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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

CORPORATIONS AMENDMENT (CROWD-SOURCED FUNDING) BILL 2016

EXPLANATORY MEMORANDUM

(Circulated by authority of the
Treasurer, the Hon Scott Morrison MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

Abbreviation	*Definition*
The Act	*Corporations Act 2001*
AML	Australian Market Licence
ASIC	Australian Securities and Investments Commission
ASIC Act	*Australian Securities and Investments Commission Act 2001*
AFSL	Australian Financial Services Licence
Bill	Corporations Amendment (Crowd-sourced Funding) Bill 2016
CAMAC	Corporations and Markets Advisory Committee
CSF	Crowd-sourced funding
CSEF	Crowd-sourced equity funding
IICA	Industry Innovation and Competitiveness Agenda
ICCPR	International Covenant on Civil and Political Rights

General outline and financial impact

Overview

Crowd-sourced funding (CSF) is an emerging form of funding that allows entrepreneurs to raise funds from a large number of investors. It has the potential to provide finance for innovative business ideas and additional investment opportunities for retail investors, while ensuring investors continue to have sufficient information to make informed investment decisions (Chapter 1).

Schedule 1 to the Corporations Amendment (Crowd-sourced Funding) Bill 2016 (the Bill) amends the *Corporations Act 2001* (the Act) to establish a regulatory framework to facilitate CSF by small, unlisted public companies. The CSF regime includes:

- eligibility requirements for a company to fundraise via CSF, including disclosure requirements for CSF offers (Chapter 2);
- obligations of a CSF intermediary in facilitating CSF offers (Chapter 3);
- the process for making CSF offers (Chapter 4);
- rules relating to defective disclosure as part of a CSF offer (Chapter 5); and
- investor protection provisions (Chapter 6).

Schedule 1 to the Bill also makes consequential amendments to the *Australian Securities and Investments Commission Act 2001* (ASIC Act) to include a crowd-funding service, as defined in the Corporations Act, in the range of financial services covered by the ASIC Act

Schedule 2 to the Bill provides new public companies that are eligible to crowd fund with temporary relief from the reporting and corporate governance requirements that would usually apply (Chapter 7). These concessions provide temporary relief to these companies to support the CSF regime by reducing the potential barriers to adopting the required public company structure.

Schedule 3 to the Bill amends the Act to provide greater flexibility in the Australian Market Licence (AML) and clearing and settlement facility licencing regimes. Under the changes, the Minister would be able to provide that certain financial market and clearing and settlement facility operators are exempt from some of the requirements in Chapter 7 of the Act. Providing for this flexibility is necessary to enable secondary trading markets for CSF securities to be licensed once the CSF regime is established. The flexibility would also facilitate the development of other emerging or specialised markets as they would be subjected to a regulatory regime tailored to best address their activities.

Date of effect: The amendments in Schedules 1 and 2 to this Bill will commence on a day to be fixed by Proclamation. If the amendments do not commence within six months from the date of Royal Assent, they will commence on the day after the end of the period of six months after Royal Assent. The amendments in Schedule 3 will commence on the day after Royal Assent.

Proposal announced: The measures were included as part of the 2015 16 Budget.

Financial impact: The measure has the following financial impact:

2015-16	***2016-17***	***2017-18***	***2018-19***
-1.2	-3.1m	-1.7m	-1.6m

The financial impact includes a movement of funds from 2015-16 to 2016-17 as part of the 2015-16 Mid-Year Economic and Fiscal Outlook.

Human rights implications: Human rights implications: This Bill raises a human rights issue. See Statement of Compatibility with Human Rights — Chapter 10, paragraphs 10.1-10.12.

Compliance cost impact: The compliance costs associated with this Bill are $50.3 million for the CSF model, and a further $0.6 million for changes to the AML regime. This has been fully offset from within the Treasury portfolio.

Summary of regulation impact statement

Regulation impact on business

Impact: This Bill will remove regulatory barriers to CSF, and will make available a new funding source for businesses. It is expected that the

overall 'per business' compliance costs for issuers that participate in crowd-sourced funding will decline. However, given the likely growth in the number of businesses raising funds through these arrangements, the aggregate compliance burden over the economy is expected to increase.

Main points:

- This measure recognises that regulatory impediments are the primary barrier to CSF in Australia. This Bill provides a model to reduce these regulatory barriers.

- Three models are discussed in the regulation impact statement — the model proposed by the Corporations and Markets Advisory Committee (CAMAC) 2013 review of crowd-funding in Australia, the model adopted in New Zealand, and a post-consultation model. These are considered against the status quo.

- The model in the Bill is the post-consultation model, which has the greatest net benefit.

- The regulation impact statement details the stages of consultation undertaken over 2014, 2015 and 2016 in considering and refining this model. This included an options paper released in December 2014, a detailed consultation paper with a proposed model released in August 2015, targeted consultation on the draft legislation in November 2015 and public consultation on draft regulations released in December 2015.

- The framework will be implemented through this Bill and associated regulations. The Government and the Australian Securities and Investments Commission (ASIC) will continue to monitor the regime to ensure the changes to the law are operating as intended.

Chapter 1
Background

Outline of chapter

1.1 This Chapter provides an overview of the Corporations Amendment (Crowd-sourced Funding) Bill 2016.

1.2 Unless otherwise stated, all references in this Chapter relate to the *Corporations Act 2001*.

Context of amendments

Policy Background

1.3 Productivity growth is a core driver of economic growth. Fostering innovation is an important way of unlocking productivity, both through innovative products and ways of doing things, and through generating knowledge spill-overs from research and development that add to the general level of knowledge in the economy.

1.4 New funding models that flexibly support emerging firms have the potential to facilitate innovation and contribute to productivity growth. A number of recent reviews have identified the potential of CSF to provide new and innovative businesses with access to the finance they need to develop their product or service and grow.

- The Government's Industry Innovation and Competitiveness Agenda, released in October 2014, called for consultation on a regulatory framework for CSF.

- The Murray Inquiry into Australia's financial system, released by the Government in December 2014, specifically recommended reducing regulatory impediments to crowdfunding by introducing graduated fundraising regulation. In its response to the Inquiry, released in October 2015, the Government accepted this recommendation.

- The Productivity Commission's Business Set-up, Transfer and Closure draft report, released in May 2015, also supported the introduction of a CSF framework.

- The Government's National Innovation and Science Agenda, released in December 2015, identified CSF as a reform that would make it easier for small businesses to raise equity funds from the public.

- The Government's FinTech Statement, released in March 2016, included CSF as a FinTech priority.

1.5 CSF is an innovative type of fundraising, typically online, that allows a large number of individual investors to make a small financial contribution towards a company.

1.6 CSF will provide an additional funding option for small businesses and start-ups in particular, that may otherwise struggle to obtain affordable finance.

- Existing legislative arrangements can be a barrier to small businesses and start-ups making securities offers:

- For proprietary companies, a limit of 50 non-employee shareholders and prohibitions on making public offers of securities mean such companies are not able to access the large number of small-scale investors that would typically be targeted under an equity CSF campaign.

- Public companies are not subject to these restrictions, but must comply with substantially higher corporate governance and reporting obligations that may be too expensive to be an option for small business. Public companies making equity or debt offers must generally also use a disclosure document, which can be costly and time consuming to prepare.

1.7 While there are currently a small number of operators of online platforms offering investment in Australian start-ups and small businesses, the current legislative arrangements outlined above significantly limit the type of service they can offer, and do not fulfil the 'crowd' element of CSF.

1.8 Facilitating CSF would also provide additional investment opportunities to retail investors, who are generally unable to gain direct access to early-stage financing activities. However, small businesses and start-ups generally present higher risks for investors compared to larger,

more established companies. CSF investments may be largely illiquid, reducing the ability of investors to exit their investment.

1.9 In order for CSF to be sustainable, any regulatory framework needs to balance reducing the current barriers to CSF with ensuring that investors continue to have an adequate level of protection from financial and other risks, including fraud, and sufficient information to allow them to make informed decisions.

1.10 The regulatory regime for operators of financial markets and clearing and settlement facilities was designed to address risks associated with the operation of traditional exchanges such as the Australian Stock Exchange or other significant financial markets and which may not be appropriate for operators of emerging and specialised markets. Amending the Australian Market Licence and clearing and settlement facility licensing frameworks to provide the Minister with the power to exempt certain market operators from some of the obligations under these regimes will ensure that the regulatory requirements can be tailored to particular markets and facilitate their development.

Summary of new law

1.11 The amendments establish a new CSF regime by:

- inserting a new Part into Chapter 6D, which deals with:
  - eligibility requirements for a company that wants to make an offer under the CSF regime;
  - the process to make a CSF offer, including the role and obligations of the CSF intermediary; and
  - the prohibitions, liabilities and investor protections applying to CSF offers, including rules relating to defective disclosure documents and advertising restrictions.

1.12 The amendments generally disapply Part 6D.2, which contains provisions relating to prospectuses and other existing disclosure documents, and Part 6D.3, which deals with prohibitions, liabilities and remedies relating to offers of securities, by stating they do not apply to CSF offers, unless expressly provided for.

1.13 Part 6D.4, which sets out ASIC's powers in relation to offers of securities, has been amended so that it applies as required to CSF offers.

1.14 The amendments set out temporary concessions from certain public company corporate governance and reporting requirements which are available to a new public company limited by shares (including a proprietary company that converts) that is eligible to make a CSF offer and satisfies certain eligibility criteria.

1.15 The exemption powers in Parts 7.2, 7.2A, 7.3 and 7.5 have been amended to provide a streamlined approach to granting some emerging or specialised financial markets and clearing and settlement facilities, and their operators, with exemptions from certain regulatory requirements.

Chapter 2
Eligibility requirements

Outline of chapter

2.1 This Chapter sets out the eligibility requirements for making a CSF offer.

2.2 Unless otherwise stated, all references in this Chapter are to the *Corporations Act 2001* and the *Corporations Regulations 2001*.

Summary of new law

2.3 The amendments establish that a CSF offer is an offer that is expressly stated to be made under the CSF regime and that is eligible to be made under the regime by meeting all of the relevant requirements.

2.4 The amendments provide that the relevant requirements for making a CSF offer are:

- the offer must be for the issue of securities of the company making the offer;
- the company making the offer must be an 'eligible CSF company' at the time of the offer;
- the securities must satisfy the eligibility conditions specified in the regulations;
- the offer must comply with the 'issuer cap'; and
- the company must not intend the funds sought under the offer to be used by the company or a related party of the company to any extent to invest in securities or interests in other entities or managed investment schemes.

2.5 The amendments also provide a regulation-making power to permit other eligibility requirements for a CSF offer to be prescribed.

Comparison of key features of new law and current law

New law	*Current law*
A CSF offer is an offer that is expressly stated to be made under the CSF regime and that is eligible to be made under the regime.	An offer requiring disclosure is an offer made under Part 6D.2 that must comply with the requirements in Parts 6D.2 and 6D.3.
An offer will be eligible to be made under the CSF regime where: • the offer is for the issue of securities of the company making the offer; • the company making the offer is an 'eligible CSF company' at the time of the offer; • the securities satisfy the eligibility conditions specified in the regulations; • the offer complies with the 'issuer cap'; and • the company does not intend the funds sought under the offer to be used by the company or a related party of the company to any extent to invest in securities or interests in other entities or managed investment schemes.	An offer requiring disclosure is an offer made under Part 6D.2 that must comply with the requirements in Parts 6D.2 and 6D.3.

Detailed explanation of new law

Establishment of a CSF regime

2.6 The amendments establish the CSF regime: a new disclosure regime that can be used by eligible CSF companies to make certain offers of securities for issue. ***[Schedule 1, Part 1, item 14, section 738A]***

2.7 The amendments provide that a company making a CSF offer is also able to offer securities of the same class pursuant to an offer that is exempt from disclosure under section 708. This allows a company to, for example, make a CSF offer of shares via an intermediary to crowd investors but also make an offer of shares to investors for whom disclosure is not required (such as venture capital funds and angel investors). ***[Schedule 1, Part 1, item 14, section 738E]***

Offers eligible to be made under the CSF regime

2.8 A CSF offer is an offer that is expressly stated to be made under the CSF regime and that is eligible to be made under the regime by meeting all of the relevant requirements. ***[Schedule 1, Part 1, item 14, section 738B]***

2.9 Part 6D.2, which contains the general rules regarding when disclosure is required for offers of securities, does not apply to CSF offers except as expressly provided for. ***[Schedule 1, Part 1, items 7, 8, 9 and 10, heading to Part 6D.2, section 703B, section 704, and section 706]***

2.10 Part 6D.3, which contains the prohibitions, liabilities and remedies that usually apply to offers of securities requiring disclosure, does not apply to CSF offers except as expressly provided for ***[Schedule 1, Part 1, items 11 and 12, heading to Part 6D.3 and section 725A].*** This is appropriate as the CSF regime establishes the prohibitions, liabilities and remedies relating to CSF offers. There is, however, an express provision that the CSF regime does not otherwise affect any liability that a person has under any other law ***[Schedule 1, Part 1, item 14, section 738ZH]***.

Eligibility requirements for a CSF offer

2.11 The relevant eligibility requirements for a CSF offer are set out in detail below.

Offer of securities for issue

2.12 The first criterion is that the offer must be for the issue, not the sale, of securities; that is, a CSF offer can only cover primary issuances. ***[Schedule 1, Part 1, item 14, paragraph 738G(1)(a)]***

Eligible CSF company

2.13 The second criterion is that the company making the offer must satisfy the definition of an 'eligible CSF company'. ***[Schedule 1, Part 1, item 14, paragraph 738G(1)(b)]***.

2.14 A company will be an eligible CSF company where it satisfies the following conditions:

- the company is a public company limited by shares, with its principal place of business and majority of directors in Australia ***[Schedule 1, Part 1, item 14, paragraphs 738H(1)(a), (b) and (c)]***;

- the company satisfies the gross assets and turnover caps ***[Schedule 1, Part 1, item 14, paragraph 738H(1)(d)]***;

- neither the company, nor any related party, is a listed corporation ***[Schedule 1, Part 1, item 14, paragraph 738H(1)(e)]***; and

- neither the company, nor any related party, has a substantial purpose of investing in securities or interests in other entities or managed investment schemes ***[Schedule 1, Part 1, item 14, paragraph 738H(1)(f)]***.

Public company limited by shares

2.15 A public company limited by shares includes:

- a public company with share capital registered under Chapter 2A (including a proprietary company that converts to become a public company limited by shares); and

- a body corporate that is registered as a public company under Part 5B.1 of the Act.

2.16 A body corporate that is registered as a public company under Part 5B.1 can include an incorporated foreign company. Such a company has, in effect, transferred its incorporation so that it can now effectively be regarded as a public company registered under the Act.

2.17 The following entities are ineligible to access the CSF regime as they will not satisfy the definition of public company limited by shares:

- proprietary companies, as they are explicitly excluded from the definition of 'public company' in section 9;

- foreign companies and registrable Australian bodies that are registered under Part 5B.2, as they will not meet the definition of a 'company' under section 9; and

- public companies that do not have share capital (for example, public companies limited by guarantee).

Principal place of business and majority of directors located in Australia

2.18 Given one of the policy objectives underpinning the CSF regime is to support Australian businesses' access to capital, one of the eligibility requirements is that a company seeking to access the CSF regime must have a principal place of business in Australia at the time it is determining its eligibility to crowd fund.

2.19 For similar reasons, another eligibility requirement is that the company must have a majority of directors (not counting alternative directors) that ordinarily reside in Australia.

Complies with consolidated gross assets and turnover caps

2.20 As the CSF regime is intended to assist small-scale businesses, there are restrictions on the size of companies that can access the regime.

2.21 Firstly, the value of the consolidated gross assets of the issuer and any related parties must be less than $25 million at the time the company is determining its eligibility to crowd fund ('gross assets test'). ***[Schedule 1, Part 1, item 14, paragraph 738H(2)(a)]***

2.22 The gross assets cap is based on the value of consolidated gross assets of an issuer and any related parties for integrity reasons to ensure that the cap applies appropriately to related parties of the same group.

2.23 The meaning of 'related party' for the CSF rules is set out in paragraphs 2.45 to 2.49.

2.24 As well as satisfying the assets test, the company and any related parties must also have consolidated annual revenue of less than $25 million ('turnover test'). ***[Schedule 1, Part 1, item 14, paragraph 738H(2)(b)]***

2.25 The turnover cap is based on the consolidated annual revenue for the 12-month period immediately prior to the time when determining eligibility to crowd fund. New companies that have not been operating for a full 12 months will still be able to crowd fund as long as their consolidated annual review for the period is under the $25 million cap.

Not a listed corporation

2.26 In order to be eligible for the CSF regime, neither the company, nor any related parties, can be a listed corporation ***[Schedule 1, Part 1, item 14, paragraph 738H(1)(e)]***. A listed corporation is 'a body corporate that is included in an official list of a prescribed financial market' (section 9). Regulation 1.0.02A lists the following as prescribed financial markets: the Asia Pacific Exchange Limited; ASX Limited; Chi-X Australia Pty Ltd; National Stock Exchange of Australia Limited; and SIM Venture Securities Exchange Limited.

2.27 The rationale for excluding listed corporations is that a company that is listed has demonstrated an ability to bear the costs and compliance requirements associated with listing on a public market. These companies generally have access to other forms of equity raisings because of their listed and continuously disclosing status, such as rights issues and share purchase plans.

2.28 An unlisted company that previously made an offer requiring disclosure under Chapter 6D.2 is not excluded from making a CSF offer. Allowing such companies to access the CSF regime will potentially reduce the fundraising costs of these businesses and provide an alternative to making a traditional offer requiring disclosure.

Not an investment company

2.29 Neither the company, nor its related parties, can have a substantial purpose of investing in securities or interests in other entities or managed investment schemes. ***[Schedule 1, Part 1, item 14, paragraph 738H(1)(f)]***

2.30 It would be inappropriate for an investment company, which will itself be investing in other unspecified entities, to undertake such activities in the lower disclosure environment provided by the CSF regime.

Securities prescribed in the regulations

2.31 The securities that are the subject of the CSF offer must be securities of a class prescribed in the regulations. ***[Schedule 1, Part 1, item 14, paragraph 738G(1)(c)]***

2.32 The Government has indicated that only fully-paid ordinary shares would be subject to crowd-funding when the regime commences. This will ensure that there are appropriate limits on the securities made available under crowd-funding as the regime commences and begins to develop. As the CSF regime is new and is expected to evolve quickly, there is a need to have the flexibility to quickly adjust the type of securities that are eligible for crowd-funding.

2.33 As crowd-funding is a new market in Australia, it is important that any changes can be implemented quickly and in response to the way the market is developing as this would ensure the market is given the best chance for success.

2.34 An important aspect of the CSF regime is to ensure investors have appropriate protections when participating in crowd-funding. Prescribing the securities eligible for crowd-funding is an important aspect of the CSF regulatory regime. It ensures the Government can

quickly amend the types of securities available on crowd-funding platforms to prevent a systemic issue from arising and maintain investor confidence.

Offer complies with issuer cap

2.35 Consistent with the policy intent that the CSF regime be used to assist start-ups and innovative small businesses to access capital, and recognising that a CSF offer does not require the same level of disclosure as existing Chapter 6D disclosure documents, there is a cap on the maximum amount of funds that an issuer company (and any related parties) can raise under the CSF regime. ***[Schedule 1, Part 1, item 14, paragraph 738G(1)(d)]***

2.36 The amendments set the 'issuer cap' at $5 million in any 12-month period with a regulation-making power to adjust the cap in the future in light of the experience with CSF. ***[Schedule 1, Part 1, item 14, subsection 738G(2)]***

2.37 A company seeking to make a CSF offer must satisfy the issuer cap, which is calculated by taking into account:

- the maximum subscription amount sought by the company under the current CSF offer;
- all amounts raised from any other CSF offers made within the past 12 months by the company or its related parties; and
- all amounts raised within the past 12 months from small scale personal offers (subsection 708(1)) and certain offers made via an Australian Financial Services Licence (AFSL) holder (subsection 708(10)) by the company or its related parties.

2.38 The table below summarises which offers count towards the issuer cap.

Table 2.1: Which offers count towards issuer cap

Timing condition	***How raised***	***By issuer***	***By related party***
	Funds sought under current CSF offer	Yes	N/A, as a company and its related parties cannot have more than one CSF offer open at a time
Only if CSF offer *made* within 12 months of current offer	Funds raised from other CSF offers	Yes	Yes
Only if funds *raised* within 12 months of current offer	Funds raised from subsection 708(1) and subsection 708(10) offers.	Yes	Yes
	Funds raised from other offers that do not require disclosure, other than subsection 708(1) and subsection 708(10) offers.	No	No

2.39 The issuer cap takes into account the maximum funds *sought to be raised* under the current CSF offer as this is potentially the amount that could be raised by the issuer under the CSF offer.

Which offers within the past 12 months count towards the issuer cap

2.40 With regard to previous offers, the issuer cap disregards amounts raised from offers that are exempt from disclosure, such as offers to sophisticated investors (subsection 708(8)) or professional investors (subsection 708(11)). This reflects the policy intent that the issuer company should continue to have access to funding from wholesale investors (such as angel investors and venture capital funds).

2.41 There are two types of offers that are exempt from disclosure which *do* count towards the issuer cap. These are 708(1) offers (small scale personal offers) and subsection 708(10) offers (offers made via an Australian Financial Services licensee where the licensee is satisfied on reasonable grounds that the person to whom the offer is made

has previous experience in investing that allows them to assess the merits and risks of the current offer).

2.42 The rationale for including the amounts raised under small scale personal offers and subsection 708(10) offers in the issuer cap is that the funds raised under such offers may involve retail investors who are very similar to crowd investors. Not including amounts raised under these offers could mean an issuer company could, in effect, raise funds in excess of the issuer cap, with a lower level of disclosure from crowd investors and other retail investors, who are not sophisticated investors and would otherwise require a disclosure document under Part 6D.2.

Distinction between offers made and funds raised

2.43 In the case of previous offers, there is a difference between how amounts raised under a previous CSF offer and amounts raised under a previous subsection 708(1) or subsection 708(10) offer count towards the issuer cap. In the case of a previous CSF offer, it is necessary to look at when the offer was *made,* not when the amount raised under the offer was *received.* A CSF offer is made when the CSF offer document relating to the offer is first published on the offer platform of an intermediary ***[Schedule 1, Part 1, item 14, subsections 738L(6) and 738N(1)].***

2.44 In the case of a subsection 708(1) or subsection 708(10) offer, funds *raised* within 12 months of the current CSF offer contribute towards the issuer cap ***[Schedule 1, Part 1, item 14, paragraph 738G(2)(c)]***. Funds from non-CSF offers are included based on when the funds were raised, not when the offer was made, in recognition of the fact there may be some difficulties, in practice, with identifying when the offer was made but there would be less difficulty in identifying when funds relating to the previous offer were received by the company.

Example 2.1 Calculation of issuer cap — previous offers

NewTech Limited is intending to make a CSF offer on 14 October 2019. The minimum and maximum amounts for that offer are $1 million and $2.3 million respectively.

NewTech previously made a CSF offer on 10 August 2018, which was completed on 15 November 2018. A total of $2 million was raised under that offer.

In the period 14 October 2018 to 6 January 2019, NewTech received amounts of $1.7 million from small scale personal offers made on 23 August 2018.

In calculating the amounts that contribute towards the issuer cap, NewTech will count the maximum amount sought to be raised under the current offer, which is $2.3 million.

In relation to the previous offers, NewTech will disregard the amounts raised under the CSF offer of 10 August 2018 as that offer was made more than 12 months prior to the current CSF offer. In relation to the previous small scale offer, NewTech will include the amount of $1.7 million as this was the amount received from small scale offers in the 12 month period prior to the current CSF offer.

