

CLEANaS Submission to the CAMAC in response to the discussion paper on Crowd Sourced Equity Funding

Thank you for the opportunity to provide input to the discussion regarding Crowd Sourced Equity Funding (CSEF). CLEANaS believes that debt or equity crowd funding, should it become available in Australia, will remove a key barrier to the growth of broad-based community owned local renewable energy schemes. CSEF schemes available in other countries, such as those facilitated by Mosaic Solar in the US (www.joinmosaic.com), have demonstrated the potential for small investors to drive the development of local renewable energy projects.

CLEANaS is the Clean Energy Association of Newcastle and Surrounds, a not-for-profit association formed in 2012 by a group of locals passionate about clean energy. CLEANaS is dedicated to driving the uptake of clean energy that our region can transition from our current dependency on fossil fuels to a more competitive and sustainable local economy. We will achieve this by working with our partners to demonstrate profitable community-led and community-owned clean energy projects; raise the profile of clean energy in the local economy through education and awareness raising; and by improving access to financing mechanisms and affordable technologies so that investment and activity grow.

Our initiatives must deliver a win-win for local community investors, local enterprise and, of course, our environment.

CLEANaS is also aware of a number of other similar community groups in NSW and throughout Australia that are also looking to establish community renewable energy projects and which face similar barriers to appropriate finance. Our discussions suggest that they share similar concerns as CLEANaS and may also benefit from the introduction of CSEF.

Community support to clean energy and environmental issues in the region is strong and there are many examples where community has come together to support these activities through donations of time and money. Local people want to see the expansion of renewable energy and reduced reliance on conventional energy services. They also want to see the local economy diversify so as to capitalise on green economic opportunities including green jobs and markets. They also want to take control of their energy costs and have access to the means of managing their energy risks.

This requires investment, and CLEANaS believes that community is ready and willing to lead the way as long as there are clear and tangible shared benefits with strong local ownership and control.

Local investors for local benefit!

Our aim is therefore to involve broad-based community investors in profitable renewable energy projects which not only deliver a return on the investment but which also provide other tangible benefits to the local community. These other benefits include, strengthening the local renewable energy industry, reducing energy costs and risks to local business and social services, providing local people with an opportunity to engage in addressing global issues.

In 2013, with the support of the NSW Office of Environment and Heritage, CLEANaS prepared its Lighthouse Community Renewable Energy (CRE) Toolkit. This is a set of technical, legal and policy tools created by CLEANaS in order to support community groups in the Newcastle and surrounding

areas to develop profitable community solar energy projects. The Toolkit includes, amongst other things, an analysis of corporate structures and financial regulations in order to determine feasible mechanisms whereby CLEANaS could facilitate small investors from the local community to invest in commercial scale solar PV projects. The findings of this study are in general agreement with the analysis provided in your discussion paper. The study identified that there is currently no cost-effective mechanism that would meet our needs, the reasons being that current regulations either restrict the number of investors (thereby not enabling broad-based ownership) or have prohibitively high compliance costs for the size of projects anticipated. Other options, such as working through existing industry managed funds, risked diluting the “local” ownership which is central to our aims and which differentiates these projects from other commercial clean energy developments.

While not in a position to provide expert commentary on many of the technical and legal questions raised within your discussion paper, CLEANaS hopes to provide the perspective of a concerned community stakeholder who sees CSEF as a mechanism to remove a key barrier to fundraising for projects which prioritise broader social and environmental benefits. Also, it is not necessarily our intention to establish a CSEF portal or other CSEF mechanism as long as an appropriate service was accessible.

These issues remain topical for CLEANaS and removing these barriers to wide scale ownership of commercial scale renewable energy is central to our mission. We welcome the questions posed in your discussion paper and provide below our response and commentary for your consideration. We remain available to support your further progress on these matters.

Best regards,

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on behalf of CLEANaS

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Responses to Questions

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

Yes. CSEF presents an opportunity to strengthening community participation in local development by enabling shared ownership, strengthening social capital, and ensuring a stronger link between investment and local priorities.

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).

CLEANaS is not in a position to provide specific guidance on how the provision is formed, however we offer the following comments on each point:

(i) The small scale offering is limited to 20 investors which is not a sufficient number to represent broad-based community participation. The alternative is to move to a public offering, however as individual projects are likely to be less than \$2million with individuals contributing relatively small amounts (less than \$2000) then this approach is not cost effective.

(iii) We advise against limiting CSEF to sophisticated, experienced or professional investors as this will exclude the potential for broad based community participation as envisaged by CLEANaS. Community investors are looking to invest smaller sums of money and may accept low rates of return and higher risk in order to generate non-financial benefits to themselves, their families and the broader community.

A local person investing in a CLEANaS project will be looking for both a financial and non-financial return on their investment. To illustrate, consider a hypothetical project where local parents are invited to invest in solar power for their kid's surf life saving club. In this case they may look to recoup their investment but will primarily be looking to see that the club has benefitted. These parents may previously have considered a small donation, whereas via CSEF they may now consider increasing their commitment. The financial return on investment is therefore NOT their primary motivation for participating although it is a motivation for them to increase the amount they would make available to the club.

(iii) No comments

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?

