

Question 1 In principle, should any provision be made in the corporations' legislation to accommodate or facilitate CSEF. if so, why, if not, why?

- 1) Number of unaccredited investors for a small scale offering should increase to at least 100 as although the average investment on the ASX is \$5000 the average investment on ASSOB is \$30,000 per unaccredited investor. This makes raises from friends, family fans and followers difficult. To achieve this corporations legislation does not need to be changed. ASIC can make this change via amending the existing class order.
- 2) Pty Limited should be made more investor friendly. This is the dominant form among Angels and early stage corporate forms and complicated and restrictive shareholder agreements cost companies a lot of money.
- 3) In terms of marketing and promotion the portal should be able to display on the public facing part of the website the tiles/badges outlining the project, funding target and progress to date.

Question 2 Should any such provision:

- (i) take the form of some variation of the small scale offering exemption and/or
- (ii) confine CSEF to sophisticated, experienced and professional investors? If so, what, if any, change should be made to the test of a sophisticated investor in this context, or
- (iii) adopt some other approach (such as discussed in Section 7.3, below).

- 1) Experience worldwide in has shown that seldom more that 200 investors are involved in an Equity Crowdfunding campaign. Any more than this will be because of misrepresentation of the opportunity or an external influence like a celebrity or recognised investor. As Crowdfunding equity raises need to keep the ability to pump them up out of the equation an increase to 100 or 200 would suffice.
- 2) Experienced or knowledgeable is the right word here. Just because someone has money doesn't mean they are "sophisticated". Maybe they inherited the money or made it in one single business. Why should they not be protected also? Professional investor is OK. Crowdfunding for the rich or sophisticated and professional investors is already legal in Australia. In regard to experienced or knowledgeable the following is suggested: The 100 points system. Example follows. Why not use a self certification system where say 100points need to be reached as they do for identification in some countries for drivers licenses The latter category may possibly work on a self certified 100 points system. (just a guide not meant to be accurate they need to reach 100 points)

- * Member of Angels Group 80 points
- * Director of Public Company 40 Points
- * Member of Directors institute 80 points
- * Company Secretarial Course 40 Points
- * Corporate Governance course 40 points
- * CPA/ CA / etc 50 points

- * Have one of the following entrepreneurial qualifications 30 points
- * Has attended an incubator or accelerator intake 30 points
- * Immediate family 80 points
- * Relative 40 points
- * Have known the issuer for more than 10 years 40 points
- * Etc etc

3) Our experience has shown that in an CSEF that has run for 8 years around 61% of investors are retail and 39% are sophisticated and professional. The latter category does not generally invest on average (as opposed to a silicon valley ready raise) until friends, family, fans and followers have invested. Restricting small early stage raises to accredited investors will kill an activity that takes place every day where family members assist friends, family, fans and followers to get started in a business endeavour or grow an existing business.

4) Despite the above it is essential that any variations or adopted procedures do not entail excessive disclosure requirements and onerous costs. It is easy here to end up like the U.S. where they will have some well-written regulations but to raise under a million is cost prohibitive.

Question 3 In the CSEF context, what changes, if any, should be made, and for what reasons, to the regulation of:

- (i) proprietary companies
- (ii) public companies
- (iii) managed investment schemes. In considering (c), should the disclosure obligations of issuers to investors differ, in principle, if investors are investing directly (as equity holders in the issuer) or indirectly (through acquiring an interest in a managed investment scheme) and if so, how and why?

Answer Q3

- 1) Proprietary companies. Pty Limited should be made more investor friendly. This is the dominant form among Angels and to make it work, complicated and restrictive shareholder agreements are used which cost companies a lot of money.
- 2) Public companies up until now have been the only ones allowed to raise funds on the ASSOB platform. This has worked well but during the last few years reluctance to use this form due to the cost relative to raise size has limited our market. By the time a startup engages accountants and auditors to manage a “public” company they wont get away with under \$20k a year of additional costs.
- 3) Early stage investors like to have direct relationships. They invest in the familiar and having an intermediary entity like a MIS would demotivate many. There is a place for this if more than say 100 investors wanted to invest in a matter.