The total amount counting towards the issuer cap is $2.3 million + $1.7 million = $4 million. As the total does not breach the issuer cap, the current CSF offer will be an eligible CSF offer (subject to the other eligibility requirements being satisfied).

Certain offers of related parties are included in the issuer cap

2.45 The issuer cap takes into account amounts raised under certain previous offers of the company's related parties.

2.46 A related party of a company seeking to make a CSF offer is:

- a 'related body corporate' of the company; or
- an entity controlled by a person who controls the company or an associate of that person. ***[Schedule 1, Part 1, item 14, subsection 738G(3)]***

2.47 A related body corporate (defined in section 50) of an issuer company would be:

- its holding company;
- its subsidiary; or
- a subsidiary of the holding company of the body corporate (a 'sister' company).

2.48 An entity controlled by a person who controls the issuer company or an associate of that person will pick up 'sister' entities of the company that are not body corporates.

2.49 The definition of 'related party' in the CSF regime is based on the approach in subsection 709(4) which applies for companies seeking to raise funds using an offer information statement (which has a cap on total funds raised of $10 million which applies to the company, its related body corporates and entities controlled by a person who controls the company or associates of such a person).

Anti-avoidance determinations

2.50 The amendments provide ASIC with a power to make a determination that transactions, assets, or revenue of closely related bodies should be aggregated ***[Schedule 1, Part 1, items 20 and 21, paragraphs 740(1)(b) and 740(2)(d)].*** A consequence of the determination is that a company may no longer be eligible to make a CSF offer as it will exceed the issuer cap, gross assets or turnover tests.

Funds not to be used for investing in another entity or scheme

2.51 The policy intent is that the CSF regime, given it involves a lower level of disclosure to investors than other types of public offers, cannot be used to raise money for 'blind pools'.

2.52 This policy intent is achieved by excluding an offer from being a CSF offer where the funds raised are intended to be used to any extent for investing in securities or interests in other entities or schemes ***[Schedule 1, Part 1, item 14, paragraph 738G(1)(e)].*** The content requirements of the CSF offer document, which will be specified in the regulations, could require the company to include in the CSF offer document a description of how it intends to use the proceeds from the offer.

Consequences where the offer is not eligible to be a CSF offer

2.53 Where an offer does not satisfy the eligibility criteria to be a CSF offer, it will default to being an offer of securities requiring disclosure under Part 6D.2, unless one of the exemptions from disclosure in section 708 applies.

2.54 Where a person makes an offer of securities requiring disclosure under Part 6D.2 but does not lodge the required disclosure document with ASIC, the person will commit an offence under subsection 727(1), which carries a maximum penalty of 200 penalty units, five years imprisonment or both.

Consequential amendments

2.55 Consequential amendments have been made to section 9 to insert a number of new definitions for concepts relevant to the CSF regime. ***[Schedule 1, Part 1, items 1, 2, 3, 4, 5 ,6, section 9]***

2.56 A consequential amendment has been made to subsection 1311(1A) to add the new Part 6D.3A (containing the provisions relating to the CSF regime). The effect is that a person will

only commit an offence under the CSF regime where a specific penalty has been set out in Schedule 3 to the Act. ***[Schedule 1, Part 1, item 33, paragraph 1311(1A)(dba)]***

Chapter 3
The role and obligations of a CSF intermediary

Outline of chapter

3.1 This Chapter sets out the role and obligations of a CSF intermediary in facilitating a CSF offer.

3.2 Unless otherwise stated, all references in this Chapter relate to the *Corporations Act 2001* and the *Corporations Regulations 2001*.

Context of amendments

3.3 The CSF intermediary occupies a central role in the CSF regime. Under the regime, all CSF offers must be made via the 'platform' of a CSF intermediary.

Summary of new law

3.4 A person that intends to operate a crowd-funding platform (the intermediary) will be required to hold an Australian Financial Services Licence (AFSL) and may also be required to obtain an Australian Market Licence (AML).

3.5 For intermediaries required to obtain an AFSL, the Bill creates a new type of financial service, being the crowd-funding service.

3.6 The intermediary has a number of obligations under the CSF regime, including:

- 'gatekeeper' obligations (which set out when the intermediary must not publish or continue to publish an issuer's offer document);
- the obligation to provide a communication facility;

- the obligation to prominently display on the platform the CSF risk warning, information on cooling-off rights, and fees charged to and interests in an issuer company;
- the obligation to ensure retail clients receive the benefit of the relevant investor protections (cooling-off rights, the investor cap, the risk acknowledgement) and that the obligation to comply with the prohibition on providing financial assistance is adhered to; and
- the obligations to close or suspend the offer as required, and handle application monies appropriately.

Comparison of key features of new law and current law

New law	*Current law*
A person that intends to operate a crowd-funding platform (the intermediary) will be required to hold an Australian Financial Services Licence (AFSL) and may also be required to hold an Australian Market Licence (AML).	No equivalent.
A new financial service has been created: a crowd-funding service.	No equivalent.
A CSF intermediary has a number of obligations under the CSF regime, including: • 'gatekeeper' obligations; • the obligation to provide a communication facility; • the obligation to prominently display on the platform the CSF risk warning, information on cooling-off rights, and fees charged to and interests in an issuer company; • the obligation to implement systems to ensure retail clients receive certain additional investor protections; and • the obligations to close or suspend the offer as required, and handle application monies appropriately.	No equivalent.

Detailed explanation of new law

Overview — the role and obligations of an intermediary

3.7 The amendments define the role of the CSF intermediary, the licensing requirements for an intermediary and the various obligations with which the intermediary must comply. The amendments are explained in detail below.

The CSF intermediary must be licensed

3.8 The Bill creates a new type of financial service: a crowd-funding service. A person that intends to provide a crowd-funding service must hold an AFSL that expressly authorises the provision of a crowd-funding service ***[Schedule 1, Part 1, items 14 and 25, section 738C and paragraph 766A(1)(ea)].*** Depending on the nature of the activities carried out by the person, they could also be considered to be operating a financial market and therefore be required to hold an Australian Market Licence (AML).

3.9 The policy intent is that the provision of the crowd funding service should be subject to the obligations and protections, particularly as they apply to retail clients, of the AFSL regime (refer to paragraphs 3.17 to 3.18). Therefore, a person that holds an AML would not satisfy the definition of CSF intermediary unless they also held an AFSL that expressly authorised the provision of the crowd-funding service. This means that a person that holds an AML cannot rely on the exemption in paragraph 911A(2)(d) for incidental financial services to provide a crowd-funding service (as they would not satisfy the definition of CSF intermediary). Under the CSF regime, a CSF offer can only be made by publishing a CSF offer document on a platform of a CSF intermediary ***[Schedule 1, Part 1, item 14, section 738L].***

3.10 The Minister has a power under section 791C that can be used to exempt operators from the obligation to hold an AML. Schedule 3 to the Bill provides the Minister with additional exemption powers that can be used to exempt certain financial market operators from specified AML obligations, allowing the AML regime to be tailored to particular markets, which could include intermediaries providing crowd-funding services.

Meaning of crowd-funding service

3.11 A person will provide a crowd-funding service if:

- a CSF offer document for a CSF offer of securities of a company is published on a platform operated by the person; and
- applications may be made to the person for the issue, by the company, of securities pursuant to the offer. ***[Schedule 1, Part 1, items 22 and 27, section 761A and subsection 766F(1)]***

3.12 A crowd-funding service is also taken to include performing all aspects of the role of CSF intermediary as required under the CSF regime ***[Schedule 1, Part 1, item 27, subsection 766F(2)]***. This means, for example, that a CSF intermediary will be taken to provide a crowd-funding service where it performs its gatekeeper obligations, holds application money on trust and operates the communication facility.

3.13 Deeming such activities to be part of the crowd-funding service means that the general obligations in section 912A (such as that the financial service must be provided efficiently, honestly and fairly) will apply to the CSF intermediary in respect of all activities it performs as part of its role of CSF intermediary.

3.14 While there is no explicit carve out from the definition of crowd-funding service applying to agents or employees of a CSF intermediary, agents and employees will not be required to obtain a separate AFSL as they will come within the scope of the exemption in paragraph 911A(2)(a). This paragraph provides that a person who provides a financial service as a representative of an AFSL holder whose licence covers the financial service is exempt from the requirement to hold an AFSL in relation to the financial service. A representative includes: an authorised representative; an employee or director of the licensee; or any other person acting on behalf of the licensee (paragraph 910A(a)). A person who operates a platform for a crowd-funding service, other than an employee or officer of the licensee or a related body corporate of the licensee will not be able to rely on this exemption as a CSF offer can only be made by publishing, on a platform of a CSF intermediary, a CSF offer document that complies with section 738J.

When and to whom is a crowd-funding service provided

3.15 The Bill makes it clear that the crowd-funding service is provided to both the person seeking to apply for the CSF securities and the company making the CSF offer. ***[Schedule 1, Part 1, item 27, subsections 766F(3) and (4)]***

3.16 In the case of a person seeking to apply for CSF securities, the crowd-funding service is provided at the time when the person first uses the application facility to apply for an offer ***[Schedule 1, Part 1, item 27, subsection 766F(3)]***. In the case of an issuer company, the crowd-funding service will be provided at the time the company enters into the hosting arrangement for the offer ***[Schedule 1, Part 1, item 27, subsection 766F(4)].***

3.17 The intermediary must determine, at the relevant time the crowd-funding service is provided, whether the person to whom the service is provided is a 'retail client'. This is important as certain additional protections and obligations under Chapter 7 are applicable to retail clients.

3.18 A person that is provided a crowd-funding service as a retail client will be entitled to certain additional protections under Chapter 7. The intermediary must ensure that they:

- provide a Financial Services Guide to an applicant or issuer that is a retail client, generally as soon as practicable after it becomes apparent to the intermediary that the financial service is likely to be provided (subsections 941A(1) and 914D(1));
- have a compliant internal dispute resolution scheme and are a member of an ASIC approved external dispute resolution scheme (paragraph 912A(1)(g) and subsection 912A(2)); and
- have arrangements for compensating retail clients for loss or damage suffered because the licensee breached its licensing obligations (section 912B).

3.19 An investor considered to be a retail client under Chapter 7 in relation to the crowd-funding service will also be a retail client for the purpose of the CSF offer, which will entitle them to certain additional investor protections such as cooling-off rights, risk acknowledgments and the investor caps ***[Schedule 1, Part 1, item 23, subsection 761G(8)]***. These protections are discussed in further detail in Chapter 6 of the Explanatory Memorandum.

3.20 A person that is not considered to be a retail client will be a wholesale client (and would not, for example, be subject to the investor cap).

When a crowd-funding service is provided to a person as a retail client

3.21 Subsection 761G(7) contains the tests for determining when a person will be a retail client in relation to the crowd-funding service. The person to whom the crowd-funding service is provided will be a retail client unless one or more of the following tests are satisfied:

- the product-value test: the price of the financial product (the securities on offer) or the value of the financial product to which the financial service relates, equals or exceeds $500,000 (paragraph 761G(7)(a) and Regulations 7.1.18 and 7.1.19); or

- the securities or crowd-funding service is provided for use in a business other than a small business (paragraph 761G(7)(b)). A small business is defined as a business employing less than 20 people, unless the business includes the manufacture of goods, where the business must employ less than 100 people (subsection 761G(12)); or

- where the securities or the crowd-funding service is not provided for use in connection with a business, the person acquiring the securities or crowd-funding service gives the intermediary a certificate prepared by a qualified accountant (defined in section 9) within the preceding six months that states that the person has net assets of $2.5 million, or gross income in the last 2 financial years of at least $250,000 (paragraph 761G(7)(c) and Regulation 7.1.28); or

- the person to whom the crowd-funding service is provided is a professional investor as defined in section 9 (paragraph 761G(7)(d)). A professional investor includes an Australian financial services licensee, a listed entity, a bank, or a person that has or controls gross assets of at least $10 million.

3.22 Subsection 761G(8) provides that, in the case of a prosecution for any offence based on a provision in Chapter 7, if the defendant (in this case the intermediary) alleges that the financial service was provided to the person as a wholesale client, the defendant will be required to raise evidence that the person to whom the crowd-funding service was provided was not a retail client. Imposing the evidential burden on the defendant is appropriate given the policy intent is to ensure that persons that acquire

financial products and financial services as retail clients have the benefit of the additional protections in the CSF regime and Chapter 7 more generally.

3.23 In the case of non-criminal proceedings, subsection 761G(9) provides that the presumption is that the financial product or crowd-funding service is provided to a person as a retail client unless the contrary is established.

3.24 The Bill provides that section 761GA, which would otherwise provide a mechanism whereby a financial services licensee could certify that a client has sufficient expertise to be treated as wholesale, does not apply to the provision of a crowd-funding service ***[Schedule 1, Part 1, item 24, section 761GA].***

'Dealing' does not include providing a crowd-funding service

3.25 Certain activities of a CSF intermediary, which relate to arranging for the issue of securities, would also fall within the definition of the 'dealing' financial service in section 766C. To address the overlap, the Bill carves out a crowd-funding service from the dealing financial service ***[Schedule 1, Part 1, item 26, subsection 766C(2A)]***. The result is that a CSF intermediary will need only one AFSL authorisation to operate a crowd-funding platform and will only need to consider when and to whom the crowd-funding service is provided for the purposes of their obligations under the CSF regime and Chapter 7 more generally.

Carve out from the definition of managed investment scheme

3.26 The amendments exclude the provision of a crowd-funding service from the definition of a managed investment scheme (MIS). This is to ensure the CSF intermediary is not subject to obligations under both the CSF regime and the MIS rules. ***[Schedule 1, Part 1, item 2, section 9]***

Obligations of a CSF intermediary

3.27 The legislation imposes a number of obligations on the CSF intermediary, referred to as a 'responsible intermediary' in relation to a particular CSF offer ***[Schedule 1, Part 1, item 14, subsection 738L(5)]***. The intermediary must comply with:

- the 'gatekeeper' obligations (which set out when an intermediary must not publish, or continue to publish, the offer document of an issuer company on its platform);
- the obligation to provide a communication facility;

- the obligation to display the CSF risk warning, display cooling-off rights and appropriately disclose fees and interests in an issuer company on the platform;

- the obligation to implement systems and procedures so that retail clients receive the additional investor protections in the CSF regime (cooling-off rights, investor cap, the risk acknowledgement and the prohibition on providing financial assistance); and

- the obligations to close or suspend the offer as required, and handle application money appropriately.

Gatekeeper obligations

3.28 An intermediary must comply with certain 'gatekeeper' obligations ***[Schedule 1, Part 1, item 14, section 738Q]***.

Intermediary must conduct prescribed checks

3.29 Prior to publishing an offer document on its platform, an intermediary must conduct certain checks, which will be specified in the regulations ('prescribed checks'). ***[Schedule 1, Part 1, item 14, subsection 738Q(1)]***

3.30 The intermediary must conduct the checks to a 'reasonable standard' ***[Schedule 1, Part 1, item 14, subsection 738Q(1)]***. The amendments include a regulation-making power that could be used to prescribe what would be considered a reasonable standard for some or all of the checks, thereby providing certainty to intermediaries conducting the checks ***[Schedule 1, Part 1, item 14, subsection 738Q(2)]***.

3.31 An intermediary that fails to conduct the checks, or fails to conduct the checks to a reasonable standard, will commit a strict liability offence, punishable by a maximum penalty of 50 penalty units ***[Schedule 1, Part 1, item 14 and 34, subsection 738Q(3) and item 245E in the table to Schedule 3]***.

3.32 Strict liability, and the level of penalty, is appropriate, because:

- the intermediary has a central role in the CSF regime and the obligation to conduct the prescribed checks to a reasonable standard is necessary to maintain the integrity of the CSF regime;

- conducting the checks and the standard to which the checks are conducted is entirely dependent on the conduct of the intermediary who is liable for the offence;

- the proposed penalty for the offence is consistent with the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* which specifies that a strict liability offence should be punishable by a maximum penalty of 60 penalty units with no term of imprisonment.

3.33 Where an intermediary fails to conduct a check, or fails to conduct a check to a reasonable standard, the intermediary is taken to have knowledge of any matter that they would have had knowledge of had they conducted the check to a reasonable standard ***[Schedule 1, Part 1, item 14, subsection 738Q(4)]***. This deemed knowledge is relevant in determining whether the intermediary has complied with its obligations to not publish, or not continue to publish, the CSF offer document (discussed below).

3.34 While the regulations will prescribe the checks that must be conducted by an intermediary prior to publishing a CSF offer document, they are not intended to limit the checks or information that may be sought by an intermediary from the issuer company or its officers.

3.35 The amendments make it an offence for an officer or employee of a company to provide information that they know to be false or misleading in a material particular, or that omits a matter or thing which renders the information misleading in a material particular. ***[Schedule 1, Part 1, item 32, paragraph 2(1)(c)]***

Intermediary must not publish or continue to publish offer document if not satisfied as to certain matters

3.36 A CSF intermediary must not publish, or continue to publish, an offer document if it:

- is not satisfied as to the identity of the company making the offer or of its directors or other officers;
- has reason to believe that any of the directors or other officers of the company are not of good fame or character;
- has reason to believe that the company or directors or other officers of the company have, in relation to the offer, knowingly engaged in conduct that is misleading or deceptive or likely to mislead or deceive;
- has reason to believe that the particular offer is not eligible to be made as a CSF offer ***[Schedule 1, Part 1, item 14, subsection 738Q(5)]***.

3.37 The purpose of the gatekeeper obligations is not to require the intermediary to conduct exhaustive due diligence on the company, its directors or other officers, or the company's business. Such an obligation would impose a relatively high burden on an intermediary, with potential flow-on costs for issuers seeking to access the intermediary's platform.

3.38 Rather, the gatekeeper obligations are intended to ensure that an intermediary does not publish, or continue to publish, the offer document in four specific circumstances. The basis for not publishing or continuing to publish the offer document is dependent on the actual knowledge of the intermediary (that is, whether they were satisfied as to certain matters or had reason to believe certain things) and what the intermediary should have become aware of from conducting the prescribed checks to a reasonable standard. Aspects of each situation where an intermediary must not publish or continue to publish an offer document are discussed below.

Not satisfied as to the identity of the company or its directors or other officers

3.39 The first situation where an intermediary must not publish or continue to publish the offer document is where the intermediary is not satisfied as to the identity of the company, its directors or other officers. ***[Schedule 1, Part 1, item 14, paragraph 738Q(5)(a)]***

3.40 For the purpose of this requirement, the relevant definition of 'officer' is the definition 'officer of a corporation' (section 9) which is broad enough to also include a person who is not a director of the company but who exerts significant influence over the company or its directors.

Has reason to believe that any of the officers are not of good fame or character

3.41 The second situation where an intermediary must not publish or continue to publish the offer document is where the intermediary has reason to believe that any of the officers of the issuer company are not of good fame or character. ***[Schedule 1, Part 1, item 14, paragraph 738Q(5)(b)].***

3.42 The amendments do not define good fame or character. However, the term is used in the licensing process as one of the preconditions prior to ASIC granting an AFSL. Specifically, subsection 913B(4) states that ASIC must be satisfied that there is no reason to believe: the person applying for the AFSL (where a natural person); or the responsible officers (where the applicant is a body corporate); or any of the partners or trustees (where the applicant is a partnership or trust) are not of good fame or character.

3.43 Subsection 913B(4) provides that ASIC must, in assessing whether there is reason to believe a person is not of good fame or character, have regard to certain matters including certain criminal convictions a person may have had, whether the person held an AFSL that was cancelled or suspended, whether a banning or disqualification order under Division 8 was previously made, or any other matter ASIC considers to be relevant.

Has reason to believe that the company or its officers have, in relation to the CSF offer, knowingly engaged in conduct that is misleading or deceptive or likely to mislead or deceive

3.44 Where an intermediary has reason to believe that an issuer has knowingly engaged in conduct that is misleading or deceptive, or conduct that is likely to mislead or deceive, the intermediary must not publish or continue to publish the offer document ***[Schedule 1, Part 1, item 14, paragraph 738Q(5)(c)].*** For example, if an intermediary in considering whether to host an offer of a company has, in its dealings with the directors, reason to believe that the directors' representations in relation to the CSF offer are dishonest, the intermediary must not publish the offer document.

3.45 In the case of an offer that is already open, if the intermediary has reason to believe that the directors have, for example, knowingly provided misleading information in response to a post on the communications facility, the intermediary must not continue to publish the offer document and must close the offer.

3.46 The obligation to close the offer will only arise where the intermediary has reason to believe the issuer *knowingly* engaged in misleading or deceptive conduct. The inclusion of 'knowingly' recognises that there may be cases where an issuer may have, for example, unintentionally provided information that is misleading. In such circumstances, it would be inappropriate if the intermediary's only course of action was to remove the offer document from the platform and close the CSF offer.

3.47 If the intermediary has reason to believe that the issuer company knowingly engaged in conduct that was misleading or deceptive, or that was likely to mislead or deceive, the intermediary must remove the offer document from the platform and close the offer.

Interaction with provisions relating to defective offer documents

3.48 Where the conduct that is misleading or deceptive, or that is likely to mislead or deceive, is in relation to a defective offer document that contains a misleading or deceptive statement, an omission, or where

there has been a new circumstance that has arisen since the document was published that would have been required to have been included in the document had it arisen before publication, the specific rules covering defective offer documents will take priority over the gatekeeper obligations. ***[Schedule 1, Part 1, item 14, subsection 738Q(6)]***

3.49 The provisions relating to defective offer documents are discussed in Chapter 4 and require an intermediary to either close or suspend an offer when it is aware that the offer document is defective. Where it suspends the offer, the company will have the opportunity to prepare a supplementary or replacement offer document to correct the defect. In effect, the rules regarding defective disclosure documents will take priority over the gatekeeper obligations.

3.50 However, where an offer document is defective, for example, because it contains a misleading statement, but the company also knowingly makes another misleading statement on the communication facility, the intermediary will be required to close the offer as the gatekeeper obligations will apply in relation to the company's conduct relating to the communication facility, even if they do not apply in relation to the offer document.

Has reason to believe that the offer is not eligible to be made as a CSF offer

3.51 An intermediary must not publish or continue to publish an offer document where it has reason to believe that the offer is not eligible to be made as a CSF offer. ***[Schedule 1, Part 1, item 14, paragraph 738Q(5)(d)]***

3.52 This obligation is intended to ensure that issuers that purport to be eligible for the CSF regime, but are not in fact eligible, are excluded from making a CSF offer. For example, if the intermediary has reason to believe that the proposed offer does not comply with the issuer cap, the intermediary must not publish the issuer's offer document.

Offences

3.53 An intermediary that fails to comply with its gatekeeper obligations will commit an offence, punishable by a maximum penalty of 60 penalty units, or imprisonment for one year, or both ***[Schedule 1, Part 1, item 34, item 245F in the table to Schedule 3].***

3.54 A related obligation is that an intermediary must have in place 'adequate arrangements' to ensure that it complies with its gatekeeper obligations ***[Schedule 1, Part 1, item 14, subsection 738Q(7)]***. This means that an intermediary must have in place policies, systems and procedures to ensure that it complies with its gatekeeper obligations, and must ensure

that those policies, systems and procedures are adhered to. This must be documented in writing. Failure to do so is an offence, punishable by a maximum penalty of 30 penalty units or imprisonment for 6 months or both ***[Schedule 1, Part 1, item 34, item 245G in the table to Schedule 3)]***.

