funding,
- Two sets of regulatory guidance dealing with the area: *Regulatory Guide 261 Crowd-Sourced funding: Guide for public companies* and *Regulatory Guide 262 Crowd-Sourced Funding for Intermediaries,*
- The consultation papers for the two final sets of regulatory guidance and a report dealing with ASIC's response to constituents are also available,
- Advice on applying to be a CSF intermediary,
- Advice on registering a company that can use the crowd funding mechanism,
- Advice on converting a company into one that can use the crowd funding mechanism, and,
- Some material on the innovation hub.

This is insufficient and somewhat outdated as far as the policy area is concerned. As no mention is made of how proprietary companies should engage in crowd-sourced funding, this could potentially lead to directors of proprietary companies (with no knowledge of the proposed changes in the policy area) to take a view that the only way to use the crowd-sourced funding mechanism is to convert the proprietary company into a public company for the purposes of this kind of unlisted entity share offering. While companies might use intermediaries such as accountants and lawyers to assist them in the process, it is still necessary to ensure that the information provided to the public is sufficiently comprehensive and able to be accessed at any time officers of a company are reflecting on whether to undertake crowd-sourced offering.

[1] http://www.asic.gov.au/regulatory-resources/financial-services/crowd-sourced-funding/

It is important that the Federal Government and the corporate regulator jointly consider the issues of the provision of clarity in relation to the proprietary companies' crowd-sourced funding regime.

Financial reporting regulation and crowd-sourced funding

It is noted that the Australian Accounting Standards Board (AASB) is currently undertaking a project dealing with reporting requirements for charities. A suggested reform in this area is proforma reporting which may have relevance to proprietary companies. Not all proprietary companies are required to prepare and have audited financial statements that are then made available on the regulator's database. It may be prudent to consider whether the model, the AASB produces for charities can be adapted for the purposes of reporting by entities that are engaged in crowd-sourced funding.

A pro forma set of financial statements or disclosures will provide a foundation set of information for those seeking to invest in a proprietary company. Proforma financial statements will need to be consistent with the recognition and measurement requirements of accounting standards already effective in Australia. It is important that the financial numbers are arrived at in accordance with the same rules so that there is a degree of comparability assured for users of that information. This is critical as users should be able to take for granted that the figures they are seeing in financial statements are calculated as required under the relevant financial reporting standards.

If you have any queries or wish to discuss our submission in greater detail then please don't hesitate to contact Tony Greco (tony.greco@publicaccountants.org.au or telephone +613 8665 3134).

Yours Sincerely,

Tony Greco

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