Question 4 What provision, if any, should be made for each of the following matters as they concern CSEF issuers:

- (i) **types of issuer:** should there be restrictions on the classes of issuers permitted to employ CSEF (for instance, investment companies are excluded from the CSEF

provisions of the US JOBS Act. In Italy, CSEF is confined to designated 'innovative start-ups')

ANS: Issuer needs to be an Australian Pty or Public company with one business operation. Investment companies should be excluded.

(ii) **types of permitted securities:** what classes of securities of the issuer should be able to be offered through CSEF

ANS: Ordinary Shares, Preference shares, Convertible Notes. Hybrids are too complicated for retail investors and most issuers.

(iii) **maximum funds that an issuer may raise:** should there be a ceiling, and if so what, on the funds that can be raised by each issuer in a particular period through CSEF. Should that ceiling include any funds raised under the small scale personal offers exemption

ANS: Max \$5 million from unaccredited investors. Should include small scale offerings amounts in the cap if a raise had been carried out under both small scale offering and CSEF legislation. No limit for funds from an accredited investor but the raise would be limited to the amount in the offering document. Investors don't want to be suddenly watered down like what happened to (some) of the early investors in Facebook.

(iv) **disclosure by the issuer to investors:** what disclosures should issuers have to provide to investors

ANS: Mandated warnings. Everything that is material for the investor to know.

(v) **controls on advertising by the issuer:** what controls, if any, should there be on advertising by an issuer

ANS: Small scale offering regs OK here except the portal should be able to publish on it's front page the same details that Crowdcube, Symbid etc around the world publish. Small Scale offering legislation does not allow this at present. If a viewer wants investment information they need to log in, accept the warnings to read.

(vi) **liability of issuers:** in what circumstances should the directors or controllers of the issuer have liability in relation to CSEF. What defences to liability should apply

ANS: When they misrepresent the opportunity or break the law

(vii) **ban on a secondary market:** should CSEF be limited to new issues, excluding on-selling of existing securities

ANS: Matchmaking is OK as here no market is needed and doesn't usually exist. Secondmarket.com has proved in the U.S. that Doctors and Dentists don't search around for investments in unknown unlisted companies. ASSOB has had a similar experience. As it takes 3 to 5 years to create value in these early stage companies there is limited demand for a secondary market. All that is needed is an efficient matching service.

(viii) **any other matter?**

ANS: Founders should not be able to sell more than 10 % of their holdings for a year after the raise begins.

Question 6 What provision, if any, should be made for each of the following matters as they concern CSEF intermediaries:

(i) **permitted types of intermediary** (also relevant to Question 5):

- (a) should CSEF intermediaries be required to be registered/licensed in some manner

ANS: Yes. They should be registered and certify they will follow a code of conduct. If they do not give advice they need not come under financial services regulations. ASSOB requires its Sponsors to observe the highest standards of professional conduct and ethical behaviour in all of their ASSOB-related activities.

- (b) what financial, human, technology and risk management capabilities should an intermediary have for carrying out its role

ANS: Intermediaries work with Portals. Seldom do early stage companies have the knowledge and expertise to raise funds. They need handholding. A portal needs legal competence to assess misrepresentation in marketing materials including the offer document. An intermediary needs to be computer literate, have high integrity and be financially literate.

- (c) what fair, orderly and transparent processes must the intermediary be required to have for its online platform

ANS: Depends what intermediary you mean. Our experience has been that raises with just portal assistance are difficult as the Issuer hasn't the time or knowledge to do the job properly and compliantly.