Other obligations of CSF intermediaries relating to their platform

3.55 The CSF regime sets out a number of other obligations that a CSF intermediary must comply with. These are that the intermediary:

- must ensure the CSF risk warning appears prominently on the platform at all times while the offer is open or suspended ***[Schedule 1, Part 1, item 14, subsection 738ZA(1)]***;
- must provide an application facility, reject any applications made other than via the application facility and not allow an application to be made while an offer is suspended or closed ***[Schedule 1, Part 1, item 14, subsections 738ZA(3) and (4)]***;
- must provide a communication facility for each CSF offer ***[Schedule 1, Part 1, item 14, subsection 738ZA(5)]***;
- must ensure that information relating to a retail investor's cooling-off rights appears prominently on the offer platform while an offer is open or suspended ***[Schedule 1, Part 1, item 14, subsection 738ZA(8)]***; and
- must disclose fees paid to it by the issuer and any interest that the intermediary has or intends to take in the issuer company prominently on the platform ***[Schedule 1, Part 1, item 14, subsection 738ZA(9)]***.

3.56 Failure to comply with any of the obligations set out above will mean the intermediary will commit an offence, punishable by a maximum penalty of 60 penalty units, one year's imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245N in the table to Schedule 3]***. The penalty of 60 penalty units and one year's imprisonment is in accordance with the fine/imprisonment ratio of 5:1 specified in the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* (section 3.1.3 of the Guide refers).

Risk warning

3.57 The intermediary must ensure that the CSF risk warning is displayed prominently on the offer platform. The purpose of the risk warning is to alert potential investors, particularly retail investors of the

potential risks associated with, and high failure rates of, start-ups and emerging companies, which are most likely to be making CSF offers.

3.58 The required wording of the general CSF risk warning will be specified in the regulations ***[Schedule 1, Part 1, item 14, subsection 738ZA(2)]***. The intermediary must ensure that the risk warning appears prominently on its platform at all times, including while an offer is suspended ***[Schedule 1, Part 1, item 14, subsection 738ZA(1)]***.

3.59 The word 'prominently' is not defined and whether the risk warning is prominently displayed will depend on the particular facts and circumstances, including the design of the offer platform.

Applications to only be made via an application facility

3.60 The intermediary must provide a facility — the application facility — on its platform to enable a person to apply for securities that are the subject of a CSF offer. All applications in response to a CSF offer must be made via the intermediary's application facility.

3.61 Where a person tries to apply for CSF securities other than via the application facility, the intermediary must reject the application and refund any money paid as soon as practicable ***[Schedule 1, Part 1, item 14, subsection 738ZA(4) and paragraph 738ZB(4)(b)]***. Requiring all applications in response to the CSF offer to be made via the intermediary is a means of ensuring that applicants are aware of and receive the various investor protections.

3.62 The application facility must only be available while the offer is open — applications must not be able to be made while an offer is closed or suspended. ***[Schedule 1, Part 1, item 14, paragraphs 738ZA(3)(a) and (c)]***

3.63 Where a retail client is trying to apply for securities that are the subject of a CSF offer, the intermediary must ensure that the investor completes a risk acknowledgment ***[Schedule 1, Part 1, item 14, paragraph 738ZA(3)(b)]***. The requirement that a person 'complete' rather than 'sign' the risk acknowledgment means it will not be mandatory for an intermediary to require an applicant to digitally sign the risk acknowledgment (although it could choose to require this). The risk acknowledgment must comply with the requirements set out in the regulations ***[Schedule 1, Part 1, item 14, paragraph 738ZA(3)(b)]***.

Communication facility for each CSF offer

3.64 The intermediary must provide a communication facility in relation to each CSF offer while the offer is open or suspended ***[Schedule 1, Part 1, item 14, subsection 738ZA(5)]***. Requiring a communication facility to be

provided in relation to each CSF offer is consistent with one of the premises underlying crowd-funding, which is that investors can, in part, rely on the collective wisdom of the 'crowd' in making their investment decision.

3.65 The purpose of the communication facility is to allow potential investors, the issuer and intermediary to communicate with each other about a particular CSF offer. Specifically, the communication facility should enable a person who accesses the offer document to make posts relating to the offer, see posts relating to the offer and ask the company making the offer, or the intermediary, questions relating to the offer. It should also enable the company or intermediary to respond to questions and posts. ***[Schedule 1, Part 1, item 14, paragraphs 738ZA(5)(a) and (b)]***

3.66 The communication facility does not need to be open to the general public, but must be made accessible to persons that are able to access the CSF offer document. Where a person is unable to access a CSF offer document until they have registered on an intermediary's platform, the person must be able to make and see posts on the communication facility for the offer on registration.

3.67 While the communication facility will provide an important mechanism for investors to communicate with each other and with the issuer company, persons who are officers, employees or agents of the issuer company, a related party or an associate of the issuer, or of the intermediary, must clearly disclose that fact when making posts on the facility ***[Schedule 1, Part 1, item 14, subsection 738ZA(6)]***. Failure to comply with this rule means the person making the post will commit an offence, punishable by a maximum penalty of 60 penalty units, or one year's imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245N in the table to Schedule 3]***.

3.68 The amendments include a power to make regulations covering the operation, management or use of the communication facility. For example, regulations could be made covering the removal of material from the communication facility. ***[Schedule 1, Part 1, item 14, subsection 738ZA(7)]***.

3.69 Statements made on the communications facility that refer to the CSF offer or would reasonably be likely to induce a person to apply for the CSF offer would ordinarily be subject to the advertising restrictions contained in the Bill. The Bill includes a carve out for statements made in good faith on the communication facility. This carve out is discussed in more detail in paragraphs 6.52 to 6.57.

Cooling-off rights must be displayed on the platform

3.70 The intermediary must ensure that the offer platform prominently displays information regarding the cooling-off rights for retail investors (refer to paragraphs 6.18 to 6.22), including the means by which the investor can exercise these rights. This information must be displayed on the platform at all times, including where an offer is open or suspended. ***[Schedule 1, Part 1, item 14, subsection 738ZA(8)]***

3.71 Whether the information is prominently displayed is a question of fact and degree and will vary depending on how the intermediary's platform is designed.

Fees and interests must be prominently displayed on the platform

3.72 There are no restrictions, in the CSF regime, on the fee arrangements that may be agreed between an issuer and intermediary. For example, there are no prohibitions on an intermediary's fees being calculated based on funds raised under the offer or an intermediary being remunerated in the form of securities in an issuer company in lieu of cash. However, it is appropriate that the fee arrangements between the issuer and intermediary be disclosed to investors and, therefore, there is a requirement that this information be prominently displayed on the platform while the offer is open or suspended. ***[Schedule 1, Part 1, item 14, paragraph 738ZA(9)(a)]***.

3.73 Similarly, while there are no restrictions on an intermediary having or taking a direct or indirect pecuniary interest in the company whose securities it is offering on its platform, it is appropriate that this information is disclosed to investors. Therefore, there is likewise a requirement that this information be prominently displayed on the offer platform at all times while the offer is open or suspended ***[Schedule 1, Part 1, item 14, paragraph 738ZA(9)(b)]***.

Intermediary must deal with application money appropriately

3.74 The client money provisions contained in Division 2 of Part 7.8 will apply to the intermediary as they are an AFSL holder. Broadly, these provisions require an intermediary to hold application money in a qualifying account (the requirements for the account are set out in section 981B). Regulations made under the Division specify matters such as when money may be withdrawn from the account, and how interest earned on the account is dealt with.

3.75 The Bill confirms that the intermediary must deal with application money in accordance with the client money provisions but also contains specific provisions (discussed below) regarding when an

intermediary must either pay money to the issuer or refund money to applicants. ***[Schedule 1, Part 1, item 14, subsection 738ZB(1)]***

When money must be paid to the issuer or refunded to the applicants

3.76 The intermediary must pay application money to an issuer, net of any fees due to the intermediary, as soon as practicable after an offer is 'complete' (that is, the minimum subscription condition has been met and all withdrawal rights have expired, refer to paragraphs 4.50 to 4.53) and the company has issued the shares to the applicants ***[Schedule 1, Part 1, item 14, subsections 738L(8) and 738ZB(2)].***

3.77 The intermediary must refund money to applicants as soon as practicable in the following situations:

- the offer was closed because it was withdrawn by the company (paragraphs 4.47) or because the intermediary was required to close the offer pursuant to its 'gate keeper obligations' (paragraph 4.48);

- the offer was closed for another reason (because the maximum offer period was reached (paragraphs 4.37 to 4.43) or the intermediary considered the offer to be fully subscribed (paragraphs 4.44 to 4.46)) but not complete; or

- an applicant exercised their withdrawal rights — these could be statutory or non-statutory cooling-off rights, or the right to withdraw an offer within one month of receiving a supplementary or replacement offer document relating to a defective offer document (paragraph 5.31) ***[Schedule 1, Part 1, item 14, subsections 738ZB(3) and (4)].***

3.78 An intermediary that does not comply with the above rules will commit a strict liability offence, punishable by a maximum of 50 penalty units ***[Schedule 1, Part 1, item 14, subsection 738ZB(5) and item 34, item 245P in the table to Schedule 3]***.

3.79 Strict liability, and the level of penalty, is considered appropriate because:

- the requirement to deal appropriately with application money is a key element of the CSF regime;

- an intermediary that fails to comply with the rules (for example, by not refunding money when cooling-off rights are exercised, or by paying money to an issuer before the securities are issued), compromises the investor protection and other elements that are central to the CSF regime;

- exposure to the penalty is entirely dependent on the conduct of the intermediary who is liable for the offence; and

- the penalty for the offence complies with the requirements of the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* (that is, the maximum penalty is no more than 60 penalty units and does not include a term of imprisonment).

Regulations may be made regarding how intermediaries are to deal with applications

3.80 The amendments provide for a regulation making power that can permit regulations to be made regarding how CSF intermediaries are to deal with applications pursuant to CSF offers, including in relation to:

- the order in which applications are to be dealt with;

- the circumstances in which applications must or may be rejected; and

- when applications are to be counted towards the maximum or minimum subscription amounts. ***[Schedule 1, Part 1, item 14, section 738ZJ].***

Consequential amendments

3.81 Consequential changes have been made to the ASIC Act to include a crowd-funding service, as defined in the Corporations Act, in the range of financial services covered by the ASIC Act ***[Schedule 1, Part 2, items 35 and 36, subsection 5(1) and subsections 12BAB(1C) and 12BAB(1D) of the ASIC Act].***

3.82 Consequential amendments have been made to extend two current exceptions to the takeover laws.

3.83 The first exception to the takeover laws relates to an acquisition that results from an issue of securities in a company to a promoter under a Chapter 6D disclosure document and where certain required disclosures have been made. The amendments extend the existing exception to cover

acquisitions that arise pursuant to a CSF offer document where the required disclosures have been made. ***[Schedule 1, Part 1, item 6, item 12 in the table in section 611].***

3.84 The second exception to the takeover laws relates to an acquisition that results from an issue of securities in a company to an underwriter or sub-underwriter under a Chapter 6D disclosure document so long as the disclosure document disclosed the effect the issue would have on the underwriter's or sub-underwriter's voting power in the company. The amendments will extend the exception to cover issues of securities pursuant to a CSF offer in a company to an underwriter or sub-underwriter as long as the relevant disclosures have been made in the CSF offer document. ***[Schedule 1, Part 1, item 6, item 13 in the table in section 611].***

3.85 As a CSF intermediary can be established as a partnership or a trust, consequential amendments have been made to ensure the rules in Chapter 7 that treat partnerships and trusts as legal persons generally apply to CSF intermediaries except where the rule is expressed to relate only to specific parts of Chapter 7. ***[Schedule 1, Part 1, item 14, paragraphs 738F(1)(a) and (b), subsection 738F(2)]***

3.86 Consequential amendments have been made to extend the application of the rules in Chapter 7 that provide that a person is generally responsible for the conduct of their directors, employees, agents to the CSF regime. ***[Schedule 1, Part 1, item 14, paragraph 738F(1)(c)]***

3.87 A regulation making power has been included to permit regulations to be made to modify how the above rules apply. ***[Schedule 1, Part 1, item 14, subsection 738F(3)]***

3.88 This modification power is required to ensure that the application of the relevant Chapter 7 provisions to the CSF regime is consistent with the existing provisions in Chapter 7. The existing provisions in Chapter 7 (sections 761F, 761FA and 769B) all have a regulation making power to exclude or modify their effect in relation to specified provisions.

3.89 In applying the existing Chapter 7 provisions to the CSF regime, it is necessary to include a similar modification power so that any changes to the application of the existing provisions to Chapter 7 can also be reflected in the application of these provisions to the CSF regime. As such, the modification power has been included to eliminate the risk that there could be a mismatch between the way the current provisions operate in relation to Chapter 7 or the intended application in Chapter 6D and the way the provisions apply in relation to the CSF regime.

Chapter 4
Process for making a CSF offer

Outline of chapter

4.1 This Chapter sets out the process of making CSF offers.

4.2 Unless otherwise stated, all references in this Chapter relate to the *Corporations Act 2001*.

Summary of new law

4.3 The amendments establish:

- that the process for making a CSF offer involves a CSF eligible company publishing a CSF offer document on a single CSF intermediary's platform;
- that a new document — a 'CSF offer document' — must be prepared for CSF offers;
- that the company must obtain certain consents of persons associated with the offer document prior to its publication;
- that a company making a CSF offer and its related parties cannot have more than one CSF offer open at a time when another CSF offer previously made by the company is open or suspended; and
- rules for determining when a CSF offer is 'open', when it may and when it must be 'closed', and the conditions that must be satisfied before an offer can be 'complete'.

Comparison of key features of new law and current law

New law	*Current law*
CSF offer must be made in accordance with the CSF regime.	An offer requiring disclosure must be made in accordance with Part 6D.2.
A CSF offer document must be prepared for a CSF offer	A disclosure document must be prepared for an offer requiring disclosure.
A CSF offer is made by publishing the CSF offer document on the platform of a single CSF intermediary.	No equivalent
A CSF offer is made when the offer document is published on the platform of a CSF intermediary.	No equivalent.
A CSF offer is open from the time when the offer is made until the offer is suspended or closed by the intermediary.	No equivalent.
A CSF offer is closed from the time when a CSF intermediary gives written notice on the offer platform that the offer is closed.	No equivalent.
A company making a CSF offer and its related parties cannot have more than one CSF offer open at a time.	No equivalent.

Detailed explanation of new law

A CSF offer must be made in accordance with the CSF regime

4.4 The amendments establish the CSF regime: a new disclosure regime that can be used by eligible CSF companies to make certain offers of securities for issue. ***[Schedule 1, Part 1, item 14, section 738A]***

4.5 An offer that is subject to the CSF regime is not subject to Part 6D.2, which contains the general rules regarding when disclosure is required for offers of securities, except as expressly provided for. ***[Schedule 1, Part 1, items 7, 8, 9 and 10, heading to Part 6D.2, section 703B, section 704, section 706]***

4.6 An offer that is subject to the CSF regime is also not subject to Part 6D.3, which contains the prohibitions, liabilities and remedies that apply to offers of securities requiring disclosure, except as expressly

provided for. ***[Schedule 1, Part 1, items 11 and 12, heading to Part 6D.3 and section 725A]***

A CSF offer document must be prepared for each CSF offer

4.7 Under the CSF regime, a CSF offer document must be prepared in relation to each CSF offer. ***[Schedule 1, Part 1, item 14, subsection 738J(1)]***

4.8 The CSF offer document must contain all the information specified in the regulations ***[Schedule 1, Part 1, item 14, subsection 738J(2)]***. The CSF offer document can also contain the CSF offer ***[Schedule 1, Part 1, item 14, subsection 738J(1)]***.

4.9 The above approach has been drafted in recognition of the fact that it is possible for a CSF offer document to satisfy the content requirements specified in the regulations (for example, by including information about the company and its business, the securities on offer, how the proceeds from the CSF offer will be used) but not contain the actual CSF offer (the offer by the company of securities for consideration). In practice, however, it is expected that a CSF offer document would contain the CSF offer as well as the information required to be included by the regulations.

4.10 The information contained in the offer document must be worded and presented in a clear, concise and effective manner and comply with any other requirements specified in the regulations. ***[Schedule 1, Part 1, item 14, section 738K]***

4.11 Where the information in a CSF offer document does not comply with the above requirements, ASIC has stop order powers ***[Schedule 1, Part 1, item 15, paragraph 739(1)(e)]*** which will enable it to order that no issues of the securities be made while the order is in force ***[Schedule 1, Part 1, item 16, paragraph 739(1A)(a)]***. This is similar to the position in relation to existing Chapter 6D disclosure documents where ASIC has stop order powers where the disclosure document is not worded in a clear, concise and effective manner. Unlike other disclosure documents, however, the CSF offer document will not need to be lodged with ASIC.

How to make a CSF offer

4.12 The amendments provide that the CSF offer must be made by a CSF eligible company publishing a CSF offer document on the platform of a single CSF intermediary. ***[Schedule 1, Part 1, item 14, subsection 738L(1)]***

4.13 The requirement that the CSF offer be made via the platform of an intermediary is a key element of the CSF regime. An offer of eligible securities by a CSF eligible company, where expressed to be made under the CSF regime, would qualify as a CSF offer (as the requirements in Division 2 of Part 1 to the Bill would be satisfied). However, it is not appropriate that companies be permitted to make CSF offers otherwise than through the platform of a licensed CSF intermediary, given the intermediary's central role in administering a number of aspects of the regime (refer Chapter 3).

4.14 The amendments require the offer document to be published on the platform of a *single intermediary*. Limiting the issuer to using one offer platform for each CSF offer is appropriate as it supports compliance with other rules in the CSF regime (for example, the issuer cap and investor cap).

Offer must be contained in, or be published together with, the offer document

4.15 As noted above (paragraphs 4.8 and 4.9) it is possible for the CSF offer not to be contained in the offer document. However, if the CSF offer is not contained in the CSF offer document, the CSF offer must be published on the intermediary's platform. ***[Schedule 1, Part 1, item 14, subsection 738L(1)]***

Applications and application money must be handled via intermediary

4.16 All applications in response to the CSF offer must be made via the intermediary's offer platform. This ensures that investors, particularly retail clients, are provided with the various protections in the CSF regime (such as the communication facility, risk warning and cooling-off rights). It is also intended that all application money in respect of applications to the CSF offer be handled by the intermediary. This ensures that application money is handled appropriately, as the intermediary, being an AFSL holder, will be subject to the client money provisions (as well as obligations in the CSF rules for when money must be paid to the issuer company and refunded to the applicants) (refer to paragraphs 3.74 to 3.79).

4.17 The obligation to ensure that applications and application money are handled via the intermediary is given effect by the provision requiring the agreement between the issuer and intermediary for the publication of the offer document (referred to in the Bill as the 'hosting arrangement') to require all applications relating to the CSF offer to be made via the intermediary's platform and all application monies to be paid to or dealt with by the intermediary. ***[Schedule 1, Part 1, item 14, subsection 738L(2)]***

Failure to comply will be an offence

4.18 If the company does not make the CSF offer as required (by publication of the CSF offer and a complying CSF offer document on the platform of a single intermediary) or the hosting agreement does not require all applications and application money to be handled via the intermediary, the company will commit an offence. ***[Schedule 1, Part 1, item 14, subsection 738L(3) and item 34, item 245A in the table to Schedule 3]***.

4.19 The offence carries a maximum penalty of 300 penalty units, five years imprisonment or both.

4.20 The five year term of imprisonment is consistent with the penalty that currently applies to a person offering securities where the offer requires disclosure under Chapter 6D.2. The penalty units for the offence have been calculated in accordance with the fine/imprisonment ratio of 5:1 specified in the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* (section 3.1.3 of the Guide refers).

Only one offer may be published at a time

4.21 An issuer company cannot have more than one CSF offer open at a time when another CSF offer previously made by the company is open or suspended. ***[Schedule 1, Part 1, item 14, subsection 738R(1)]***

4.22 In addition, a company cannot make a CSF offer at the same time as a related party of the company makes a CSF offer. The purpose of this prohibition is predominantly to support the enforceability of the issuer cap, which applies to funds raised by the issuer and its related parties. Allowing the issuer and its related parties to make simultaneous CSF offers would make it difficult to enforce the issuer cap. ***[Schedule 1, Part 1, item 14, subsection 738R(2)]***

4.23 Failure to comply with the prohibitions against making more than one offer at a time is an offence carrying a maximum penalty of 300 penalty units, five years imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245H in the table to Schedule 3].***

Consents required prior to publication

4.24 Consistent with the arrangements applying under Chapter 6D.2 to other disclosure documents, a company must not arrange for publication of the CSF offer document until they obtain the necessary consents.

4.25 Firstly, the company must obtain the consent in writing of each person named in the offer document as a director or proposed director prior to publication. ***[Schedule 1, Part 1, item 14, subsection 738M(1)]***

4.26 Where the CSF offer document includes a statement by a person, or includes a statement that is indicated in the offer document to be based on a statement by a person, the company must not arrange for publication of the offer document unless:

- that person has consented in writing to the statement being included in the offer document in the form and context in which it is included;
- the offer document states the person has given their consent; and
- the person has not withdrawn their consent prior to publication. ***[Schedule 1, Part 1, item 14, subsection 738M(2)]***

4.27 The consents must be retained by the company for a period of seven years. ***[Schedule 1, Part 1, item 14, subsection 738M(3)]***

4.28 The requirement to obtain and retain written consents is important as the consents may be relevant to any criminal proceedings or cause of action that an investor may wish to commence in the event that the CSF offer document is defective (Chapter 5).

4.29 Failure to obtain or retain written consents is a strict liability offence, carrying a maximum penalty of five penalty units. The penalty is consistent with the existing penalty applying to the comparable offence in Chapter 6D. ***[Schedule 1, Part 1, items 14 and 34, subsection 738M(4) and item 245B in the table to Schedule 3]***

4.30 Strict liability, and the level of penalty for the new offence, is appropriate, for a number of reasons:

- a person named in the offer document as a director or proposed director, or a person said to have made a statement included in the offer document are potentially criminally liable or are exposed to an action for recovery of loss or damage by investors in the event the offer document is defective. Requiring the company to obtain written consent of these persons prior to publication is therefore a crucial step as it provides an opportunity for the person to try to amend the contents of the offer document, or not provide consent, to minimise their potential liability;

- the requirement to obtain written consent and retain the consent for seven years is clear and easy to understand, and the offence depends entirely on the action or non-action of the company which is liable for the offence.

4.31 Consistent with the Government's *Guide to Framing* Commonwealth Offences, Infringement Notices and Enforcement Powers, the maximum penalty for the offence is below the maximum penalty amount in the Guide of 60 penalty units and the penalty does not include a term of imprisonment.

Timing rules related to a CSF offer

When a CSF offer is open, closed and complete

4.32 A CSF offer is open from the time when it is first published on the platform of the responsible intermediary ***[Schedule 1, Part 1, item 14, subsection 738N(2)].***

4.33 A CSF offer can only be closed by an intermediary giving written notice on the offer platform that the offer is closed.

4.34 An intermediary has the power to close a CSF offer at any time, although the hosting arrangement between the intermediary and the issuer can place limits on when the intermediary can close the offer except where the intermediary is required, under these amendments, to close an offer. ***[Schedule 1, Part 1, item 14, subsections 738N(3) and (5)]***.

4.35 When an intermediary gives notice on the platform that an offer is closed, the offer will be closed from the time when notice is first given ***[Schedule 1, Part 1, item 14, subsection 738N(3)]***. It is not necessary for the notice to continue to appear on the platform for the offer to be closed.