We have no comments on specific changes. However we would wish any changes to consider that general community owned projects will:

- *involve more than the number of investors currently permitted for proprietary companies;*
- *will not be so large as to be feasible given the compliance costs associated with public companies;*
- *risk losing the “local community” emphasis if aggregated within a managed fund;*

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’)

We have no proposals with regards to who / what should be restricted. However, from CLEANaS perspective, we see that the types of investments likely to be serviced by CSEF are diverse yet fall outside the scope of current issuers. We would therefore caution against using any overly restrictive classification, such as ‘innovative start-ups’, which may unnecessarily rule out many potential projects that are based on proven approaches (e.g. crowdsourced grant funding), but which have a new emphasis (e.g. equity finance).

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

No comments

- (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

CLEANaS projects are unlikely to be viable under a public offering or managed fund due to compliance costs and minimum size investment. Consideration of maximum fund ceiling should take into account compliance costs and minimum size of individual investments so as to ensure that overall compliance costs balance risks to investors but are not a barrier to broad-based participation of small investors.

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

CLEANA S has no specific comments, however we recognise that if issuers are engaging many smaller investors who are investing relatively small amounts, then requirements for disclosure and subsequent compliance costs should be correspondingly reduced. There should also be some recognition, in the case of community projects, that “local” linkages increase investor awareness and that the perceived benefits are not solely financial (as is generally the case for normal commercial investments).

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

No specific comments, however for community projects such as proposed by CLEANAS there is clearly a geographically and/or socially delineated cohort of prospective investors to whom we would wish to advertise, which would differentiate us from other issuers.

(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

From CLEANAS’ perspective the investments will be in specific project offerings and as such we would expect liabilities for CSEF to be similar to those of a proprietary company.

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

No comments

(viii) **any other matter?**

Question 5 In the CSEF context, what changes, if any, should be made, and for what reasons, to the current licensing requirements applicable to intermediaries?

No comments

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
- (b) what financial, human, technology and risk management capabilities should an intermediary have for carrying out its role
- (c) what fair, orderly and transparent processes must the intermediary be required to have for its online platform
- (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

CLEANA5 offers no specific comments on these matters although intermediary requirements should reflect their specific role as “facilitator” and be balance with their overall contribution to the underlying risk factors to which the investor and issuer are exposed.

(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
- (b) what preliminary/ongoing due diligence checks should intermediaries be required to conduct on issuers and their management
- (c) what preliminary/ongoing due diligence checks should intermediaries be required to conduct on the business conducted by issuers
- (d) to what extent should intermediaries be held liable for investor losses resulting from misleading statements from issuers made on their websites
- (e) to what extent should intermediaries be held liable for investor losses resulting from their websites being used to defraud investors
- (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
- (g) what controls should be placed on issuers having access to funds raised through a CSEF portal

General comment to (ii):

The good initiative should not be suffocated by over-regulating it. The liabilities should sit at the issuer, not at the intermediaries. To avoid scams the intermediaries should conduct some basic checks to ensure that the issuer and investor. Additionally the intermediaries should have some checkpoints to detect different fraudulent activities (like scam schemes, money laundering, etc.).

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

- (a) what, if any, screening or vetting should intermediaries conduct on investors
- (b) what risk and other disclosures should intermediaries be required to make to investors
- (c) what measures should intermediaries be required to make to ensure that any investment limits are not breached
- (d) what controls should be placed on intermediaries offering investment advice to investors
- (e) should controls be placed on intermediaries soliciting transactions on their websites
- (f) what controls should there be on intermediaries holding or managing investor funds

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

(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

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

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

General comment to (iii):

We believe that the intermediaries should not be seen as offering investment advice, but only as the providers of the platform. Hence the disclosure requirements should be placed on the issuers. Generally, the risks and fees should be transparent upfront.

The intermediaries should however provide the means for the investors, potential investors and issuers to discuss the projects openly.

(iv) **any other matter?**

No comments

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.

No comments.

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

CLEANA S recommends not having any restrictions on type of investor as we believe that CSEF is filling a gap in investment mechanisms which targets a specific type and size of investment which will be naturally differentiated from other types of investments (and hence investors).

(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

Instead of looking to sophisticated investors to "vett" an enterprise, CSEF should look to "crowd vetting" instead. This is a mechanism used in some current crowdsourcing schemes whereby a project is not funded unless it

reaches a critical funding pledge level, this being a proxy measure of the crowd's expectations for success of the venture.

(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*

The limit on maximum funds may be appropriate to limit the risk exposure of individual investors but should not be so much as to create unnecessary fragmentation of the equity. Also, the limit should not be so high as to reduce the potential for "crowd vetting" of investments.

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

Yes. The risks related to the platform as well as to the project should be made transparent and they should be acknowledged by the investor.

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

No comments

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

No comments

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

No comments

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

No comments

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

No comments

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

No comments

(xi) **any other matter?**

No other comments

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?

No comment

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

It should be remembered, that there are currently other ways available for funding large scale projects, but relatively small projects struggle due to the cost related to the high regulatory requirements. CSEF could be the long awaited solution for these problems, but only, if the requirements are proportional to the project size and to the risk that an individual investor takes.