- (d) should an intermediary be required to have an internal dispute resolution and be a member of an external dispute body, such as the Financial Services Ombudsman

ANS: No. Intermediary's are just facilitators. Any Disputes will be between the Issuer and the Investor as it is their raise. The intermediary should not colour this relationship by wording content on the portal or taking actions that create a dispute. In 300 raises ASSOB has not had any disputes fulfilling a role like this that would need to go to arbitration.

(ii) **intermediary matters related to issuers:** these matters include:

- (a) what, if any, projects and/or issuers should intermediaries not permit to raise funds through CSEF

ANS: Anything illegal and inappropriate

- (b) what preliminary/ongoing due diligence checks should intermediaries be required to conduct on issuers and their management

ANS: Initial due-diligence on the entity, IP and people involved including background checks. Then once marketing materials are ready due-diligence to ensure the documentation fairly represents the offering.

- (c) what preliminary/ongoing due diligence checks should intermediaries be required to conduct on the business conducted by issuers

ANS: That it is a legal entity, has no blemishes and is in a form to issue the shares in the offering document

(d) to what extent should intermediaries be held liable for investor losses resulting from misleading statements from issuers made on their websites

ANS: No statements should be made by intermediaries. All documentation on the portal should be prepared by issuers and signed off by them. Any misleading statements are the responsibility of the issuer not the intermediary. However if the intermediary rates raisings, publishes viewpoints, embellishes text etc they should be fully liable.

(e) to what extent should intermediaries be held liable for investor losses resulting from their websites being used to defraud investors

ANS: Not at all provided they can show they carried out the required due-diligence. The relationship is consummated between an issuer and an investor by them. All representations made are by the issuer.

(f) what possible conflict of interest/self-dealing situations may arise between issuers and intermediaries (including intermediaries having a financial interest in an issuer or being remunerated according to the amount of funds raised for issuers through their funding portal), and how these situations might best be dealt with

ANS: We see already in Australia Incubators, Accelerators, Angel Investors and others in the early stage space taking percentages in companies and promoting them through the media about their investments which implies publically the company is in raise mode. It is doubtful all of these are professional or sophisticated investors. The existing small scale offering legislation does not allow pecuniary interest, nor to promote investment as it happens during a raise, so our platform is at a disadvantage here. Especially when most early stage companies always ask if they can pay their “upfront fees” in shares. Some simple rules could enable intermediaries to have a pecuniary interest in lieu of fees and no more. This ability would propel the number of companies raising capital. As there is a limited secondary market the pecuniary interest is usually lost or gains value many years down the track.

(g) what controls should be placed on issuers having access to funds raised through a CSEF portal

ANS: They should only be released once a prescribed minimum subscription is reached.

(iii) **intermediary matters related to investors:** these matters include:

(a) what, if any, screening or vetting should intermediaries conduct on investors

ANS: They meet legislated requirements and money laundering regs.

(b) what risk and other disclosures should intermediaries be required to make to investors

ANS: Those legislated like detailed in small scale offerings legislation. Disclosures however are the domain of the issuer.

(c) what measures should intermediaries be required to make to ensure that any investment limits are not breached

ANS: Should monitor every transaction to ensure limits not breached. They need to have full access or control over the share registry as issuers can see; extra parcels not realising the consequences or otherwise.

(d) what controls should be placed on intermediaries offering investment advice to investors

ANS: No advice should be given. I know of no CSEF platform worldwide that gives advice

(e) should controls be placed on intermediaries soliciting transactions on their websites

ANS: If you mean obtaining issuers no. If you mean obtaining investors then they need to be obtained by promoting the portal generally or using the issuers own words not their own.

(f) what controls should there be on intermediaries holding or managing investor funds

ANS: Funds should be in an independently managed trust account

(g) what facilities should intermediaries be required to provide to allow investors to communicate with issuers and with each other

ANS: They should not communicate via the portal. Meetings can be arranged via the portal but interactions should be kept off the portal.