When an intermediary must close an offer

4.36 The Bill sets out five circumstances, discussed in detail below, where an intermediary must close a CSF offer (paragraphs 4.37 to 4.48). Where an intermediary fails to close the offer as required, the intermediary will commit an offence, punishable by a maximum penalty of 30 penalty units, six months imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245C in the table to Schedule 3]***. The offer must be closed at the earliest of the following times:

- three months after the CSF offer is made;
- if the offer document states a date by which the offer will close, that date;

- when the intermediary considers the offer to be fully subscribed;
- when the company withdraws the offer; or
- when the company's 'gatekeeper' obligations require the intermediary to remove the offer document from its platform.

Offer must be closed after three months

4.37 A CSF offer can be open for a maximum of three months ***[Schedule 1, Part 1, item 14, paragraph 738N(4)(a)]***. It is appropriate that there be a capped maximum offer period to ensure information contained in the CSF offer document (which is a limited disclosure document) remains current. A three month time limit is also consistent with the notion of CSF as a simpler, faster way of raising funds with streamlined disclosure.

4.38 The three month time limit cannot be extended for any reason. This means, for example, if the company became aware that the offer document was defective two months into the offer period, the intermediary would still be required to close the offer at the end of three months after the CSF offer was initially made, even if the company prepared a supplementary or replacement offer document. The company would not be precluded, however, from making a new CSF offer.

4.39 Assuming the CSF offer is closed at three months, the intermediary must determine, after the expiry of all withdrawal rights, whether:

- the offer is 'complete': that is, the minimum subscription condition is met disregarding withdrawn applications. The intermediary will be required to pay application money to the issuer following the issue of the securities ***[Schedule 1, Part 1, item 14, subsection 738N (7) and subsection 738ZB(2)]***; or
- the offer is unsuccessful as the minimum subscription amount was not raised. This means the intermediary must refund application money to applicants ***[Schedule 1, Part 1, item 14, subsection 738ZB(3)]***

4.40 An intermediary that closes the offer because the three month time limit is reached may, but is not required to, remove the offer document from its platform ***[Schedule 1, Part 1, item 14, subsection 738P(2)]***. The intermediary will, therefore, have the option of maintaining the offer document on the platform after the offer is closed as an archive of the previous offers it has hosted.

Offer must be closed by the date specified in the offer document

4.41 The issuer company is not required to specify an offer close date in the offer document. However, if the issuer does specify a date (or period) by which the offer will close, the intermediary must close the offer at that time (or upon expiry of that period) ***[Schedule 1, Part 1, item 14, paragraph 738N(4)(b)]***.

4.42 Neither the intermediary nor the issuer are able to extend the closing date beyond what was specified in the offer document, including if the offer document was found to be defective and the issuer prepared a replacement or supplementary offer document.

4.43 An intermediary that closes the offer because the offer closure date specified in the offer document is reached may, but is not required to, remove the offer document from its platform. ***[Schedule 1, Part 1, item 14, subsection 738P(2)]***

Offer must be closed when intermediary considers the offer fully subscribed

4.44 An intermediary has the power to close an offer when it considers the offer to be fully subscribed to the maximum subscription amount ***[Schedule 1, Part 1, item 14, subsection 738L(7) and paragraph 738N(4)(c)].*** This is consistent with the policy intent that an issuer not be able to raise more than the maximum subscription amount specified in the offer document as disclosures regarding the purpose to which funds would be put would be premised on the basis that no more than the maximum subscription amount would be raised.

4.45 Allowing an intermediary to close an offer where they 'consider' the offer to be fully subscribed provides some flexibility. For example, an intermediary may allow the application facility to receive applications that exceed the maximum subscription amount if, from experience, it expects a certain proportion of applicants will withdraw their acceptances (pursuant to cooling-off rights). If the offer does result in applications worth more than the maximum subscription amount being received, even after taking into account withdrawals of acceptances, the intermediary should reject applications to ensure that no more than the maximum amount is collected and transferred to the issuer. Application money relating to rejected applications must be returned to the investor ***[Schedule 1, Part 1, item 14, paragraph 738ZB(4)(b)]***.

4.46 An intermediary that closes a CSF offer because it considers the offer to be fully subscribed may, but is not required to, remove the offer document from its platform. ***[Schedule 1, Part 1, item 14, subsection 738P(2)]***

Offer must be closed if the company withdraws the offer or gatekeeper obligations apply

4.47 A company has the power to withdraw a CSF offer at any time before the offer is complete ***[Schedule 1, Part 1, item 14, section 738S)]***. To do so, the company must notify the intermediary that the offer is withdrawn. Once an intermediary receives such a notification it must, as soon as practicable, close the offer and remove the offer document from its platform. ***[Schedule 1, Part 1, item 14, paragraph 738N(4)(d) and subsection 738P(1)]***

4.48 The intermediary must close an offer if it is required to remove the offer document pursuant to its gatekeeper obligations (discussed in paragraphs 3.28 to 3.54) and must remove the offer document from its platform. Failure to comply is an offence, punishable by a maximum penalty of 30 penalty units, six months imprisonment or both ***[Schedule 1, Part 1, items 14 and 34, paragraph 738N(4)(e), subsection 738P(1), item 245D in the table to Schedule 3]***

Dealing with application money once an offer is closed

4.49 Once an offer is closed, the next step is for the intermediary to determine if the offer is 'complete' and, if so, handle application money appropriately.

4.50 There are three conditions that must be satisfied before an offer can be 'complete'.

4.51 Firstly, the offer must have closed because: the three month maximum duration of a CSF offer expired; the offer close date specified in the offer document was reached; or the intermediary considered the offer to be fully subscribed ***[Schedule 1, Part 1, item 14, paragraph 738N(7)(a)]***. If an offer is closed for another reason (for example, because it was withdrawn by the issuer, or the intermediary had to close the offer pursuant to its 'gatekeeper' obligations), it can never be 'complete'.

4.52 The second condition is that all possible withdrawal rights — whether statutory or provided for by the intermediary — which permit an applicant to withdraw their application must have expired ***[Schedule 1, Part 1, item 14, paragraph 738N(7)(b)].*** This means that an intermediary must wait for the expiry of the 48 hour cooling-off rights for retail clients (refer to paragraphs 6.18 to 6.22), the one month right to withdraw an application (which applies to all investors where an issuer publishes a supplementary or replacement offer document in relation to a defective offer document, refer to paragraph 5.31) and any other non-statutory withdrawal rights that the intermediary provides.

4.53 The final condition is that the value of the applications received, disregarding any applications that have been withdrawn or rejected by the intermediary, must exceed the minimum subscription amount set out in the offer document ***[Schedule 1, Part 1, item 14, paragraph 738N(7)(c))]***.

4.54 An offer that is closed but not complete, because it was withdrawn by the issuer or the intermediary was required to close the offer pursuant to its 'gatekeeper' obligations, will result in the intermediary refunding application money held to the applicants (paragraph 3.77).

Chapter 5
Defective CSF offer documents

Outline of chapter

5.1 This Chapter sets out the rules concerning defective CSF offer documents.

5.2 Unless otherwise stated, all references in this Chapter relate to the *Corporations Act 2001*.

Summary of new law

5.3 The amendments define when a CSF offer document is deemed to be 'defective'. The definition is aligned with the existing provisions in Chapter 6D applying to prospectuses and other offer documents.

5.4 The amendments set out notification obligations applying to certain classes of persons if they become aware that an offer document is defective. A number of further obligations and possible actions applying to the intermediary and company making the offer are defined in circumstances where an offer document is defective.

5.5 Liabilities arising from a defective disclosure document are set out in the amendments. These include criminal liability as well as exposure to action for recovery of loss or damage where the statement, omission or new circumstance which led to the document being defective is *materially adverse* from the point of view of an investor.

Comparison of key features of new law and current law

New law	*Current law*
A company must not make a CSF offer under a defective offer document.	A company must not make an offer of securities requiring disclosure under a defective disclosure document.
A CSF intermediary must not publish or continue to publish a CSF offer document if the document is defective and the intermediary knows the offer document is defective.	No equivalent.

New law	*Current law*
Persons that are liable on the CSF offer document must notify the company and the CSF intermediary if they become aware that the offer document is defective.	Persons liable on the disclosure document must inform the person making the offer if they become aware of deficiencies in the disclosure document.
A CSF intermediary must suspend a CSF offer if it becomes aware that the CSF offer document is defective.	No equivalent.
A company can prepare a supplementary or replacement CSF offer document where the original CSF offer document is defective or does not satisfy the requirements of a CSF offer document.	A company can prepare a supplementary or replacement disclosure document to correct a deficiency in the original disclosure document or to change the terms of the offer.
An intermediary that publishes a supplementary or replacement CSF offer document must notify applicants that made applications pursuant to the original CSF offer document that they have one month from the date of the notice in which to withdraw their application.	If the original disclosure document is defective, the company could either: repay application money to applicants; give applicants a supplementary or replacement disclosure document and one month to withdraw their application; or issue the securities to the applicants and provide them with one month to return the securities and be repaid.
A company that offers securities under a CSF offer document that is defective commits an offence if the defect is materially adverse from the point of view of an investor.	A company that offers securities under a defective disclosure document commits an offence if the defect is materially adverse from the point of view of an investor.
An intermediary that publishes a CSF offer document that it knows to be defective commits an offence if the defect is materially adverse from the point of view of an investor.	No equivalent.
An investor that suffers loss or damage because of a defective CSF offer document is able to recover the amount of the loss or damage from persons liable on the offer document.	An investor that suffers loss or damage because of a defective disclosure document is able to recover the amount of the loss or damage from persons liable on the disclosure document.
ASIC may make a stop order in relation to a defective CSF offer document.	ASIC may make stop orders in relation to defective disclosure documents.

Detailed explanation of new law

Prohibition on making offers under a defective CSF offer document

5.6 The amendments provide that a company must not offer securities under a CSF offer document if the document is defective ***[Schedule 1, Part 1, item 14, subsection 738Y(1)].*** A company will be taken to offer securities under a CSF offer document, at all times, before the offer is closed, while the document is published on a platform of the intermediary ***[Schedule 1, Part 1, item 14, subsection 738Y(2)]***.

5.7 The amendments provide that an intermediary must not publish or continue to publish a CSF offer document if the document is defective and the intermediary *knows* the document is defective ***[Schedule 1, Part 1, item 14, subsection 738Y(3)]***. For the purposes of determining whether the intermediary knew the offer document was defective, the intermediary is taken to have knowledge of any matter that they would have had knowledge of had they conducted the prescribed checks to a reasonable standard ***[Schedule 1, Part 1, item 14, subsection 738Q(4)]***.

When an offer document will be 'defective'

5.8 A CSF offer document will be defective where:

- the document contains a misleading or deceptive statement; or
- there is an omission from the document of information required to be included in the document; or
- since the document was published, a new circumstance has arisen that would have been required to have been included in the document had it arisen prior to the document being published. ***[Schedule 1, Part 1, item 14, subsection 738U(1)]***

5.9 The amendments provide that a misleading statement includes a statement about a future matter where the person making the statement does not have reasonable grounds for making the statement ***[Schedule 1, Part 1, item 14, subsection 738U(2)]***.

Notification obligations where the offer document is defective

5.10 The amendments place obligations on certain persons associated with the offer document to provide written notification to the company and intermediary if they become aware, while the CSF offer is open, that the offer document is defective:

- if the issuer company becomes aware that the document is defective, it must notify the responsible intermediary as soon as practicable ***[Schedule 1, Part 1, item 14, subsection 738V(1)]***;

- if the intermediary becomes aware that the offer document is defective, the intermediary must notify the company as soon as practicable ***[Schedule 1, Part 1, item 14, subsection 738V(2)]***; and

- if another person who is liable on the offer document (refer paragraph 5.42) becomes aware that the offer document is defective, that person must notify the company and the intermediary as soon as practicable ***[Schedule 1, Part 1, item 14, subsection 738V(3)].***

5.11 The notification obligation only arises where the person required to notify *becomes aware* that the offer document is defective. If the person does not know that the document is defective, then no obligation to notify will arise.

5.12 In the case of an intermediary, it is relevant to note that an intermediary is taken to have knowledge of any matter that they would have known of had they conducted the prescribed checks to a reasonable standard ***[Schedule 1, Part 1, item 14, subsection 738Q(4)].***

5.13 Notification that an offer document is defective is critical because:

- it will trigger the intermediary's obligation to remove the offer document from the platform and will prevent further applications from being received under a defective offer document; and

- for applicants that have already applied for securities under the defective offer document, they will either be provided with a supplementary or replacement offer document that corrects the defect and be given one month to withdraw their acceptance, or the offer will close but not complete, which will mean applicants will not be issued with securities and will be refunded any application money paid.

5.14 In light of the above and to ensure that investors are basing their investment decisions on a compliant offer document, it is necessary to ensure that persons who are aware that an offer document is defective provide the relevant written notifications. This is achieved by providing that a person that fails to comply with their notification obligations commits a strict liability offence, punishable by a maximum penalty of 50 penalty units. ***[Schedule 1, Part 1, items 14 and 34, subsection 738V(4) and item 245J in the table to Schedule 3]***

Intermediary's obligation to suspend offer

5.15 Once an intermediary becomes aware that the offer document is defective, the intermediary must remove the offer document from its platform and either close the offer or suspend the offer, by giving notice on the offer platform that the offer is suspended ***[Schedule 1, Part 1, item 14, subsections 738N(6), 738X(1) and (2)].***

5.16 The offer will continue to be suspended until: the company provides a replacement or supplementary offer document that the intermediary publishes, in which case the offer will be 'open'; or the intermediary closes the offer (either pursuant to their general power to close an offer or because they are required to do so pursuant to their gatekeeper obligations).

5.17 The notice advising of the suspension must continue to appear on the offer platform for the entire time the offer is suspended and no applications may be received while the offer is suspended. ***[Schedule 1, Part 1, item 14, subsection 738X(3)]***

5.18 If the intermediary does not comply with their obligations to remove the offer document and either close or suspend the offer, or (where the offer is suspended) the notice that the offer is suspended does not appear on the offer platform at all times until the suspension ends, the intermediary will commit a strict liability offence, punishable by a maximum penalty of 50 penalty units. ***[Schedule 1, Part 1, items 14 and 34, subsection 738X(4) and item 245K in the table to Schedule 3]***

5.19 Imposing an obligation on the intermediary to remove the defective offer document and either close or suspend the offer is necessary to ensure that no further applications can be received in respect of a defective offer document. For a person that has already applied for the offer, the intermediary, by closing or suspending the offer, ensures that the applicant will not be issued with securities under the CSF offer unless the person receives a replacement or supplementary offer document that corrects the defect and is given one month within which to withdraw their application.

5.20 In light of the above, the fact that the penalty for the offence complies with the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* and the fact that exposure to the offence is entirely dependent on the conduct of the intermediary, the strict liability offence is considered to be appropriate.

When a company may prepare a supplementary or replacement offer document

5.21 The company can prepare a supplementary or replacement offer document in relation to an original CSF offer document in the following circumstances:

- where the original offer document is defective, to correct a defect in the original offer document;
- where the original offer document does not comply with the requirement that information contained therein be clear, concise and effective, and comply with any regulations, to correct the non-compliance; and
- in any other circumstances permitted by the regulations. ***[Schedule 1, Part 1, item 14, subsection 738W(1)]***.

5.22 A supplementary or replacement offer document cannot be provided in any other circumstance.

5.23 If the supplementary or replacement offer document is provided to correct a defective or otherwise non-compliant offer document, it must not incorporate any changes other than to correct the defect or non-compliance, unless this is permitted by the regulations. Where the regulations do permit other changes to be incorporated, the supplementary or replacement offer document must comply with any conditions imposed by the regulations. ***[Schedule 1, Part 1, item 14, subsection 738W(2)]***

5.24 The amendments set out certain requirements that replacement or supplementary offer documents must adhere to:

- at the beginning of the supplementary offer document there must be a statement that it is a supplementary offer document, an identification of the affected offer document it supplements and a statement that the supplementary and affected offer document are to be read together;

- at the beginning of the replacement offer document there must be a statement that it is a replacement offer document and a statement identifying the document it replaces. ***[Schedule 1, Part 1, item 14, subsections 738W(3) and (4)]***

5.25 The company will need to ensure that it obtains the relevant consents in relation to the replacement or supplementary offer document ***[Schedule 1, Part 1, item 14, paragraph 738W(6)(a)].*** 'Fresh' consents will be required for persons that are liable on the CSF offer document as a whole (such as directors and persons named as proposed directors). However, if a person had consented to a statement in the original offer document and the supplementary or replacement offer document does not make a material change to the form or context of that statement, the company will not need to obtain a 'fresh' consent from that person ***[Schedule 1, Part 1, item 14, subsection 738W(7)].***

5.26 Failure to obtain the relevant consents in relation to the supplementary or replacement offer document will mean the company will have committed the offence of failing to obtain the required consents prior to publication, which carries a maximum penalty of five penalty units. ***[Schedule 1, Part 1, item 34, item 245B in the table to Schedule 3]***

5.27 An intermediary that is provided with a supplementary or replacement offer document by the company is not obliged to publish the offer document. Non-publication could be due to the intermediary's 'gatekeeper' obligations which will apply to a supplementary or replacement offer document in the same way as they applied to the original offer document. ***[Schedule 1, Part 1, item 14, paragraph 738W(6)(b)]***.

5.28 If the document provided is a supplementary offer document that the intermediary decides to publish, it must publish the supplementary offer alongside the original offer document ***[Schedule 1, Part 1, item 14, paragraph 738W(5)(a)]***. Once the intermediary does so, the supplementary and original offer documents are taken to be the CSF offer document for anything that happens after the publication ***[Schedule 1, Part 1, item 14, subsection 738W(8)]***.

5.29 If the document provided to the intermediary is a replacement offer document that it decides to publish, the intermediary must only publish the replacement offer document ***[Schedule 1, Part 1, item 14, paragraph 738W(5)(b)]***. Once the intermediary does so, the replacement offer document (and not the original offer document) is taken to be the CSF offer document for anything that happens after its publication ***[Schedule 1, Part 1, item 14, subsection 738W(9)]***.

5.30 Once the intermediary publishes the supplementary or replacement offer document on its platform, the offer will be open again, which means that new applications can be received via the application facility.

Intermediary's obligation to notify existing applicants of withdrawal rights when the supplementary or replacement offer document is published

5.31 Once the supplementary or replacement offer document is published, the period of suspension ends and the intermediary must give written notice to all applicants that accepted the offer prior to its suspension that they have one month (from the date of the notice) in which to withdraw their acceptance and obtain a refund of application money paid ***[Schedule 1, Part 1, item 14, subsections 738X(5), 738X(6) and 738X(7)]***. Failure to provide the required notice will mean the intermediary will commit a strict liability offence, punishable by a maximum penalty of 30 penalty units ***[Schedule 1, Part 1, item 34, item 245L in the table to Schedule 3].***

5.32 Strict liability, and the level of penalty, is appropriate, because:

- persons that have applied for the offer have based their investment decision on a defective disclosure document and it is therefore important that they be notified of their right to withdraw from the offer;
- the notifications are entirely dependent on the conduct of the intermediary who is liable for the offence;
- the proposed penalty for the offence is consistent with the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* which specifies that a strict liability offence should be punishable by a maximum penalty of 60 penalty units with no term of imprisonment.

5.33 An applicant that wants to withdraw their acceptance must do so in writing within one month of receiving the notice from the intermediary ***[Schedule 1, Part 1, item 14, subsection 738X(9)]***. The intermediary must refund the application money of anyone who exercises their withdrawal rights as soon as practicable ***[Schedule 1, Part 1, item 14, paragraph 738T(1)(a) and subsection 738ZB(4)]***.

5.34 Once the suspension ends and the CSF offer is open, the usual rules covering when an offer is 'closed' and when it is 'complete' apply (refer Chapter 4 of the Explanatory Memorandum). If there is a further defect in the offer document, the offer may be suspended once more.

Intermediary's obligations if the company does nothing

5.35 When the company becomes aware that the offer document is defective, there is no obligation on the company to do anything other than notify the intermediary that the offer document is defective. The amendments do not require the company to, for example, withdraw the offer or prepare a replacement or supplementary offer document. Therefore, a company may do nothing once the offer is suspended.

5.36 However, even if the company does nothing once the offer is suspended, an intermediary may choose to close the offer (so long as this is in accordance with the hosting arrangement) ***[Schedule 1, Part 1, item 14, subsection 738N(3)]*** . Even if it does not choose to close the offer, there will come a point in time (no later than three months after the offer was first made) where the intermediary will be required to close the offer ***[Schedule 1, Part 1, item 14, paragraphs 738N(4)(a) and (b)]***. As the offer will be closed but not 'complete', the intermediary will be required to refund application money to applicants as soon as practicable after the offer is closed ***[Schedule 1, Part 1, item 14, paragraph 738N(4)(b)]***.

Liabilities relating to defective documents that are materially adverse from the perspective of an investor

5.37 Consistent with the approach applying to prospectuses and other existing disclosure documents, persons associated with the offer may be criminally liable or be exposed to action for recovery of loss or damage where the offer document is defective and the statement, omission or new circumstance which led to the document being defective is *materially adverse* from the point of view of an investor.

Criminal liability

5.38 A company that offers securities under a CSF offer document that is defective commits an offence if the statement, omission or new circumstance that caused the document to be defective is materially adverse from the point of view of an investor. ***[Schedule 1, Part 1, item 14, subsection 738Y(4)]***.

5.39 Likewise, an intermediary that publishes an offer document that it *knows* to be defective commits an offence if the statement, omission or new circumstance that caused the document to be defective is materially adverse from the point of view of an investor ***[Schedule 1, Part 1, item 14, subsection 738Y(4)]***. This means an intermediary will not commit an offence where the defect in the offer document is materially defective if the intermediary did not know the offer document was defective. For the purpose of determining what an intermediary knows, an intermediary is

taken to know all matters that they would have known had they conducted the prescribed checks to a reasonable standard ***[Schedule 1, Part 1, item 14, subsections 738Q(4) and 738Y(3)]***.

5.40 The penalty for a person that commits the offence is a maximum penalty of 300 penalty units, five years imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245M in the table to Schedule 3]***.

5.41 There are a number of defences that are available to a person who would otherwise be criminally liable. These are discussed at paragraphs 5.45 to 5.53.

Investor's right to recover for loss or damage

5.42 An investor that suffers loss or damage because of a defective document is able to recover the amount of the loss or damage from certain persons associated with the offer, including:

- the issuer and its directors, to the extent the loss or damage was caused by any part of the offer document;
- persons named, with their consent, in the offer document as proposed directors, to the extent of loss or damage caused by any part of the offer document;
- a person named in the offer document with their consent as having made a statement that is included in the CSF offer document or on which a statement made in the CSF offer document is based, to the extent of loss or damage caused by the inclusion of the statement in the CSF offer document;
- a person whose conduct resulted in, or was involved in, the offer document being defective, to the extent of loss or damage caused by that conduct;
- the intermediary that published the offer document to the extent the intermediary knew that the offer document was defective, to the extent of the loss or damage caused by any part of the offer document. ***[Schedule 1, Part 1, item 14, subsection 738Y(5)]***

5.43 For the purpose of determining what an intermediary knew about the offer document, the intermediary is taken to have known of anything that they would have known had they conducted the prescribed checks to a reasonable standard. ***[Schedule 1, Part 1, item 14, subsection 738Q(4)]***

5.44 An investor has six years from the day the cause of action arose in which to commence recovery proceedings. ***[Schedule 1, Part 1, item 14, subsection 738Y(6)]***

Defences against criminal liability and action for recovery of loss

5.45 The amendments set out the defences available to a person who would otherwise commit an offence or be liable for loss or damage in relation to a defective offer document. The defences are similar to those that are available in relation to certain existing disclosure documents. For these defences a defendant bears an evidential burden to point to evidence that suggests a reasonable possibility that the matter exists or does not exist. Once the defendant discharges this evidential burden, the prosecution must disprove these matters beyond reasonable doubt.

5.46 The evidential burden on the defendant is therefore fully consistent with the principle in the *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* which establishes the general rule that a defendant should only bear an evidential burden of proof for an offence-specific defence.

5.47 The first defence applies where a person did not know the offer document was defective ('lack of knowledge' defence). This defence is currently available in respect of offer information statements (but not in respect of prospectuses, which have a higher 'due diligence' threshold).

5.48 A company will not commit an offence where they did not know the offer document was defective ***[Schedule 1, Part 1, item 14, paragraph 738Z(1)(a)]***. The company bears the evidential burden of establishing that it did not know that the offer document was defective. This is appropriate as the company is best placed to raise evidence that they did not know the offer document was defective.

5.49 A person, other than an intermediary, who would otherwise be liable in respect of an action for recovery of loss or damage in relation to a defective offer document will not be liable if they did not know that the offer document was defective. This person bears the evidential burden of establishing that they did not know the offer document was defective as they are best placed to present the evidence required to demonstrate why they formed the view that the offer document was not defective.***[Schedule 1, Part 1, item 14, paragraph 738Z(1)(b) and subsection 738Z(2)]***

5.50 The 'lack of knowledge' defence is not available to the intermediary as the intermediary would anyway only be liable where it knew that the offer document was defective but continued to publish it ***[Schedule 1, Part 1, item 14, subsections 738Y(3) and 738Z(2)]***.

5.51 A second defence is available where the person placed 'reasonable reliance' on information given by another person, other than if that information was given by an employee, agent or (in the case of a company) a director ***[Schedule 1, Part 1, item 14, subsection 738Z(3)]***. The evidentiary burden for this defence rests on the person making the claim as they are best placed to demonstrate that they did in fact place reasonable reliance on information from someone else.

5.52 Consistent with the position in relation to existing disclosure documents, a person that performs a particular professional or advisory function will not be taken to be an agent of the body or individual ***[Schedule 1, Part 1, item 14, subsections 738Y(3) and 738Z(5)]***.

5.53 As is the case with the lack of knowledge defence, the 'reasonable reliance' defence is not available to the intermediary given the intermediary would only be liable where they *knew* the offer document was defective. ***[Schedule 1, Part 1, item 14, subsection 738Z(4)]***.

Withdrawal of consent — statements and omissions

5.54 A person who is named in a CSF offer document as being a proposed director or underwriter, or as making a statement included in the document, or making a statement on the basis of which a statement is included in the offer document, is not liable for loss or damage and does not commit an offence if they publicly withdrew their consent to being named in the document. ***[Schedule 1, Part 1, item 14, subsection 738Z(6)]***

5.55 A person making use of this defence has the evidentiary burden of demonstrating that they did in fact withdrew their consent publically as they would be best placed to be able to do this.

5.56 This defence is available in relation to existing Chapter 6D disclosure documents.

5.57 To make use of any of these defences, the relevant person will have to provide evidence as appropriate that they did not know that the offer document was defective, appropriately relied on information from another person or publicly withdrew consent to being referenced in the offer document. In each of these cases, it is appropriate that the person making use of the defence is required to raise the required evidence as they are the ones best placed to do so.

ASIC stop order powers

5.58 ASIC's stop order powers have been extended so that they apply where a company offers securities under a defective CSF offer document ***[Schedule 1, Part 1, item 15, paragraph 739(1)(d)]***. ASIC may order that no

offers, issues, sales or transfers of the securities are to take place while the order is in force ***[Schedule 1, Part 1, item 16, paragraph 739(1A)(a)]***.

Consequential amendments

5.59 Consequential amendments have been made to provide that the general rules prohibiting misleading and deceptive conduct in the Corporations Act do not apply in relation to a CSF offer document ***[Schedule 1, Part 1, item 30, subparagraph 1041H(3)(a)(iia)]***. This amendment means that defective CSF offers will be treated in the same way as existing Chapter 6D disclosure documents.

5.60 Corresponding consequential amendments have been made to provisions in the ASIC Act: section 12DA (prohibition on misleading or deceptive conduct) and section 12DB (prohibition on making false or misleading representations) to exclude these provisions from applying to CSF offer documents ***[Schedule 1, Part 2, item 37, subparagraphs 12DA(1A)(a)(iii) and 12DB(2)(a)(iii) of the ASIC Act]***. The carve out from these provisions in the ASIC Act is limited to CSF offer documents, the provisions will continue to apply to other misleading or deceptive conduct or false representations made by the issuer company or the intermediary.

5.61 Amendments have also been made to exclude the State Fair Trading Act of any State or Territory from applying to CSF offers made under a defective CSF offer document ***[Schedule 1, Part 1, item 31, subparagraph 1041K(1)(a)(iia)]***. This amendment means that CSF offer documents will be treated in the same way as existing Chapter 6D disclosure documents.

Chapter 6
Investor Protections

Outline of chapter

6.1 This Chapter sets out the investor protection provisions that are part of the CSF regime.

6.2 All legislative references within this Chapter are to the *Corporations Act 2001* unless specified otherwise.

Summary of new law

6.3 The amendments establish certain protections for all investors, with some additional protections applying to retail clients. These protections ensure that investors can make informed decisions and reduce the extent to which they may be subjected to excessive levels of risk under the new CSF regime.

6.4 The additional protections that apply to retail clients are:

- an investor cap of $10,000 per issuer via a particular intermediary within a 12-month period;
- unconditional cooling-off rights;
- a prohibition on providing financial assistance to enable investments in CSF offers; and
- the requirement to obtain a risk acknowledgment prior to accepting a CSF application.

6.5 The amendments restrict the advertising of CSF offers or intended CSF offers.

6.6 The existing prohibition on securities hawking may apply to certain offers of securities that are also the subject of a CSF offer.

6.7 The amendments make it an offence for a person to make an offer that is expressed as a CSF offer but that relates to a company that has not yet been formed or does not exist.

Comparison of key features of the new law and current law

New law	*Current law*
A CSF intermediary must reject an application from a retail investor that breaches the retail investor cap of $10,000 per issuer company via the intermediary's platform within a 12-month period.	No equivalent.
A CSF intermediary must reject an application from a retail investor where the investor has not completed the risk acknowledgment.	No equivalent.
A retail investor has an unconditional right to withdraw from a CSF offer within 48 hours of making the application.	No equivalent.
The company making the CSF offer and its related parties, and the CSF intermediary that hosts or intends to host a CSF offer and its associates, cannot financially assist or arrange financial assistance for a retail investor to acquire securities under a CSF offer.	No equivalent.
A person can advertise or publish a statement in relation to a CSF offer or intended CSF offer so long as the advertisement or statement complies with the advertising rules.	A person can advertise or publish a statement in relation to an offer of securities or intended offer requiring disclosure so long as the advertisement or statement complies with the advertising rules.
A person must not make an offer expressed as a CSF offer in relation to a company that has not been formed or does not exist.	A person must not make an offer of securities that needs disclosure under Part 6D.2 in relation to a company that has not been formed or does not exist.

Detailed explanation of new law

6.8 The CSF regime contains certain investor protections that apply only to an investor treated as a retail client in relation to the CSF offer.

Protections for retail clients

6.9 For the purposes of the CSF regime, a retail client for the purpose of a CSF offer is defined in the same way as a retail client for the

purpose of a crowd-funding service ***[Schedule 1, Part 1, item 14, section 738D]***. Paragraphs 3.21 to 3.24 explain when a person will be treated as a retail client in relation to a crowd-funding service.

Investor caps

6.10 The Bill establishes a $10,000 cap as the maximum amount a retail client can invest in relation to CSF offers by a particular issuer via the same intermediary within a 12-month period to limit a retail investor's exposure to a single company. The amount of the cap can be adjusted by regulations. ***[Schedule 1, Part 1, item 14, subsection 738ZC(1)]***

6.11 The investment cap is applied as an obligation on a CSF intermediary to reject an application from a retail client where it would otherwise breach the cap. When assessing whether the cap would be breached, the intermediary should only take account of investments made on its offer platform and not investments made in the issuer company via other platforms.

6.12 It is expected that CSF intermediaries will have the necessary systems to ensure that amounts invested by retail investors are appropriately tracked so that an application from a retail client that would exceed the cap is rejected. Where an application is rejected because it would otherwise breach the cap, the intermediary must refund application money to the investor as soon as practicable ***[Schedule 1, Part 1, item 14, paragraph 738ZB(4)(b)].***

Example 6.1: Investor caps

On 2 January of the current year, Donna makes an application to invest $9,000 in a CSF offer by New Tech Ltd via Value Add Pty Ltd, a licensed CSF intermediary.

New Tech's CSF offer is successful and the company decides to make a second CSF offer 6 months later using the Value Add platform again. Donna was very happy with her investment in New Tech and decides to participate in their second offer.

On 5 July Donna attempts to make an investment of $5,000 in New Tech but is unable to complete the application on the Value Add platform. This is because the $5,000 allocation would take her total investment in New Tech via the Value Add platform beyond the $10,000 cap within 12 months.

6.13 The Bill provides rules relating to the investor cap if two or more people make a joint application for securities. Where there are joint applicants, each of the applicants is taken to have made an individual application for the purposes of calculating the amounts contributing to

each applicant's investor cap. The amount each of the applicants is considered to have invested is determined by dividing the total amount invested under the joint application by the total number of applicants. ***[Schedule 1, Part 1, item 14, subsection 738ZC(2)]***

6.14 If the amount being attributed to each applicant under a joint application would result in any one of the individual applicants exceeding their investor cap, the CSF intermediary must reject the joint application and refund the application money. There is a regulation-making power to allow the default rules relating to joint applications to be amended by regulation. ***[Schedule 1, Part 1, item 14, subsection 738ZC(2)]***

6.15 An intermediary that does not reject an application by a retail client, which leads to a breach of the investor cap, commits an offence punishable by a maximum penalty of 30 penalty units. ***[Schedule 1, Part 1, item 14, subsection 738ZC(1) and item 34, item 245Q in the table to Schedule 3]***

6.16 In the case of a prosecution related to this offence, the defendant would bear an evidential burden for establishing that the investor was not a retail client in relation to the CSF offer ***[Schedule 1, Part 1, item 23, subsection 761G(8)].*** Imposing the evidential burden on the defendant is necessary and appropriate to ensure investors that are retail clients are provided with the additional investor protections, such as the investor cap, provided to retail clients under the CSF regime.

6.17 There are no penalties for a retail client that makes, or purports to make, an application that exceeds the investor cap.

Cooling-off rights

6.18 The Bill provides all retail clients who make an application in relation to a CSF offer with an unconditional right to withdraw their application within 48 hours of it being made ***[Schedule 1, Part 1, item 14, subsection 738ZD(1)]***

6.19 The cooling-off rights provide retail clients with time to reconsider their decision to invest and allow the investor to withdraw their application in the event they no longer wish to proceed with the investment.

6.20 The investor must exercise their cooling-off rights in accordance with the method specified by the intermediary. ***[Schedule 1, Part 1, item 14, subsection 738ZD(2)]***

6.21 The intermediary is required to display information regarding the retail investors' statutory cooling-off rights prominently on the offer platform including the means by which an investor can exercise those rights ***[Schedule 1, Part 1, item 14, subsection 738ZA(8)]***. These requirements are discussed in paragraphs 3.70 to 3.71.

6.22 Where an investor exercises their cooling-off rights, the intermediary must refund their application money as soon as practicable. ***[Schedule 1, Part 1, item 14, paragraph 738ZB(4)(a)]***

Example 6.2: Exercise of cooling-off rights

Eric applies to invest $7,000 in a CSF offer by AlphaBeta Ltd via the Value Add Pty Ltd CSF platform at 10:00 am on 20 April. He thinks about his decision to invest and at 9:00 am on 21 April he decides that he has changed his mind and wants to withdraw his application.

Eric can withdraw as he is within the 48 hours withdrawal period but he must indicate his withdrawal to Value Add in accordance with the instructions they have provided on their platform.

Example 6.3: Exercise of cooling-off rights on a public holiday

Bec also applies to invest $4,000 in the same CSF offer by AlphaBeta Ltd at 5:30 pm on 23 April. She decides at 1:00 pm on 25 April that she wants to withdraw her application.

Bec is able to withdraw her application as she is within the 48 hour withdrawal period even though 25 April is ANZAC Day and a public holiday across Australia. She will have to withdraw the application in accordance with the instruction provided on the platform. The platform operator will have to ensure that the withdrawal can be made even though it is a public holiday. 6.23 Intermediaries will also have to have appropriate mechanisms to ensure that potential investors can access their withdrawal rights in the event of technical or other problems with the platform, including unavailability for routine maintenance.

Prohibition on the provision of financial assistance

6.23 The Bill prohibits the following persons from providing financial assistance or arranging to provide financial assistance to a person that is a retail investor:

- a company making the CSF offer or intended offer (an offer that is yet to be made);
- related parties of the company;

- a CSF intermediary that is hosting or intending to host the CSF offer; and
- any associates of the CSF intermediary. ***[Schedule 1, Part 1, item 14, subsections 738ZE(1) and (2)]***.

6.24 The amendments define who is taken to be a related party of the company (refer to paragraphs 2.45 to 2.49). An 'associate' of an intermediary is determined in accordance with sections 10 to 17.

6.25 The Bill confirms that the prohibition applies whether the financial assistance was provided before or after the acquisition of securities under the offer and also covers financial assistance provided in the form of a dividend ***[Schedule 1, Part 1, item 14, subsection 738ZE(3)].*** The Bill provides that the terms 'financially assist' and 'financial assistance' have the same meanings as they do for section 260A of the Act ***[Schedule 1, Part 1, item 14, subsection 738ZE(4)].***

6.26 Contravention of the prohibition is an offence, punishable by a maximum penalty of 300 penalty units, five years imprisonment, or both. The term of imprisonment is consistent with the penalty applicable under section 260A. The penalty of 300 penalty units has been calculated based on the fine/imprisonment ratio of 5:1 specified in the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* (section 3.1.3 of the Guide refers). ***[Schedule 1, Part 1, item 34, item 245R in the table to Schedule 3]***

Protections applying to all investors

Advertising restrictions

6.27 The Bill provides for a general prohibition on advertising CSF offers except in certain circumstances.

6.28 The purpose of the advertising rules is to protect investors by ensuring they make informed decisions regarding the merits of a CSF offer based on the information contained in the CSF offer document rather than advertisements.

6.29 Issuers and intermediaries are permitted to advertise CSF offers as long as the advertisement or publication complies with the rules set out in the Bill.

Scope of the advertising prohibitions

6.30 The advertising restrictions apply to advertisements of CSF offers and intended CSF offers (offers that are yet to be made). ***[Schedule 1, Part 1, item 14, paragraph 738ZG(1)(a)]***

6.31 The advertising restrictions also apply to statements that refer to CSF offers or intended offers (whether directly or indirectly) or statements that are reasonably likely to induce people to apply for securities under a CSF offer or intended offer. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(1)(b)]***

When a statement will be taken to indirectly refer to a CSF offer or to reasonably induce investors to apply

6.32 In determining whether a statement indirectly refers to a CSF offer or intended offer, or is reasonably likely to induce investors to apply for securities offered under a CSF offer or intended offer, the Bill provides that regard must be had to three factors:

- whether the statement is part of normal advertising directed at maintaining or attracting customers ***[Schedule 1, Part 1, item 14, paragraph 738ZG(3)(c)];***
- whether the statement contains information that deals with the affairs of the body publishing the statement ***[Schedule 1, Part 1, item 14, paragraph 738ZG(3)(d)];*** and
- whether an investor would likely be encouraged to invest in the securities on the basis of the statement rather than the CSF offer document ***[Schedule 1, Part 1, item 14, paragraph 738ZG(3)(e)]***.

Not within scope of the advertising restrictions

6.33 The advertising restrictions do not apply to the publication of a CSF offer, CSF offer document, or any other information relating to a CSF offer that is on the platform of the intermediary ***[Schedule 1, Part 1, item 14, subsection 738L(4) and paragraph 738ZG(2)(a)]***. In the absence of this carve out, the intermediary would be required to include a statement that a person should, in deciding whether to make an application under the offer, consider the CSF offer document and general CSF risk warning (refer to paragraphs 6.40 to 6.43). However, it would be unnecessary to include a statement directing a person's attention to the offer document and the general CSF risk warning given, in order to read the statement, the person would already have to be viewing the offer platform which would itself already display the CSF offer document and general CSF risk warning.

6.34 However, the Bill provides that statements made on a communication facility, even where the communication facility is part of the offer platform, will remain subject to the advertising restrictions ***[Schedule 1, Part 1, item 14, subsection 738ZG(2)]***. There is a separate exception to the advertising rules that applies for statements made in good faith on the communication facility, discussed at paragraphs 6.52 to 6.57.

6.35 The advertising restrictions do not apply to advertisements or publications that do not refer to particular CSF offers or intended offers and that do either or both of the following:

- identify a person as a CSF intermediary;
- provide general information about the intermediary's CSF services. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(2)(b)]***

6.36 This exclusion from the advertising restrictions is to permit the intermediary to advertise its intermediation services.

Exceptions to the advertising restrictions

6.37 The Bill sets out some exceptions to the advertising restrictions that are consistent with the exemptions available in relation to advertising other types of offer documents under chapter 6D of the Act. ***[Schedule 1, Part 1, item 14, section 738ZG(4)]***

6.38 A person relying on one of these exemptions has an evidential burden of pointing to the relevant evidence that suggests a reasonable possibility that the matters required under an exemption exists. Once the defendant discharges this evidential burden, the onus is on the prosecution to disprove the matters beyond reasonable doubt.

6.39 This approach is consistent with the principle in the *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* which establishes the general rule that a defendant should only bear an evidential burden of proof for an offence specific defence. In this case, the person seeking to use one of the exemptions to the restrictions on the publication of CSF offers is required to bear an evidential burden in showing that the specific exemption applies.

Advertisement includes a statement that a person must, in deciding whether to invest in the CSF offer, consider the CSF offer document and risk warning

6.40 An advertisement or publication will not contravene the advertising restrictions where the advertisement or publication includes a statement that a person should, in deciding whether to make an application

under the offer, consider the CSF offer document and general CSF risk warning. ***[Schedule 1, Part 1, item 14, subsection 738ZG(6)]***

6.41 A person relying on this exemption has the evidential burden of demonstrating that their statement complies with the requirements to fall within the exemption as they are best placed to provide this evidence. The same requirements apply whether the advertisement is in relation to an open CSF offer (one where the CSF offer document has been published) or an intended offer. This is different to how advertisements relating to offers of an unlisted company are treated: an advertisement made before the disclosure document has been lodged with ASIC is subject to stricter controls regarding what can be included in the advertisement than an advertisement made after the disclosure document has been lodged (paragraph 734(5)(b) compared with subsection 734(6)).

6.42 The rationale for relaxing some of the advertising restrictions applying to intended offers is that the CSF regime builds in certain investor protections, for example, that applications can only be made via the platform of an intermediary that is required to prominently display important information for investors (such as the CSF offer document and risk warning). The regime also provides additional protections for retail investors (such as the unconditional cooling-off rights).

6.43 Where the advertisement or publication does not include the required statement (and no other exceptions apply), the person advertising or publishing the statement will commit an offence (refer to paragraphs 6.64 to 6.66).

Exception for publishers

6.44 Media businesses that publish an advertisement in the ordinary course of their business are not subject to the advertising restrictions. The exception only applies if the media business does not know and does not suspect that the publication would breach the advertising restrictions. ***[Schedule 1, Part 1, item 14, subsection 738ZG(7)]***

6.45 The exception only applies in relation to media businesses that are newspapers, magazines, radio and television broadcasters, and their electronic equivalents. ***[Schedule 1, Part 1, item 14, subsection 738ZG(10)]***

6.46 A publisher relying on this exemption will bear the evidentiary burden in this case as the exemption relies on their state of mind.

6.47 The exception also extends to news reports or other genuine comment in the media that refer to a CSF offer document that is published on an intermediary's platform, information in such an offer document and information that is contained in certain other permitted reports. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(c)]***

6.48 It is appropriate for the person claiming the defence to bear the evidential burden as they are best placed to point to the source of the information used. Reports about securities of the company making the CSF offer or intended offer that are published by an *independent* third party are also an exception to the advertising restrictions. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(d)]***

6.49 An entity will be considered an independent third party if it is: not the company making the CSF offer; not acting for that company; not a director of the company; not the CSF intermediary hosting the offer; and not anyone else who has an interest in the success of the issue of the securities. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(d)]***

6.50 An entity will not be considered independent if they receive consideration or any other benefit for the publication that contravenes the advertising restrictions. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(d)]***

6.51 In this case, it is appropriate that the person making the publication bear the evidential burden as they are best placed to demonstrate their independence from the company making the CSF offer. An advertisement or publication not covered by this exception will contravene the advertising restrictions (unless another exception applies) and the person advertising or publishing the statement will commit an offence (refer to paragraphs 6.64 to 6.66).

Statements made in good faith on the communication facility

6.52 This exception to the advertising restrictions is to enable statements to be made on the communication facility for a CSF offer as long as the statement is made in good faith. ***[Schedule 1, Part 1, item 14, subsection 738ZG(8)]***

6.53 The evidential burden of demonstrating that the statement was made in 'good faith' falls on the person making the statement. This is appropriate as the person making the statement is best placed to raise evidence as to why the statement was made in good faith, given it could at least in part involve some inquiry as to the person's state of mind and knowledge.

6.54 In the absence of this exception, any person (including a prospective investor) making a statement on the communication facility would be required to include, in addition to their statement, a statement

that a person, in deciding whether to make an application pursuant to the CSF offer, should consider the CSF offer document and general CSF risk warning. If the person failed to include the required statement, they would breach the advertising restrictions and commit a strict liability offence, punishable by a maximum penalty of 30 penalty units.

6.55 As it would be impracticable to require every person using the communication facility to include the required statement every time they made a statement on the facility, the amendments create an exception for statements made in good faith on the communication facility, by any person (including the issuer company or intermediary). ***[Schedule 1, Part 1, item 14, subsections 738ZG(1) and (8)]***

6.56 A statement not made in good faith would not be covered by this exception. The evidential burden of demonstrating that the statement was made in 'good faith' falls on the person making the statement. This is appropriate as the person making the statement is best placed to raise evidence as to why the statement was made in good faith, given it could at least in part involve some inquiry as to the person's state of mind and knowledge.

6.57 Where the person is unable to show the statement was made in good faith, the person will commit an offence (refer to paragraphs 6.64 to 6.66).

Exceptions for certain reports and notices

6.58 This exception is to enable the publication of certain notices and reports relating to a company making a CSF offer.

6.59 The exception enables the publication of a notice or report of a general meeting of a company making a CSF offer. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(a)]***

6.60 . In this case, it is appropriate that the person making the publication bears the evidentiary burden of showing that it consists solely of a notice or report of the company's general meeting as that person is best placed to have records of the meeting and know the circumstances surrounding the meeting.

6.61 The exception also covers reports about the company that are published as long as the reports do not contain material information about the company that is not included in the CSF offer document or annual report and do not actually refer to the CSF offer. ***[Schedule 1, Part 1, item 14, paragraph 738ZG(9)(b)]***

6.62 The person making the publication is best placed to bear the evidential burden in these circumstances as they are best placed to point to the source of information previously made public by the company.

6.63 An advertisement or publication not covered by this exception will contravene the advertising restrictions (unless another exception applies) and the person advertising or publishing the statement will commit an offence (refer to paragraphs 6.64 to 6.66).

Consequences of contravening the advertising restrictions

6.64 A person that advertises or publishes a statement in contravention of the advertising restrictions commits a strict liability offence, punishable by a maximum penalty of 30 penalty units ***[Schedule 1, Part 1, item 14, subsection 738ZG(5) and item 34, item 245T in the table to Schedule 3]***.