(h) what disclosure should be made to investors about being able to make complaints against the intermediary, and the intermediary's liability insurance in respect of the role as an intermediary

ANS: This is not relevant unless the intermediary steps over the line and gives advice or uses words to market the offering that are not the issuers words. It is a dangerous road if portals position themselves as the principal in transactions. They would need an AFSL if they wanted to do this and then it is not CSEF. The crowd need to deal directly with the issuer to be CSEF.

(i) what disclosure should be made about the commission and other fees that intermediaries may collect from funds raised

ANS: Should be fully disclosed and transparent

(j) what, if any, additional services should intermediaries provide to enhance investor protection

ANS: Need to have control or full informational access to the share registry to ensure every investor gets their share certificate.

(iv) **any other matter?**

ANS: No

Question 7 In the CSEF context, what provision, if any, should be made for investors to be made aware of:

- (i) the differences between share and debt securities
- (ii) the difference between legal and beneficial interests in shares
- (iii) any classes of shares in the issuer and its implications for investors. A related question is whether disclosure, alone, would suffice.

ANS: Debt securities have their own area in Crowdfunding. The Australian platform SocietyOne.com.au does this well and it has nothing to do with shares. They are totally different areas under different legislation.

Question 8 What provision, if any, should be made for each of the following matters as they concern CSEF investors:

(i) **permitted types of investor:** should there be any limitations on who may be a CSEF investor

ANS: No other than max 200 retail investors. Retail, Family, Experienced, Professional, Sophisticated and Overseas are the categories that should be available.

(ii) **threshold sophisticated investor involvement (Italy only):** should there be a requirement that sophisticated investors hold at least a certain threshold interest in an enterprise before it can make CSEF offers to other investors

ANS: No. It seldom happens this way. After experiencing 300 raises on ASSOB's CSEF platform very few are attractive to accredited investors as first investors. The accredited investors usually wait until friends, fans, family and followers have invested.

(iii) **maximum funds that each investor can contribute:** should there be some form of cap on the funds that an investor can invest. In this context, there are a number of possible approaches under *Issuer linked caps* and under *Investor linked caps*

ANS: We have never found this to be an issue. I know the Americans are going down this path but it is a nightmare to manage and in the end will be self certification as getting certificates from Accountants etc is just too cumbersome and costly for the investor and the issuer. If the authorities are honestly concerned about citizens overcommitting themselves then ensuring to gamble you needed a card which monitored daily and annual limits would be a good start. If it is OK for gambling and not in an area that is creating the jobs

(iv) **risk acknowledgement by the investor:** should an investor be required to acknowledge the risks involved in CSEF

ANS: Absolutely. They should sign that they are fully aware that there is a high chance they will lose all their money and that statistically they will lose their money and they accept this.

(v) **cooling off rights:** should an investor have some right of withdrawal after accepting a CSEF offer

ANS: 10 day cooling off period

(vi) **subsequent withdrawal rights (Italy only):** should an investor have some further withdrawal right subsequent to the offer

ANS: No unless the offer terms are discovered to be wrong and they invested on the wrong basis.

(vii) **resale restrictions:** should there be restrictions for some period on the on-sale of securities acquired through CSEF

ANS: No

(ix) **reporting:** what ongoing reporting should be made by the intermediary and/or issuers to investors in regards to their investment

ANS: Intermediaries don't report. Issuers do. Issuers should give 3 monthly updates (every 3 months) on how they are spending their money.

- (x) **losses:** what recourse should investors have in relation to losses resulting from inadequate disclosure

ANS: Full recourse if the inadequate disclosure was material

- (xi) **remedies:** what remedies should investor have in relation to losses results from poor management of the enterprise they invest in

ANS: None.

- (xii) **any other matter?**

ANS: No

Question 9 Should any accommodation for CSEF in the Corporations Act be in the form of incremental adjustments to the existing provisions, or be in the form of a self-contained regulatory regime for CSEF?