6.65 Strict liability is appropriate because of the importance of ensuring that investors applying for CSF offers do so after forming a view of the merits of the CSF offer, based on the information contained in the CSF offer document and having regard to the general CSF risk warning. This is particularly important given CSF investments will be high risk (given the relatively high failure rate of start-ups and small businesses).

6.66 The penalty of 30 penalty units complies with the Government's *Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* as it is below the recommended maximum penalty of 60 penalty units and does not include a term of imprisonment.

Prohibition on hawking securities

6.67 Section 736 prohibits a person from offering securities for issue (or sale) in the course of, or because of, an unsolicited meeting or telephone call. The prohibition on securities hawking in Part 6D.3 is an important safeguard against a person being pressured into acquiring securities without potentially having all of the information to make an informed decision or the benefits of the protections offered under the CSF regime.

6.68 The prohibition has not been specifically amended to apply to CSF offers because CSF offers can only be made via an intermediary's platform. Nevertheless, it is possible for the securities hawking prohibition to apply to securities under a CSF offer where the offer actually made in the course of the unsolicited meeting or telephone call is *not* expressed to be made as a CSF offer. In such cases, the offer will not be a CSF offer and *will*, therefore, be covered by the securities hawking prohibition in section 736.

6.69 Where the person offering the securities does so in a way that the offer is expressed as a CSF offer (and the offer is eligible to be made as a CSF offer), the prohibition on securities hawking will not apply (refer to paragraph 2.10). However, as the CSF offer would have been made otherwise than on the platform of an intermediary, the rules regarding how a CSF offer must be made (refer Chapter 4 of the Explanatory Memorandum) will have been contravened, which is an offence.

Offering securities of a company that does not exist

6.70 The amendments prohibit a person from making an offer expressed as a CSF offer in relation to a company that has not been formed or that does not exist ***[Schedule 1, Part 1, item 14, section 738ZF].*** This is comparable to the rule in section 726, which makes it an offence for a person to offer securities in a body that has not been formed or that does not exist where the offer requires disclosure under Part 6D.2. Section 726 does not apply to a CSF offer as a CSF offer is not an offer requiring disclosure under Part 6D.2, which is why these amendments create a new offence.

6.71 The offence carries a maximum penalty of 300 penalty units, five years imprisonment, or both ***[Schedule 1, Part 1, item 34, item 245S in the table to Schedule 3]***.

ASIC stop order powers

Defective advertising of CSF offers

6.72 ASIC's stop order powers have been extended so that they apply where an advertisement or publication for a CSF offer or intended offer is defective because there is a misleading or deceptive statement in the advertisement, or the advertisement does not include the required statement advising that a person should, in considering whether to apply for the offer, consider the CSF offer document and general CSF risk warning ***[Schedule 1, Part 1, items 15, 18 and 19, paragraph 739(1)(f), subsection 739(6) and paragraph 739(6)(c)]***.

6.73 Where the advertisement is defective, ASIC may order may that the relevant conduct specified in the stop order must not be engaged in. ***[Schedule 1, Part 1, item 17, paragraph 739(1A)(b)]***

Offers expressed as, but not eligible to be, CSF offers

6.74 The amendments extend ASIC's stop order powers so that they apply to offers expressed to be made as CSF offers but that are not eligible to be made as CSF offers. ***[Schedule 1, Part 1, item 15, paragraph 739(1)(g)]***

6.75 ASIC may order that no offers, issues, sales or transfers of the securities are to take place while the order is in force. ***[Schedule 1, Part 1, item 16, paragraph 739(1A)(a)]***

Consequential amendments

6.76 A consequential amendment has been made to one of the exceptions to the existing advertising restrictions in Part 6D.3 to add CSF offer documents. The consequential amendment is intended to cover the situation where a company has made both a CSF offer and an offer requiring disclosure under Chapter 6D. A reference to both offers in a report of the company could breach both the advertising restrictions in the CSF regime as well as the existing restrictions applying to advertising of disclosure documents. The effect of the consequential amendment is that a report about a company that does not contain material information about the company that has not previously been included in a Chapter 6D disclosure document *or a CSF offer document* and that does not refer to the offers will not contravene the existing advertising restrictions in Part 6D.3. ***[Schedule 1, Part 1, item 13, subparagraph 734(7)(c)(i)]***

6.77 Consequential amendments have been made to subsection 1018A(4). The subsection sets out the general exceptions to advertising restrictions applying to financial products. An existing exception for reports by the issuer where information was previously made available in a disclosure document lodged with ASIC has been extended to include CSF offer documents. An exception for news reports, or genuine comment, in the media relating to information contained in a disclosure document lodged with ASIC has been extended to include CSF offer documents. ***[Schedule 1, Part 1, items 28 and 29, subparagraphs 1018A(4)(c)(i) and 1018A(4)(d)(i)]***

Chapter 7
Corporate Governance Concessions

Outline of chapter

7.1 This Chapter sets out the temporary concessions from certain public company corporate governance and reporting requirements available to a new public company that is eligible to crowd fund and has completed or intends to complete a CSF offer within the required time.

7.2 Unless otherwise stated, all references in this Chapter relate to the *Corporations Act 2001*.

Context of amendments

7.3 As the CSF regime is only available to public companies, it will exclude start-ups and other small-scale enterprises that do not adopt a public company structure. Restricting the CSF regime in this way could potentially reduce the number of companies using the CSF regime and consequently substantially reduce the effectiveness of the regime.

7.4 To address this, the Bill creates temporary concessions from certain public company corporate governance and reporting requirements for new public companies limited by shares and proprietary companies that convert to a public company that satisfy the CSF eligibility criteria at the time of registration as a new public company and at the end of the relevant financial year, and that complete a CSF offer within the required timeframe. The purpose of the concessions is to reduce the barriers to adopting a public company structure.

7.5 The corporate governance concessions are only available to companies that register as, or convert to, a public company *after* the commencement of the CSF regime. This is to ensure that public companies currently subject to the public company requirements do not reduce their reporting or governance standards.

Summary of new law

7.6 A company that is registered as, or that converts to, a public company limited by shares after the commencement of the CSF regime will be eligible for the corporate governance and reporting concessions.

7.7 The concessions are only available to companies that are eligible and intend to crowd fund at the time they are registered and that successfully complete a CSF offer within 12 months of registration or conversion, and have not undertaken any fundraising offers requiring disclosure.

7.8 The corporate governance and reporting concessions apply for a maximum of five years from the date of registration as, or conversion to, a public company limited by shares. The concessions are:

- an exemption from needing to hold an Annual General Meeting (AGM) under the usual rules;
- the option to only provide financial reports to shareholders online; and
- the company not being required to appoint an auditor or have audited financial reports until more than $1 million has been raised from CSF offers.

Comparison of key features of new law and current law

New law	*Current law*
A company that is registered as, or converts to, a public company limited by shares after the commencement of the CSF regime and that satisfies the eligibility criteria is eligible for certain corporate governance and reporting concessions for up to five years.	No equivalent.
A company that is eligible for the corporate governance and reporting concessions is not required to hold an AGM under section 250N.	Under section 250N, a public company must hold an AGM each year.

New law	*Current law*
A company that is eligible for the corporate governance and reporting concessions is only required to provide financial reports to shareholders online.	A public company may provide financial reports to shareholders: by hard copy or email (where the shareholder has made an election to receive the reports in this way); by making the report readily accessible on a website; or by directly notifying, in writing, all persons that did not make an election as to how to receive the report, the website at which the reports may be accessed.
A company that is eligible for the corporate governance and reporting concessions is not required to appoint an auditor or have audited financial reports until more than $1 million has been raised from CSF offer or other offers requiring disclosure.	A public company must appoint an auditor within one month of registration and its financial reports must be audited each year.

Detailed explanation of new law

7.9 The concessions are only available to a company that registers as a public company, or converts to a public company, after the commencement of the CSF regime. In order to be eligible to claim the concessions, the company must satisfy certain eligibility criteria on registration as or conversion to a public company limited by shares and at the end of the financial year in which it is claiming the concession.

Must be eligible on registration or conversion

7.10 In order to be eligible for the concessions, a newly registered company limited by shares must indicate, on its application for registration, that it will satisfy the requirements to be an eligible CSF company (Chapter 2 of the Explanatory Memorandum) on registration and that it intends to make a CSF offer after registration within the next twelve months ***[Schedule 2, item 1, paragraph 117(2)(mc)]***.

7.11 Similarly, a proprietary company that converts to become a public company limited by shares is only eligible for the concessions if they make a statement that they satisfy the requirements to be an eligible CSF company on conversion and they intend to make a CSF offer within 12 months of conversion. ***[Schedule 2, item 2, paragraph 163(2)(d)].***

7.12 A company that gives misleading information about its intention to make a CSF offer will commit an offence under section 1308 of the Act.

7.13 A company that does not indicate the above in its application for registration or conversion will be ineligible for the concessions.

Must be eligible at end of financial year

7.14 The company must determine its eligibility to claim the concessions at each financial year end.

7.15 A company is eligible for the concessions for a particular year where it satisfies the following criteria:

- it is an eligible CSF company at the end of the financial year;
- it has, in its application for registration or conversion, indicated that it will be an eligible CSF company on registration or conversion and that it intends to make a CSF offer;
- the current financial year ends within five years of the date of the company's registration;
- where the current financial year ends more than 12 months since registration or conversion, the company has successfully completed a CSF offer;
- either it is the company's first financial year, or where it is not the company's first financial year, the company has been eligible for the concessions in relation to every earlier financial year; and
- the company has not made any offers of securities for issue or sale that need disclosure under Chapter 6D.2 since they started accessing these corporate governance concessions.
  [Schedule 1, Part 1, item 14, section 738ZI]

Must complete a CSF offer within 12 months of registration

7.16 The requirement that the company complete a CSF offer within 12 months of registration as, or conversion to, a public company limited by shares is intended to ensure the concessions are targeted to companies that use the CSF regime.

7.17 Recognising that it will take some time for a newly formed company to complete a CSF offer, the company has a period of 12 months from registration as, or conversion to, a public company limited by shares within which to successfully complete a CSF offer.

7.18 The offer must be complete within the 12-month period. A company that makes a CSF offer that is open at the end of the 12 month period will not be eligible for the CSF corporate governance concessions even if the offer subsequently successfully completes.

7.19 Likewise, if the company makes a CSF offer that closes but does not 'complete' (for example, because the minimum subscription condition is not met), the company will be ineligible to claim the concessions.

7.20 While the companies described in paragraphs 7.13, 7.18 and 7.19 will not be eligible for the public company corporate governance and reporting concessions outlined in paragraphs 7.21 to 7.40, they may still be eligible to make a CSF offer, subject to satisfying the relevant eligibility criteria (refer to Chapter 2 of the Explanatory Memorandum).

Concession 1: Relief from holding an AGM

7.21 If the financial year end for the company is within 18 months of the date of registration, or conversion, the company does not need to hold an AGM if it satisfies the requirements to claim the public company concessions at the end of the financial year. ***[Schedule 2, item 3,subsection 250N(5)]***

7.22 For all subsequent financial years, the company does not need to hold an AGM if it satisfies the requirements to claim the public company concessions at the end of that financial year. ***[Schedule 2, item 3, subsection 250N(6)]***

7.23 The policy rationale for providing relief from having to hold an AGM is that, while AGMs serve a purpose in the general engagement process between companies and their shareholders and are a mechanism for accountability of those in control of the company, holding an AGM poses practical difficulties and costs for start-ups and other small-scale enterprises. The concession, therefore, is intended to reduce the burdens associated with holding an AGM for a limited period. Notwithstanding the company will not be required to hold an AGM under section 250N, the directors may still be required to call a general meeting under other circumstances (for example, pursuant to subsection 249D(1), on the request of members with at least 5 per cent of the votes that may be cast at the general meeting).

Concession 2: Relief from preparing audited annual financial reports

7.24 Public companies must have their financial reports audited (sections 295 to 297). However, recognising the compliance burden that can arise for a newly formed public company (particularly where it has converted from a proprietary company where audited financial reports are not required), a company can elect not to have audited financial reports where:

- they satisfy the general eligibility criteria to claim the concessions (paragraph 7.15); and
- as at the end of the current financial year, the company has raised less than $1 million from all CSF offers. ***[Schedule 2, item 6, subsection 301(5)]***

7.25 Recognising that the obligation to have audited financial reports provides an important safeguard for investors, the exemption from having audited financial reports ceases at the earlier of: five years from the date of registration as, or conversion to, a public company; or when the company raised more than $1 million from CSF offers. The cap is based on offers made at any time — the $1 million cap does not reset every year.

Relief from appointing an auditor

7.26 As the Bill provides an exemption from the requirement to prepare audited financial reports, the Bill exempts the directors of a company from needing to appoint an auditor within one month of registration where the following requirements are satisfied:

- on registration, or conversion, the company satisfied the general eligibility criteria to claim the concessions (paragraph 7.15). ***[Schedule 2, item 17,at the end of subsection 327A(1A))]***

7.27 As public companies that meet these eligibility requirements are not required to hold an AGM, the obligation under section 327B to appoint an auditor at an AGM will not be triggered. Similarly, as these public companies do not have an obligation to have audited statements, the obligation to appoint an auditor to fill a casual vacancy under section 327C is also not triggered.

7.28 However, the directors of public companies that lose access to the corporate governance concessions (for example by not successfully undertaking a CSF offer within 12 months or at the end of the five year concession period) will be required to appoint an auditor within 1 month of the company losing its access to the corporate governance concessions unless an auditor has been appointed at a general meeting. ***[Schedule 2, item 18, section 328C(1)]***

7.29 An auditor appointed in this way will hold office until the company's first annual general meeting. The normal rules relating to the appointment of auditors in sections 327B to 327E will apply after this. ***[Schedule 2, item 18, section 328C(2)]***

7.30 Once a public company loses access to the concessions, its directors must take reasonable steps to ensure an auditor is appropriately appointed. A failure by the directors to do this is an offence which carries a maximum penalty of 25 penalty units, 6 months' imprisonment or both. The penalty mirrors the existing penalty for a public company where the directors fail to appoint an auditor within one month of being required to. ***[Schedule 2, item 18, section 328C(3) and Schedule 2, item 19, item 116MC in Schedule 3]***

7.31 A similar requirement to appoint an auditor is in place for a public company that raises more than $1 million from CSF offers. This company will lose its access to the exemption from having audited financial statements (paragraph 7.24) and its directors will therefore be required to appoint an auditor within 1 month of this occurring. A failure by the directors to do this is an offence which carries a maximum penalty of 25 penalty units, 6 months' imprisonment or both. The penalty mirrors the existing penalty for a public company where the directors fail to appoint an auditor within one month of being required to. ***[Schedule 2, item 18, section 328D and Schedule 2, item 19, item 116MD in Schedule 3]***

7.32 A company that loses its concession from having audited financial statements because it has raised more than $1 million from CSF offers will still have access to the other corporate governance concessions until it is no longer eligible for them.

7.33 As these companies will not be required to hold an AGM, the normal rules relating to the appointment of an auditor at a public company's AGM under section 327B does not automatically apply. To

address this, a replacement provision has been introduced that replicates section 327B.

7.34 Under this new provision, an auditor appointed to a public company that loses its concession from having audited financial statements because it has raised more than $1 million from CSF offers will hold office until the auditor dies, is removed from office or conflict of interest situations arise. These rules mirror the existing provisions that apply in relation to auditors of public companies under section 327B. ***[Schedule 2, item 18, section 328E]***

7.35 Changes to and obligations in relation to appointing replacement auditors can occur in accordance with the existing provisions relating to auditors in sections 327C — 327F. Where there is a need to appoint a new auditor this will be done by the directors of the company until the next AGM (which may be a few years away if the other corporate governance concessions still apply to the company).

Concession 3: Annual financial reports only to be provided online

7.36 Public companies must provide a financial report, directors' report and auditor's report to shareholders each year. The company must, on at least one occasion, directly notify each shareholder in writing that they may elect to receive the reports in either hard or electronic copy free of charge and, if they do not so elect, they may access the reports on a specified website.

7.37 The requirement to notify shareholders of the options to receive the annual reports and to provide the reports in the format elected by the shareholder may impose significant costs on a start-up or small-scale enterprise.

7.38 The Bill provides that a company that satisfies the general eligibility criteria to claim the concessions (paragraph 7.14) at the end of the financial year only needs to provide its annual reports via a website and does not need to notify shareholders of alternative ways of receiving the reports. ***[Schedule 2, items 7 and 8, subsections 314(1) and 314(1AF)]***

7.39 A similar amendment has also been made to enable a company that qualifies for the concessions to provide its concise financial report to shareholders by making the report available on a website. ***[Schedule 2, item 9, subsection 314(2A)]***

7.40 Consequential amendments have been made to the content requirements of the annual directors' report. The amendments provide that a company that claims the audit concessions is not required to include

a copy of the auditor's declaration in its directors' report. ***[Schedule 2, items 4 and 5, subsections 298(1AA) and 298(1AC)]***

Consequential amendments

7.41 Consequential amendments have been made to the notes under subsection 324CA(1A), subsection 324CB(1A), subsection 324CC(1A), subsection 324CE(1A), subsection 324CF(1A), subsection 324CG(1A) and subsection 324CG(5A) to indicate that the appointment of an auditor for a public company with crowd-sourced funding will be terminated in circumstances where the auditor notifies ASIC of conflict of interest situations unless a second notice under section 328E is provided in 21 days. This consequential amendment is necessary to ensure section 328E mirrors section 237B. ***[Schedule 2, items 10-16, notes under subsection 324CA(1A), subsection 324CB(1A), subsection 324CC(1A), subsection 324CE(1A), subsection 324CF(1A), subsection 342CG(1A) and subsection 324CG(5A)]***

Chapter 8
Exemptions from regulatory requirements relating to Australian Market Licences and clearing and settlement facility licences

Outline of chapter

8.1 This Chapter sets out the new exemption powers that can be used to provide for a more tailored regulatory regime to facilitate the operation of specialised and emerging financial markets and clearing and settlement facilities, including in relation to CSF securities.

8.2 All legislative references within this Chapter are to the *Corporations Act 2001* unless specified otherwise.

Context of amendments

8.3 Currently, under Part 7.2 of the Act, any person that falls within the definition of operating a financial market is required to obtain an Australian Market Licence (AML) or seek an exemption from the Minister. The Minister has the power to exempt a market from the operation of Part 7.2 in full, but does not have the power to provide a partial exemption from particular requirements under the regime.

8.4 The AML regime was designed to address the risks associated with the operation of traditional exchanges (such as the Australian Securities Exchange) or other significant financial markets and imposes obligations commensurate with the nature and risks of those financial markets. The full suite of obligations may not be as appropriate for operators of emerging or specialised financial markets such as crowd-sourced funding (CSF) intermediaries.

8.5 Generally, requiring these types of market operators to obtain an appropriately modified AML may ensure that they have adequate arrangements to meet their obligations and to provide the market environment expected by persons participating in the market.

8.6 Amending the AML framework to provide the Minister with the power to exempt certain market operators from specified obligations would ensure that the AML regime could be tailored to particular markets. The exemption power could be used to facilitate the development of emerging and specialised markets, including CSF intermediaries.

8.7 To be able to effectively tailor the regulatory obligations to suit emerging or specialised financial markets, similar partial exemption powers are required in relation to Parts 7.2A, 7.3 and 7.5 of the Act.

8.8 Part 7.2A provides for Australian Securities and Investments Commission (ASIC) supervision of financial markets. Some or all of these requirements may not be suitable for all emerging and specialised financial markets. Similarly, Part 7.5 requires AML holders to maintain compensation arrangements designed for public markets but that may not be appropriate for other types of financial markets.

8.9 Part 7.3 provides for the licensing of clearing and settlement facilities. The definition of clearing and settlement is wide and could apply to emerging or specialised financial markets and their operators owing to some incidental activities they perform as part of operating a financial market. These include transferring money between the trading accounts of investors. Like Part 7.2, some of the requirements imposed by Part 7.3 may not be appropriate for such incidental activities.

8.10 As such, providing the Minister with enhanced powers to exempt some emerging and specialised financial markets — such as intermediaries operating facilities for secondary trading in CSF interests — from some or all of the requirements in parts 7.2, 7.2A, 7.3 and 7.5 would provide for a more effective, efficient and flexible regulatory regime.

8.11 The ability to offer more tailored regulation of financial markets and clearing and settlement facilities, and their operators would provide a more agile framework that would facilitate innovation in and the development of new types of funding mechanisms, including CSF.

Summary of new law

8.12 The Bill provides the Minister with additional exemption powers to provide financial markets and clearing and settlement facilities, and their operators, with exemptions from specified parts of the AML and clearing and settlement facility licensing regimes.

8.13 The Bill amends the existing exemption power under Part 7.2 of the Act to provide the Minister with the power to exempt a financial market or class of financial markets, or their operators, from some of the AML regulatory requirements under Part 7.2 of the Act. The existing exemption power only allows for a full exemption from holding an AML.

8.14 An identical exemption power is also being introduced into Part 7.2A of the Act so that the Minister can exempt a financial market or class of financial markets, or their operators, from some or all of the obligations relating to ASIC supervision under Part 7.2A of the Act. This is a new exemption power that exactly mirrors the amended exemption power being introduced into Part 7.2 of the Act.

8.15 The existing exemption power in Part 7.3 of the Act is being amended to provide the Minister with the power to exempt a clearing and settlement facility or class of clearing and settlement facilities, or their operators, from some of the clearing and settlement facility licensing requirements under Part 7.3 of the Act. The current exemption power only allows for a full exemption from needing a licence for operating a clearing and settlement facility.

8.16 An identical exemption power is also being introduced into Part 7.5 of the Act so that the Minister can exempt a financial market or class of financial markets, or their operators, from some or all of the compensation arrangement requirements under Part 7.5 of the Act. This is a new exemption power that exactly mirrors the amended exemption power being introduced into Part 7.2 of the Act.

8.17 The introduction of these four identical exemption powers creates a streamlined approach to granting some emerging or specialised financial markets and clearing and settlement facilities, and their operators, with exemptions from some of the regulatory requirements in Parts 7.2, 7.2A, 7.3 and 7.5 of the Act to provide for a more tailored regulatory approach.

Summary of key features of new law and current law

New law	*Current law*
The Minister may exempt a financial market or class of financial markets, or their operators, from some of the AML requirements.	The Minister may exempt a financial market or class of financial market from all of the AML requirements.

New law	*Current law*
The Minister can exempt a financial market or class of financial markets, or their operators, from some or all of the obligations relating to ASIC supervision.	No equivalent.
The Minister may exempt a clearing and settlement facility or class of clearing and settlement facilities, or their operators, from some of the clearing and settlement facility licensing requirements	The Minister may exempt a clearing and settlement facility or class of clearing and settlement facility from all the clearing and settlement facility licensing requirements
The Minister can exempt a financial market or class of financial markets, or their operators, from some or all of the compensation arrangement requirements.	No equivalent.

Detailed explanation of new law

8.18 The Bill provides for changes in the exemption powers in Parts 7.2, 7.2A, 7.3 and 7.5 of the Act. The changes provide a more flexible and appropriate regulatory regime for emerging and specialised financial markets and their operators.

Exemptions from AML obligations

8.19 The Bill repeals the exemption power in existing section 791C of the Act and replaces it with an amended exemption power. ***[Schedule 3, item 1, section 791C]***

8.20 The new amended exemption power largely replicates the existing power being replaced but provides greater flexibility in allowing the Minister to provide an exemption from specified obligations under Part 7.2 of the Act (as opposed to only being able to provide a complete exemption from the AML regime). The changes will offer more tailored regulation for financial markets and their operators. ***[Schedule 3, item 1, subsection 791C(1)]***

8.21 The exemption can be applied in relation to a particular market or a particular class of markets. Where an exemption is made in relation to a class of financial markets, then the exemption is a legislative instrument and is subject to disallowance and sunsetting, consistent with the existing exemption power. ***[Schedule 3, item 1, subsection 791C(4)]***

8.22 Where an exemption applies in relation to a particular market, an exemption is not a legislative instrument and the Minister is required to publish a notice of the exemption in the Gazette ***[Schedule 3, item 1, subsection 791C(5)]***. This is the same approach as is currently provided for in the existing exemption power.

8.23 The new exemption also replicates the Minister's powers to vary or revoke an exemption after providing notice and providing affected market operators with the opportunity to make submissions. The only change to these requirements is that notice of a change to an exemption relating to a class of financial markets must be published on the ASIC website instead of a newspaper. ***[Schedule 3, item 1, subsections 791C(2) and (3)]***

8.24 The new amended exemption power has also been rewritten to reflect modern drafting requirements.

8.25 As the existing exemption is being repealed to be replaced with the amended exemption, a savings provision has been introduced to ensure that all exemptions made prior to the change continue to operate. ***[Schedule 3, item 2]***

Exemptions from ASIC supervision

8.26 The Bill provides the Minister with a new power to exempt a particular financial market or a class of financial markets from ASIC supervision under Part 7.2 of the Act. ***[Schedule 3, item 3, section 798M]***

8.27 This new exemption power operates identically to the amended exemption power being introduced into Part 7.2 of the Act (refer to paragraphs 8.19 to 8.25 for a detailed description of how the power operates).

8.28 There is already a broad regulation making power under section 798L of the Act to exempt financial markets or types of financial markets from ASIC supervision under Part 7.2A of the Act.

8.29 The new exemption power is being introduced despite the existence of the regulation making power so that a consistent approach can be taken in providing a more tailored regulatory regime for emerging and specialised financial markets and their operators. Under this approach, where relevant, the Minister can exempt a financial market or class of financial markets, or their operators, from obligations relating to ASIC supervision in the same way that these markets can be given an exemption from the AML requirements in Part 7.2 of the Act.

Exemptions from clearing and settlement licensing obligations

8.30 The Bill repeals the exemption power in existing section 820C of the Act and replaces it with an amended exemption power. ***[Schedule 3, item 4, section 820C]***

8.31 The change to the exemption power is identical to the change being made to the exemption power in Part 7.2 of the Act (see paragraphs 8.19 to 8.25 for a detailed description of how the power operates).

8.32 The main change to the provision is, therefore, to give the Minister the power to exempt a clearing and settlement facility or class of clearing and settlement facilities from part of the clearing and settlement licensing regime ***[Schedule 3, item 4, subsection 820C(1)].***

8.33 The changes will offer more tailored regulation for clearing and settlement facilities and their operators. The new exemption also replicates the Minister's powers to vary or revoke an exemption, with the required notice now able to be provided on the ASIC website rather than in a newspaper ***[Schedule 3, item 4, subsections 820C(2) and (3)]***.

8.34 The new amended exemption power has also been rewritten to reflect modern drafting requirements.

8.35 As the existing exemption is being repealed to be replaced with the amended exemption, a savings provision has been introduced to ensure that all exemptions made prior to the change continue to operate. ***[Schedule 3, item 5]***

Exemptions from compensation regime requirements

8.36 The Bill provides the Minister with a new power to exempt a particular financial market or a class of financial markets from the compensation arrangement requirements under Part 7.5 of the Act. ***[Schedule 3, item 6, section 893B]***

8.37 This new exemption power operates identically to the amended exemption power being introduced into Part 7.2 of the Act (see paragraphs 8.19 to 8.25 for a detailed description of how the power operates).

8.38 There is already a broad regulation making power under section 893A of the Act to exempt financial markets or types of financial markets from the compensation arrangements requirements under Part 7.5 of the Act.

8.39 The new exemption power is being introduced despite the existence of the regulation making power so that a consistent approach can be taken in providing a more tailored regulatory regime for emerging and specialised financial markets and their operators. Under this approach, where relevant, the Minister can exempt a financial market or class of financial markets from some of the compensation arrangement requirements in Part 7.5 of the Act in the same way that these markets can be given an exemption from the AML requirements in Part 7.2 of the Act.

Application and transitional provisions

8.40 These amendments will take effect from the day after the Bill receives Royal Assent. This is before the CSF regime commences because the changes will have application to other emerging or specialised market operators in addition to CSF intermediaries.

8.41 These amendments will take effect from the day after the Bill receives Royal Assent. This is before the CSF regime commences because the changes will have application to other emerging or specialised market operators in addition to CSF intermediaries.

Chapter 9
Regulation impact statement

1. WHAT IS THE PROBLEM THAT NEEDS TO BE ADDRESSED?

1.1 REGULATORY BARRIERS TO CSEF

9.1 Crowd-sourced equity funding (CSEF) is an innovative type of online fundraising that allows a large number of individuals to make small financial contributions towards a company, in exchange for an equity stake in the company. It has the potential to provide finance for innovative business ideas that may struggle to attract funding under traditional models.

9.2 However, there currently exists a range of regulatory impediments to the use of CSEF. These include governance and reporting requirements for companies, equity fundraising rules and requirements for financial intermediaries as set out in the Corporations Act 2001 ('Corporations Act'). These are described in more detail in Section 1.4.

9.3 While these arrangements exist to protect and promote the interests of market participants, including investors, each has the effect of increasing the regulatory burden and cost of fundraising through CSEF. The overall cost of conducting a CSEF offer under current equity fundraising laws is prohibitively expensive, as the amount of funds raised through CSEF is typically smaller than through other equity fundraising activities. Current regulatory settings are therefore constraining development of the CSEF market in Australia.

9.4 A number of other jurisdictions including New Zealand, the United States, the United Kingdom and Canada (Ontario) have already, or are in the process of, implementing regulatory regimes for CSEF. The introduction of an appropriate regulatory framework that would facilitate CSEF in Australia would ensure that Australia remains responsive to the funding needs of innovative businesses.

9.5 Productivity growth is a core driver of economic growth. Fostering innovation is an important way of unlocking productivity, both through innovative products and ways of doing things, and through generating knowledge spillovers from research and development that add to the general level of knowledge in the economy. New funding models

that flexibly support emerging firms — including CSEF — have the potential to facilitate innovation and contribute to productivity growth.

9.6 A number of recent reviews have identified the potential of CSEF to provide new and innovative businesses with access to the finance they need to develop their product or service and grow.

- The Government's Industry Innovation and Competitiveness Agenda, released in October 2014, called for consultation on a regulatory framework for CSEF. The Government's Innovation and Science Agenda is putting in place measures to support technology, research and start-ups and ensure that the Australian economy is more innovative and agile. This includes ensuring that finance is available to facilitate innovative activity.

- The Murray Inquiry into Australia's financial system, released by the Government in December 2014, specifically recommended reducing regulatory impediments to crowdfunding by introducing graduated fundraising regulation. In its response to the Inquiry, released in October 2015, the Government accepted this recommendation.

- The Productivity Commission's *Business Set-up, Transfer and Closure* draft report, released in May 2015, also supported the introduction of a CSEF framework.

9.7 There are three main stakeholders groups with an interest in the development of a framework to remove the regulatory impediments to CSEF:

- Companies seeking to raise funds stand to benefit from the establishment of a CSEF framework. This is particularly the case for innovative firms and start-ups, which typically have more difficulty obtaining bank debt finance than established firms, but for whom existing equity fundraising is prohibitively expensive. These companies would be *issuers* of CSEF offerings.

- Individuals seeking new opportunities to invest stand to benefit from the increased range of financial products that CSEF would present. These individuals would be able to diversify the range of products they invest in, and would be *investors* in CSEF offerings.

- A number of organisations are seeking to establish and operate a platform that allows issuers to list their CSEF offerings, bringing together issuers and potential investors. These organisations would operate as *intermediaries* in the CSEF market.

1.2 THE NEED TO IMPROVE ACCESS TO FINANCE FOR SMALL AND INNOVATIVE BUSINESSES

9.8 Access to finance is crucial for innovative new businesses, particularly those that are creating a new product or service or significantly improving an existing product or service. Innovative developments often require costly research and development in the early stages of a business at a time when there may be little or no revenue flowing in.

9.9 Obtaining affordable finance to fund development of innovative new products is difficult in some cases. As part of its 2013 small business election commitments, the Government committed to improving small businesses' access to affordable finance to ensure they have the opportunity to establish and develop.

9.10 Difficulties in accessing debt finance can arise as a result of gaps in information between lenders and borrowers. As the provision of debt finance requires an assessment of a business' ability to service the debt, small businesses and start-ups that do not have adequate evidence of past performance or prospects for success can face particular challenges accessing credit. Lenders may not be willing to bear the cost of obtaining detailed credit-related information to assess the level of risk involved in lending to a smaller business. Some businesses may also struggle to obtain finance from lenders due to insufficient collateral being offered in the event of default.

9.11 However where a bank loan can be obtained, it may not be well suited to the business. Bank loans involve regular repayments starting almost immediately, and failure to meet these payments risks default of the loan. In reality the cash flows of small businesses, particularly start ups, can be volatile, making it difficult to meet such regular repayments.

9.12 Equity finance may therefore be a more suitable option than debt for some businesses. Unlike debt finance, equity does not require immediate repayments and equity investors generally accept that returns are contingent on profits.

1.3 THE ROLE OF CSEF

9.13 In recent years, a number of innovative financing mechanisms have emerged that draw on the crowd to expand the funding options available to small businesses including peer-to-peer lending, rewards based crowdfunding and equity and debt crowdfunding. These mechanisms complement more established financing options offered by professional investors focused on start-up businesses such as angel investing and venture capital.

9.14 If appropriately regulated, CSEF may improve the ability of small businesses to access equity finance.

9.15 For small businesses, CSEF could be more useful than traditional equity markets as the compliance costs involved in traditional equity fundraising can be relatively expensive compared to the amount of funds that a small business would generally seek to raise. These compliance costs could absorb a significant proportion of any funds raised, reducing the utility of the fundraising for the small business or start-up.

9.16 Facilitating CSEF in Australia has the potential to provide a competing source of funds for small businesses, reducing their reliance upon bank debt and, potentially, at the margin driving down the cost of finance for small businesses overall. CSEF may be particularly beneficial for the types of businesses that find bank finance more difficult to obtain, such as start ups and other firms with innovative products.

9.17 Facilitating CSEF would also provide additional investment opportunities to retail investors, who are generally unable to be directly involved in early stage financing activities, such as angel investing, due to the size of investment required. CSEF would allow for retail investors to broaden their range of investments and to become involved in funding products and services that interest them.

9.18 However, start ups generally present higher risks for investors compared to more established companies, particularly those listed on public exchanges, and retail investors would likely face the same information gaps as those faced by lenders. CSEF investments may also be largely illiquid, reducing the ability of investors to exit their investment and may be at greater risk of dilution from later capital raisings than investments in larger companies.

9.19 Current disclosure and corporate governance arrangements, outlined in section 1.4, seek to address information asymmetries between investors and managers of companies. However, the compliance costs associated with these obligations can be prohibitive for small businesses

and start ups seeking to raise funds in a way they are not for larger, more established companies that have ready access to public equity offers.

9.20 Addressing some of these costs via a CSEF framework may make CSEF a viable fundraising option. However, in order for CSEF to be sustainable, any regulatory framework needs to balance reducing the current barriers to CSEF with ensuring that investors continue to have an adequate level of protection from financial and other risks, including fraud, and sufficient information to allow investors to make informed investment decisions. While establishing a regime that works for issuers and intermediaries will be an important precursor to the success of CSEF, a high failure rate, an illiquid secondary market, or large investor losses in the early stages may result in investors losing confidence in CSEF as an investment mechanism.

9.21 Options 1, 2, and 4 outlined below seek to strike such a balance between reducing some of the disclosure and corporate governance obligations and putting in place other protections for retail investors.

1.4 CURRENT REGULATORY ARRANGEMENTS

9.22 Governance and reporting requirements for companies, equity fundraising rules and requirements for financial intermediaries are set out in the Corporations Act.

9.23 These requirements have over time been implemented to address the inherent conflicts of interest in corporations in which the owners of the company, that is the shareholders ('principal') and managers of the company ('agent') are separate. As the agent typically has better information than the principal about the company, the principal cannot easily be assured of the performance of the agent ('agency costs').

9.24 The law provides a number of mechanisms to minimise these agency costs such that companies are directed and controlled in a manner that protects and promotes the interests of participants. These mechanisms differ between the two broad categories of companies provided for in the Corporations Act: public companies and proprietary companies.

9.25 Public companies are able to make public equity offers and are not subject to restrictions on the number of shareholders they may have. Public companies are subject to a range of reporting and corporate governance obligations to protect shareholders and address agency costs, including:

- Auditors who assist in the monitoring of managers by attesting to the accuracy of companies' financial statements.

- A board of directors, each of whom has fiduciary duties to act with reasonable care and diligence, in the interests of the company, and for a proper purpose.

- Disclosure of information by companies allows shareholders to properly monitor managers and directors. Obligations such as annual financial reports, prospectus (or offer information statements in some cases) and continuous disclosure obligations seek to address the asymmetry in access to information regarding the operation and prospects of a company that exists between the managers and the owners. This information is used to determine whether a person wishes to become, remain or exit from being a shareholder of a company.

- Annual general meetings, which provide a forum for shareholders to be informed about financial and other matters, ask questions of management and make decisions relating to matters that need to be considered.

- Members' rights to call a meeting, undertake litigation against the company and vote when resolutions are put forward by the company.

9.26 There are also a range of requirements in relation to the contents of disclosure documents, the process for making equity offers, liability for misleading statements in offer documents and restrictions on advertising to ensure the disclosure is clear, effective and reliable.[1]

9.27 Proprietary companies are intended to be closely-held companies where the shareholders have access to the management and consequently information asymmetries and agency costs are likely to be lower than in more widely-held public companies. Proprietary companies are therefore subject to reduced compliance and transparency obligations, relative to public companies. Proprietary companies are defined as either

1 Corporations Act, Chapter 6D.

small proprietary companies[2] or large proprietary companies[3], with small proprietary companies having lower compliance obligations than large proprietary companies.

9.28 To ensure they reflect this closely-held nature, proprietary companies are prohibited from making public offers of equity[4] and are limited to having no more than 50 non-employee shareholders.

9.29 For both public and proprietary companies, there are certain exemptions from the requirement to use a disclosure document in primary capital raisings. These exemptions include wholesale (professional, sophisticated and experienced) investors (who are less likely to suffer from information asymmetries) and 'small scale personal offers' (where a personal offer is made and no more than $2 million is raised in any 12-month period from no more than 20 Australian investors, to facilitate small capital raisings that may not occur if a disclosure document were required).[5]

9.30 As at March 2015, approximately 99 per cent of all registered Australian companies were proprietary companies. There were approximately 2,188,000 proprietary companies (the vast majority likely to meet the definition of small proprietary company) and approximately 22,100 public companies.

9.31 Entities that meet the definition of carrying on a financial services business, including CSEF intermediaries, must hold an Australian Financial Services Licence (AFSL) and comply with AFSL licensing obligations.[6] AFSL holders are subject to a range of obligations, including ensuring the financial services are provided efficiently, honestly and fairly, having in place adequate arrangements to manage conflicts of interest, having adequate financial, technological and human resources, and membership of an external dispute resolution scheme where the licensee provides services to retail clients.[7] Licensees may also be subject

2 Corporations Act, s45A(2) defines a small proprietary company as a proprietary company with at least two of: consolidated financial revenue of less than $25 million; consolidated gross assets of less than $12.5 million; and fewer than 50 employees.

3 Corporations Act, s45A(3) defines a large proprietary company as a proprietary company with at least two of: consolidated financial revenue of $25 million or greater; consolidated gross assets of $12.5 million or greater; and 50 or more employees.

4 Corporations Act, s113(3), subject to exceptions for offers to existing shareholders and employees of the company or subsidiary. Proprietary companies may make offers where that offer would not require disclosure under Chapter 6D.

5 Corporations Act, s708.

6 Under s761A of the Corporations Act, carrying on a financial services business is defined as providing a financial service. Provision of a financial service is defined in s766A.

7 Corporations Act, s912A.

to additional specific conditions on their licence. Licensees or their authorised representatives are generally also required to give retail clients a Financial Services Guide, which must meet certain content requirements.[8]

9.32 Entities that fall within the definition of conducting a financial market[9], possibly including some CSEF intermediaries, must also hold an Australian Market Licence (AML) and comply with the AML licensing obligations. The AML regime is designed to address the risks associated with large public exchanges (such as the ASX) and imposes considerable obligations on holders, including cost recovery requirements, market integrity rules and ongoing ASIC supervision.

9.33 Investors are not generally subject to legislated limits on the amount they can invest in public equity raisings, although issuers conducting initial public offers may decide of their own accord to limit the size of investment parcels or scale back applications where the target raising has been exceeded.

9.34 Investors have certain rights to withdraw their application before the closing of an equity offer where a condition included in the disclosure document has not been met, the disclosure document included a misleading or deceptive statement, or there has been a material adverse change in the circumstances of the issuer.[10]

1.5 REVIEW OF CSEF

9.35 Consideration of CSEF and whether it could be facilitated in Australia was referred to the Corporations and Markets Advisory Committee (CAMAC) in June 2013. CAMAC considered the potential of CSEF in Australia and the limitations preventing development of a CSEF regime under current conditions, and reported back in June 2014.

9.36 While CSEF has potentially large benefits to fundraisers and, potentially, investors, CAMAC identified significant regulatory barriers to the development of CSEF platforms in Australia. CAMAC also noted that CSEF platforms may be required to hold an AML.

9.37 CAMAC identified prohibitions on proprietary companies making public offers of equity as a factor preventing CSEF. This

8 Corporations Act, Division 2, Part 7.7.

9 As defined in the Corporations Act, s767A. Under s911A(2)(d), an intermediary that is a holder of an AML is not required to also hold an AFSL.

10 Corporations Act, s724.

prohibition means that, even with the wholesale and small scale personal offer exemptions, proprietary companies are not able to access the large number of small scale investors that would typically be targeted under a CSEF campaign. The 50 non employee shareholder cap for proprietary companies also limits the scope for small companies to raise funds from a large number of investors.

9.38 While operating under a public company structure may avoid these issues, this would come with increased costs and reporting and corporate governance obligations that may be too expensive to be an option for small businesses. Public companies making equity offers must use a prospectus (or an information statement in some cases) where they are not eligible for an exemption. Disclosure documents can be costly and time consuming to prepare, and small businesses may not be able to use equity for fundraising as a result.

9.39 Overall, CAMAC formed the view that CSEF should be facilitated in Australia for public companies, but that existing legislation created a barrier. CAMAC recommended that a regulatory regime for CSEF be developed, as has been done in several overseas jurisdictions, so that equity fundraising may become available to a wider range of public companies.

2. WHY IS GOVERNMENT ACTION NEEDED?

9.40 The main barriers to widespread use of CSEF in Australia that CAMAC identified are regulatory in nature. These barriers are not easily able to be addressed by potential CSEF participants.

9.41 There are currently a small number of operators of online platforms offering investment in Australian start ups. Under current legislation, none of the platforms are able to make their services available to all investors. Instead, they offer their services either only to wholesale investors via a managed investment scheme, or utilise the small scale personal offer exemption and an Australian Securities and Investments Commission (ASIC) class order that provides relief from certain regulatory requirements.[11] The platforms also do not offer secondary trading.

9.42 While this environment may be suitable for some companies and investors, it does not comprehensively address the barriers to CSEF in

11 ASIC Class Order 02/273: Business Introduction or Matching Services.

Australia and in particular, does not allow offers to be made to, or traded by, the 'crowd'.

3. POLICY OPTIONS ORIGINALLY CONSIDERED?

9.43 Following CAMAC's recommendation and the Industry Innovation and Competitiveness Agenda's recommendation, the Government consulted with the public, industry stakeholders and other Australian Government departments on potential regulatory frameworks to facilitate CSEF in Australia for public companies.

9.44 Due to the existing restrictions on proprietary companies making public equity offerings and the cap of 50 non-employee shareholders for these companies, the Government consulted only on options to facilite CSEF for public companies.

9.45 On 8 December 2014, the Government released a public discussion paper on potential models to facilitate CSEF. Three options were included in the discussion paper to elicit stakeholder feedback and draw out the key elements of any potential model that may continue to present a barrier to effective facilitation of CSEF.

- Option 1: a regulatory framework based on the CAMAC model;
- Option 2: a regulatory framework based on the New Zealand model; and
- Option 3: the status quo.

9.46 The discussion paper noted that the Government had not made a final decision on its preferred CSEF framework, and was not limiting itself to implementing either the CAMAC or New Zealand models in full. Instead, feedback from the consultation process was to assist the Government in developing its preferred approach to CSEF.

9.47 The three options were chosen for consultation as they represent a spectrum of approaches to CSEF. The model recommended by CAMAC draws on an extensive review of approaches implemented or proposed to be implemented by foreign jurisdictions, with a focus on reducing public company compliance costs and minimising risks to investors. As outlined in section 3.2, the model implemented by New Zealand takes a different approach to that of CAMAC in a number of key areas, including public company compliance costs, companies eligible to use CSEF, investor limits and certain intermediary requirements. The

status quo option was included as a baseline against which to compare regulatory options, consistent with the Government's requirements for regulation impact statements.

9.48 The terminology used to refer to the various participants in CSEF reflects that used in CAMAC's report:

- Issuer: a business registered as a company under the Corporations Act that wishes to offer its equity through an online intermediary;
- Intermediary: an online platform that allows businesses to offer their equity to crowd investors, subject to the requirements of the Corporations Act; and
- Investor: a member of the crowd seeking to invest in a CSEF issuer.

3.1 OPTION 1: CAMAC MODEL

9.49 Option 1 involves the implementation of a CSEF regime based on CAMAC's recommendations. CAMAC recommended the development of a separate legislative framework for CSEF to make it easier for CSEF to be used in Australia.

9.50 CAMAC recommended that CSEF issuers be required to be public companies. A new category of public company — the 'exempt public company' — would be created and would be relieved of some of the compliance requirements for public companies for a period of up to three to five years. Such companies would be exempt from requirements for continuous disclosure, holding an annual general meeting, executive remuneration reporting, half yearly reporting, and appointing an independent auditor and having a financial report audited (unless they have raised up to $1 million via CSEF or any other prospectus exemption and cumulative expenses of $500,000). On expiry of the audit exemption, the issuer would be required to have the financial accounts for all previous years it was subject to the exemption audited. CAMAC's recommendations focused on the Corporations Act, and it did not propose any changes to any other legislation, including to the tax treatment of exempt public companies.

9.51 CAMAC's proposed framework for CSEF fundraising includes:

- for issuers: limitation of the regime to certain small enterprises that have not already raised funds under the existing public offer arrangements, limitation of the regime to one class of fully paid ordinary shares, reduced disclosure

requirements, a cap of $2 million on the amount that can be raised through CSEF in any 12-month period (excluding funds raised under existing exemptions from the need to provide a prospectus to certain wholesale investors), restrictions on advertising of the equity offer and prohibitions on conflicts of interest;

- for intermediaries: requirements for intermediaries to have an AFSL including membership of an external dispute resolution scheme, requirements to undertake limited due diligence and provide risk warnings to investors, provisions to prevent certain conflicts of interest, prohibitions on offering investment advice and on lending to CSEF investors, provision of communications facilities on its website for each issuer; and

- for investors: investment caps of $2,500 per investor per 12-month period for any particular CSEF issuer and $10,000 per investor per 12-month period in total CSEF investment, signature of risk acknowledgement statements prior to investment and cooling off and other withdrawal rights.