ANS: There is no evidence anywhere worldwide that unaccredited equity Crowdfunding is any more than what happens normally that friends, fans, family and followers of businesses invest in businesses they are connected to, interested in or passionate about.

To date worldwide just on \$300 million has been raised in equity platforms. \$136 million of that by ASSOB in Australia. Crowdcube has yet to get to 20 million raised despite operating in the U.K, with a larger market, relaxed rules and press coverage to die for. Developing special legislation for something that is very very small on the world stage is overkill and a reaction to international press stories and uninformed influencers.

Equity raises do not embrace instant gratification and are thus hard work as the rewards are many years down the track. Unaccredited investors don't usually invest in things their peer groups haven't. Even reward based platforms like Indiegogo say "Don't bother starting your raise if you don't know where your funders are coming from". And equity is 10 times harder than this. Creating a contained regulatory regime for CSEF may result in shiny new legislation and no raises.

Australia is the only country in the world with workable CSEF regulations in the form of small scale offering legislation for retail investors. Even Symbid and Crowdcube haven't had 8 years of experience in dealing with \$88 million raised from retail / unaccredited investors and in a much larger market they still are tracking at around on million to two million pounds a month.

At the moment, to raise \$500,000 as a small scale offering 20 parcels in 12 months would require possibly 20 retail investors at \$50,000 each. Back in 2005 \$30k was the average ASX investment. Now it is around \$6k. However ASSOB's average parcel size has hovered around \$30k since 2005 due to the 20/12 restriction.

While we have managed to facilitate around 300 businesses to raise \$135 million through CSEF with this high average parcel size the ability to accept contributions in the range of \$2k to \$6k would materially alter the ability of SME's to obtain investors. (and limit investor risk) Even with a £10 pound minimum investment Crowdcube's average parcel size in August was £3,240. Other than Seedrs and Symbid in Holland these are the only platforms worldwide transacting in the **unaccredited crowdfunding** investor space.

Crowdcube accepts investment as low as 10 pounds per investor yet in August 2013, their largest month ever the average investors per matter was just 116. Average investment was 3,240 pounds which would match for with 100 to 200 parcels of \$5000 for a \$500k to one million raise if adopted here in Australia.

The Crowd is predominantly “your crowd” in CSEF. Why re-invent the wheel. America is doing that and for SME’s they will be priced out of raises due to compliance costs. As it is it won’t work in the USA under \$1 million raises. OK they have a lot more businesses and people so it may work but Australia is different.

Question 10 What, if any, other matters which come within the scope of this review might be considered?

1) Context is important here. Early stage companies raising capital have very little money. Thus heavy hitters with AFSL’s etc will not make a living in this space. This is an area where a matchmaking platforms will operate. Any attempt to turn platforms into responsible entities etc will stop Crowdfunding in its tracks. We have already seen Seedrs.com operating Europe wide under a U.K. umbrella. Word is that Singapore wants to service Asia and Australia with Crowdfunding platforms. We live in a global world.

2) Portals are facilitators not advisors.

3) One of the biggest issues in the exempt market regime is not that investors are uneducated in making investment decisions or easily duped by marketing materials (in fact, the internet has enhanced an investors ability to make better decisions about how to invest and given them access to information about companies and officeholders (social due diligence) that they would not normally know about), but that Issuers remain ignorant of the laws around capital raising, are uninformed about the importance of corporate governance and their duties and fail to understand their own capabilities and role in the business. Too many times have we seen investors disregarded by Issuers due to lack of education of the role of director or an inability for the business to perform resulting in directors withholding important information, which runs the risk of ultimately eroding investor confidence in new business or the share market generally. Unless education is embraced as a prerequisite to CSEF, the issues we have witnessed and many more, will continue.

4) ASIC has the powers now to increase Small Scale Offerings to 100, have higher visibility and responsibility from registered platforms and enable portals to have tiles that profile raisings but require acceptance of risk warnings before proceeding to offer docs etc.