Further details on CAMAC's recommendations are included at Appendix, Section 9.1.

3.2 OPTION 2: NEW ZEALAND MODEL

9.52 Option 2 involves the implementation of the CSEF model that came into force in New Zealand in April 2014. New Zealand's Financial Markets Authority issued the first financial licence to a CSEF platform in July 2014, with the first CSEF raising completed in mid September 2014.

9.53 New Zealand's model has some broad similarities to CAMAC's proposed scheme, including:

- limitation of the regime to one class of fully paid ordinary shares;

- a cap of $2 million on the amount that can be raised through CSEF disclosure relief in any 12-month period inclusive of any fundraising via the New Zealand equivalent of the small scale personal offer exemption but excluding investments by wholesale investors;

- requirements for intermediaries to be licensed and belong to an external dispute resolution scheme, undertake limited due diligence checks and provide disclosure statements and risk warnings to investors; and

- investors must sign a risk acknowledgement statement.

9.54 Differences in the New Zealand model compared to CAMAC's recommended framework include:

- no CSEF-specific exemptions from public company compliance costs such as financial reporting and audit;

- the regime is not specifically limited to small enterprises;

- there are minimum disclosure requirements and investment caps are voluntary, with issuers and intermediaries to have in place arrangements to provide greater disclosure where there are no or high voluntary investor caps or the issuer is seeking to raise a significant amount of funds;

- there are no restrictions on intermediaries' fee structures, although fees paid by the issuer must be disclosed; and

- intermediaries are able to invest in issuers using their platform, although details of any investments must be disclosed.

3.3 OPTION 3: STATUS QUO

9.55 Under option 3, there would be no change to the current requirements under the Corporations Act for proprietary companies, public companies and for public fundraisings. These include:

- the limit of 50 non-employee shareholders for proprietary companies, and prohibitions on making public offers of equity, subject to certain exemptions, including the small scale personal offer exemption;

- financial reporting and corporate governance requirements for public companies that are more onerous than those that apply to proprietary companies; and

- the requirement to provide a disclosure statement when making public offers of equity.

9.56 Intermediaries would remain subject to a number of existing requirements, including:

- the need to hold an AFSL and comply with AFSL licensing obligations if they meet the definition of carrying on a financial services business, or to hold an AML and comply with AML licensing obligations if they fall within the definition of conducting a financial market; and

- if a managed investment scheme (MIS) structure is used to facilitate online equity offers, the intermediary would need to comply with MIS requirements, including having a responsible entity that is a public company with an AFSL, disclosure and compliance obligations.[12]

9.57 Under this option, CSEF would not be regulated as a specific form of investment. Small businesses and start ups seeking to raise early stage capital would need to comply with the above existing requirements.

4. GOVERNMENT CONSULTATION ON CSEF MODELS

9.58 Stakeholder feedback was sought on the Government's discussion paper via the Treasury website.[13] This invitation was communicated to individual stakeholders who requested to be kept up to date as part of the Industry Innovation and Competitiveness Agenda consultation process. In addition, the then Minister for Small Business wrote to 26 known stakeholders across the start-up, venture capital, crowdfunding and legal sectors. Written submissions were sought by 6 February 2015.

9.59 Supplementing this process, targeted consultation was conducted by the then Minister for Small Business, who hosted industry roundtables on 2 February and 16 February 2015 in Sydney and Melbourne, respectively.

9.60 The purpose of these consultations was to seek stakeholder feedback that would help to inform the Government's decision to develop a CSEF framework and its design. These decisions required the

12 Corporations Act, Chapter 5C sets out specific requirements in relation to managed investment schemes.

13 See: http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Crowd-sourced-Equity-Funding

Government to balance facilitating CSEF with maintaining appropriate investor protection and minimising the compliance burden. Roundtable meetings with stakeholders provided forums for the Minister to discuss the detailed elements of a desirable legislative model and better understand the views and concerns of parties directly affected.

9.61 Forty-one written submissions were received in response to the discussion paper. Submissions were received from a broad range of stakeholders including crowdfunding platform operators, advisory and legal firms, industry bodies and public organisations, universities, individuals, a financial service provider and ASIC. Twenty-eight stakeholders participated in the industry roundtables. Treasury also held eight bilateral meetings, predominantly with stakeholders who attended the roundtables or have an interest or experience in crowdfunding. Treasury also held teleconference bilateral meetings with financial conduct regulators in New Zealand and the United Kingdom to gain insight into how crowdfunding has developed in those markets following implementation of their regulatory frameworks.

9.62 Stakeholder feedback from these processes expressed support for a regulatory crowdfunding model, with consensus amongst the above stakeholder groups that the legislative and regulatory barriers identified by CAMAC make it costly and impractical for small businesses to access CSEF. Stakeholders agreed that a framework should be light-touch, giving investors the ability to invest and diversify their investments. The view that the Government should ensure issuers and all investors have access to a minimum standard of information to make informed decisions was also shared.

9.63 There was limited consensus on a range of design elements, including the appropriateness of the investor cap thresholds, the role of issuers regarding disclosure and the role and associated remuneration structure of intermediaries under the CAMAC model. Targeted consultation meetings and bilateral discussions raised alternative design elements.

9.64 While a diverse range of views were received on CAMAC's 'exempt public company' proposal, stakeholders generally considered this to be unnecessary for facilitating CSEF in Australia. While this structure would relieve the regulatory and compliance requirements associated with being a public company, stakeholders noted it would also increase the complexity of the Australian regulatory regime, particularly for smaller businesses, and it would still be too burdensome to become a public company given the amount of finance that is typically raised. Stakeholders expressed a preference to allow both public and proprietary companies to access CSEF.

9.65 Stakeholders also expressed a lack of clarity as to whether CSEF intermediaries would fall within the definition of operating a financial market and therefore require an AML. Stakeholders noted that the costs associated with AML obligations could be a barrier to the establishment and development of platforms, particularly those that seek to offer secondary trading. The feedback from these consultation processes led to a fourth option for facilitating CSEF to be developed. This option is discussed in more detail in Section 5. This option was adjusted further following introduction of the Corporations Amendment (Crowd-sourced Funding) Bill 2015 into Parliament in December 2015, an inquiry by the Senate Economics Committee into the Bill, and Government consultations with its FinTech Advisory Group. The Government increased the eligibility cap for using CSEF from $5 million annual turnover and gross assets and reduced the cooling off period from five working days to 48 hours.

5. OPTION 4: POST-CONSULTATION MODEL

9.66 Following the feedback received from the consultation processes outlined above, a fourth option for facilitating CSEF for public companies, drawing on elements of the CAMAC and New Zealand models, was developed. This regulation impact statement therefore considers four options:

- Option 1: a regulatory framework based on the CAMAC model;
- Option 2: a regulatory framework based on the New Zealand model;
- Option 3: the status quo; and
- Option 4: a post-consultation model.

9.67 Key features of the post-consultation model include:

- for issuers:
  - access to CSEF would be limited to unlisted Australian public companies with less than $25 million in turnover per

annum and $25 million in gross assets, including those that have previously undertaken fundraising through CSEF[14];

– on public company compliance requirements: exemptions from certain public company obligations, as recommended by CAMAC, would be available to certain eligible companies;

i) on expiry of the compliance exemptions, a company would only be required to obtain a full audit for the previous financial year's accounts, rather than for any period for which the company's accounts were not audited;

ii) companies wishing to access the compliance exemptions would have one year to conduct a CSEF raising before losing access to the relief. Companies that conduct a CSEF raising would remain eligible for the exemptions until they reach certain financial thresholds;

– a cap of $5 million on the amount that can be raised through CSEF disclosure relief in any 12-month period inclusive of any fundraising via the small scale personal offer exemption but excluding wholesale investors;

– limitation of the regime to one class of fully paid ordinary shares;

– use of a template disclosure document;

– restrictions on advertising of the equity offer; and

– requirements relating to material adverse changes during the offer period;

• for intermediaries:

– requirements for intermediaries to have an AFSL including membership of an external dispute resolution scheme;

14 The Corporations Amendment (Crowd-sourced Funding) Bill 2015, introduced into Parliament in December 2015, specified eligibility caps of $5 million turnover per annum and $5 million in gross assets.

– exemption from AML obligations where an intermediary is facilitating only primary issuance, and access to a reduced AML regime where they facilitate secondary trading;

– requirements to undertake limited due diligence and provide generic risk warnings to investors;

– no restrictions on fee structures or having an interest in an issuer using its platform, but fees and interests must be disclosed;

– a prohibition on lending to investors; and

– provision of a communication facility on its website for each issuer; and

• for investors:

– an investment cap of $10,000 per offer;

– signature of risk acknowledgement statements prior to investment; and

– cooling off and other withdrawal rights.

9.68 The post-consultation model draws on elements of both the CAMAC and New Zealand models. Other elements, such as expiry of compliance requirement exemptions, diverge from the approach recommended by CAMAC in areas that are not incorporated into the New Zealand model. The approach to other elements, such as investor caps, seek to balance the approaches taken under the CAMAC and New Zealand models.

9.69 Table 1 compares the key elements of the CAMAC, New Zealand and post-consultation models.

9.70 In response to stakeholder feedback, the Government also began consulting on whether CSEF should be extended to proprietary companies. The Government released a public discussion paper on whether CSEF could be extended to proprietary companies on 4 August 2015. The feedback from this consultation is being considered, and any policy options to facilitate CSEF for proprietary companies will be developed after the introduction of legislation to facilitate CSEF for public companies.

Table 1: Key elements of the CAMAC, New Zealand and post-consultation models

Issue	CAMAC model	New Zealand model	Post-consultation model
Issuers			
Eligible issuers	Australian-incorporated issuers that must be either a public company or an exempt public company. Limited to certain small enterprises that have not raised funds under the existing public offer arrangements. Cap in size of $10 million in capital.	New Zealand-incorporated companies.	Unlisted Australian-registered issuers that must be a public company (including with exemptions from certain compliance requirements). Cap in size of $25 million in turnover per annum and $25 million in gross assets.[15]
Relief from public company compliance costs	Available to exempt public companies, with a cap of $5 million in turnover per annum and $5 million in capital. Relief from a range of compliance requirements, including annual general meetings, and audit requirements (up to a certain threshold). Exempt status available for a period of up to three to five years, subject to turnover and capital thresholds.	No CSEF-specific exemptions.	Relief from a range of compliance requirements, including annual general meetings, and audit requirements (up to $1 million raised from CSEF and other offers requiring disclosure), for companies on incorporation or conversion to a public company. Companies on incorporation or conversion to a public company must conduct a CSEF raising within one year or lose eligibility for relief.
Maximum funds an issuer may raise	Cap of $2 million in any 12-month period, excluding funds raised under existing prospectus exemptions for wholesale investors.	Cap of $2 million in any 12-month period, excluding funds raised under existing prospectus exemptions for wholesale investors.	Cap of $5 million in any 12-month period, inclusive of any fundraising via the small scale personal offer exemption but excluding wholesale investors.
Permitted securities	One class of fully paid ordinary shares.	One class of fully paid ordinary shares.	One class of fully paid ordinary shares.
Disclosure requirements	Reduced disclosure requirements, including a template disclosure document.	Minimum disclosure requirements, with issuers and intermediaries to have in place arrangements to provide greater disclosure where there are no or high voluntary investor caps or the issuer is seeking to raise significant funds.	Reduced disclosure requirements, including a template disclosure document.

15 The Corporations Amendment (Crowd-sourced Funding) Bill 2015, introduced into Parliament in December 2015, specified caps of $5 million annual turnover and gross assets.

Issue	CAMAC model	New Zealand model	Post-consultation model
Advertising	Restrictions on advertising and publicity of offers, with exemptions for dissemination of the disclosure document and advertising and publicity that are accompanied by certain mandatory statements.	Not specified in legislation.	Restrictions on advertising and publicity of offers, with exemptions for dissemination of the disclosure document and advertising and publicity that are accompanied by certain mandatory statements.
Material adverse change during the offer period	Issuer to amend disclosure document and provide to intermediary for publication. Investors to have the ability to opt-out of their acceptance of the offer.	Not specified in legislation.	Issuer to amend disclosure document and provide to intermediary for publication. Investors to have the ability to opt-out of their acceptance of the offer.

Table 1: Key elements of the CAMAC, New Zealand and post-consultation models (continued)

Issue	CAMAC model	New Zealand model	Post-consultation model
Intermediaries			
Licensing	Hold an AFSL and comply with licensing requirements, including membership of an external dispute resolution scheme.	Be licensed and comply with licensing requirements, including membership of an external dispute resolution scheme.	Hold an AFSL and comply with licensing requirements, including membership of an external dispute resolution scheme. Exemption from AML obligations when facilitating only primary issuances, and access to a reduced AML regime for facilitating secondary trading.
Due diligence	Undertake limited due diligence checks on the issuer.	Undertake limited due diligence checks on the issuer.	Undertake limited due diligence checks on the issuer.
Risk warnings	Provide generic risk warnings to investors.	Provide disclosure statements and generic risk warnings to investors.	Provide generic risk warnings to investors.
Fee structures	Prohibited from being remunerated according to the amount of funds raised by the issuer, or in the securities or other interest of the issuer.	No restrictions on fee structures, although fees paid by an issuer must be disclosed.	No restrictions on fee structures, although fees paid by an issuer must be disclosed.
Interests in issuers	Prohibited from having a financial interest in an issuer using its website.	Permitted to invest in issuers using their platform, although details of any investments must be	Permitted to invest in issuers using their platform, although details of any investments must be disclosed.

Issue	CAMAC model	New Zealand model	Post-consultation model
		disclosed.	
Provision of investment advice to investors	Prohibited.	Not specified in legislation.	Not specified in legislation. Existing rules relating to the provision of investment advice will apply to intermediaries.
Lending to CSEF investors	Prohibited.	Not specified in legislation.	Prohibited.
Communications facilities	Provide a communication facility on its website for each issuer.	Intermediary must have adequate disclosure arrangements to enable investors to readily obtain timely and understandable information, which can include question and answer forums.	Provide a communication facility on its website for each issuer.
Investors			
Investment caps	$2,500 per issuer per 12-month period and $10,000 in total CSEF investment per 12-month period.	Voluntary investor caps, with the level of disclosure dependent upon the level of any voluntary caps and the amount of funds the issuer is seeking to raise.	$10,000 per offer, with no maximum aggregate investment, for retail investors.
Risk acknowledgement	Signature of risk acknowledgement statements prior to investment.	Signature of risk acknowledgement statements prior to investment.	Signature of risk acknowledgement statements prior to investment.
Cooling off and withdrawal rights	Unconditional right to withdraw for 5 days after accepting offer. Additional rights in relation to material adverse changes during the offer period.	Not specified in legislation.	Unconditional right to withdraw for 48 hours after accepting offer.[16] Additional rights in relation to material adverse changes during the offer period.

16 The Corporations Amendment (Crowd-sourced Funding) Bill 2015, introduced into Parliament in December 2015, specified a cooling off period of 5 business days.

6. IMPACT ANALYSIS OF THE CSEF MODELS

6.1 OPTION 1: CAMAC MODEL

9.71 Current disclosure and corporate governance arrangements are intended to minimise information asymmetries and agency costs between investors and managers of companies to protect and promote the interests of shareholders. However, the compliance costs associated with obligations can be burdensome for small companies.

9.72 A benefit of CAMAC's model is that it seeks to address the key elements of the current corporate and fundraising regimes that act as a hindrance to CSEF, such as requirements for public companies to appoint an auditor, have their financial statements audited and hold annual general meetings, and prepare extensive disclosure documents. This would make it easier for issuers to use CSEF, and consequently make it more attractive for intermediaries to establish CSEF platforms.

9.73 However, compared to the status quo, investors would have less access to information on which to make an investment decision and assess ongoing performance. This represents a divergence from the current approach for public companies. The CAMAC model seeks to balance the proposed reductions in transparency and disclosure obligations and address the higher risks that generally arise from investing in start-ups and small businesses by putting in place some additional protections for investors, including:

- situating the intermediary at the centre of the model, and in addition to being licensed, places a number of obligations on intermediaries and prohibits them from certain activities that may give rise to conflicts with the interests of investors;
- limiting the size of the companies able to use CSEF and prohibiting previous public equity raisings, to ensure that CSEF is targeted to small, simple companies and minimise the risk of regulatory arbitrage with existing public offer arrangements that require more substantive disclosure;
- requiring investors to acknowledge and sign a statement outlining the risks of CSEF investments, such as the risk of business failure, losing the funds invested and that investments may be illiquid for an extended period, to ensure that investors are aware of the risks prior to investing; and
- limiting the amount of funds retail investors may invest via CSEF in any 12-month period, to compensate for reduced

disclosure by issuers and the higher risks associated with investing in small businesses and start-ups that may not have an extensive history or customer base. CSEF disclosure documents may be less informative for investors compared to the status quo because:

- the amount of information required would be reduced;
- with a shorter history or rapidly developing product, service or market, the ongoing applicability of descriptions of the business and potential future developments or opportunities on which an investor makes their investment decision may be lower than for a more established company with a less variable business plan; and
- CAMAC did not specify whether issuers would need to lodge their disclosure document with ASIC. Were disclosure documents not required to be lodged, there would be a reduced level of external review compared to ASIC's existing approach to reviewing prospectuses, and consequently reduced assurance that the disclosure document provides all the required information.

9.74 In an environment of higher-risk businesses and reduced protections through the initial disclosure document, investor caps would limit retail investors' exposure, and consequently potential losses. Limiting the amount of potential losses may assist in maintaining investor confidence in CSEF as an investment mechanism. Investor caps also send a signal to CSEF investors that CSEF investments may be riskier than other potential investments, and that CSEF should only form a limited portion of a diversified investment portfolio. Such a signal may improve investor education and assist in better informed investment decisions.

9.75 A further benefit of implementing the approach recommended by CAMAC, relative to retaining the status quo, is that Australia would keep pace with developments in overseas jurisdictions, reducing the incentive for Australian businesses and investors to leave Australia to access CSEF.

9.76 Compared to the status quo, issuers would continue to incur costs ensuring their compliance with issuer and shareholder caps, with an additional cost associated with assessing their continued eligibility to raise funds via CSEF and maintain exempt public company status (if applicable). Issuers would be required to operate as public companies (or exempt public companies), rather than use the proprietary company structure. This would result in issuers incurring additional compliance

costs, particularly where they would otherwise meet the definition of a 'small proprietary company'.[17]

9.77 Intermediaries would incur costs associated with performing limited due diligence on companies seeking to raise funds via their platforms, providing the template disclosure documents and risk disclosure documents to investors, receiving and recording acknowledgements of risk disclosure statements, monitoring investor compliance with issuer caps and providing facilities for investors to communicate with issuer companies.

9.78 Investors would be limited in the amount they can invest in businesses, unless they were eligible for one of the existing wholesale investor exemptions. Investors would also be required to monitor compliance with investor caps and acknowledge a risk disclosure statement that intermediaries would be required to provide.

Issues Arising from CAMAC's Recommendations

9.79 There are specific elements of CAMAC's proposed framework that may result in an overly complex or restrictive system or otherwise continue to present a barrier to effective facilitation of CSEF in Australia.

9.80 The creation of a new category of public company would add complexity to the corporate governance framework and may increase risks of regulatory arbitrage compared to the status quo.

- Increasing complexity may mean that start-ups and small companies may have difficulty understanding their obligations.

- There may be an incentive for firms to structure themselves as exempt public companies to avoid costs associated with compliance requirements such as audited financial reporting and annual general meetings, without any genuine intention to raise funds via CSEF. This would result in a reduction in transparency without any offsetting increase in the ability for targeted firms to raise capital.

17 Small proprietary companies and large proprietary companies are defined in s45A of the Corporations Act. Key differences in compliance requirements for small proprietary companies compared to large proprietary companies include annual financial reports and directors' reports and audit. Differences in compliance requirements for small proprietary, large proprietary and public companies under current arrangements are discussed further in section 4.4.

9.81 CAMAC proposed that a number of different caps and thresholds be implemented for different elements of its CSEF framework related to issuers (see table 2). These caps are intended to ensure that CSEF is targeted at small businesses and start ups and reduce the potential for regulatory arbitrage. They are also intended to balance a reduction in compliance costs, such as preparation of a full disclosure document or audit processes, with maintaining investor protections.

Table 2: Caps and thresholds recommended by CAMAC

Category	Cap or threshold	Policy objective of cap or threshold
Eligibility to conduct a CSEF issue	Limited to certain companies with simple structures, with a cap of $10 million in capital	Minimise distortions and the potential for regulatory arbitrage in the fundraising regime while targeting CSEF to small issuers less likely to be able to absorb the compliance costs of a public equity offer under existing requirements.
Eligibility to become or remain an exempt public company	Limit of $5 million in turnover per annum and $5 million in capital	Minimise distortions and the potential for regulatory arbitrage in the corporate governance and reporting regime while addressing identified barriers to enterprises incorporating as public companies and conducting public equity offers.
Exempt public companies eligible for exemption from auditing requirements	Limited to companies that have raised up to $1 million in funds via CSEF or any other prospectus exemption and cumulative expenses of $500,000	Address a key compliance burden related to incorporation as a public company for issuers in the early stages of fundraising, and avoid issuers raising small amounts needing to spend a significant proportion of those funds on audit obligations rather than developing the business. Balance this objective with maintaining transparency and investor assurance once an issuer has raised a significant amount of capital and spent a significant proportion of that capital.
Cap on the amount of funds that can be raised via CSEF or other exemptions from disclosure requirements	Limit of $2 million per 12-month period for any individual or related group of companies	Balance addressing a barrier to fundraising with ensuring investors have access to full disclosure documentation for larger raisings. Align the CSEF cap with the existing small scale personal offer exemption.

9.82 This compares to an existing ASIC class order that increases the cap on funds that may be raised under the small scale personal offer exemption from $2 million to $5 million per 12-month period under certain circumstances.[18]

18 ASIC Class Order 02/273: Business Introduction or Matching Services.

9.83 However, there are potential issues with the proposed caps:

- the interaction of the various caps and thresholds may be complex for issuers, intermediaries and investors to understand and monitor; and
- the level of the caps and thresholds is necessarily a matter of judgement. The caps proposed by CAMAC may not appropriately balance the funding needs of small businesses and investor protection.

9.84 To reduce the risk of conflicts of interest arising between intermediaries and investors that could compromise intermediaries' neutral service provider role, CAMAC recommended that intermediaries be restricted from having an interest in an issuer and from being paid in the shares of the issuer or according to the amount of funds raised. However, costs of this approach include:

- a potential reduction in the pool of potential intermediaries and/or investors;
- a restriction on paying intermediaries in shares may be a barrier for start-ups that are likely to have poor cash flow in the establishment phase; and
- the requirement for an issuer to pay a fee to the intermediary that is fixed at a set dollar amount, rather than a fee based on a percentage of the funds raised, may act as a disincentive for issuers raising relatively small amounts of funds.

9.85 While noting that CSEF platforms may require an AML, CAMAC did not make any recommendation regarding this. Without change in the current regulatory framework, intermediaries may continue to have a lack of certainty as to their requirement to hold an AML, and it may limit the establishment of CSEF platforms, particularly those facilitating secondary trading.

9.86 CAMAC recommended caps on the amount investors could invest per issue and in CSEF overall per 12 month period. While having an important investor protection role, implementing investor caps could make it difficult for issuers to raise funds via CSEF. Investor caps may also result in a large number of micro investors, who may consequently have limited ability to exert discipline and control over the issuer. Furthermore, intermediaries would have difficulty in monitoring investors' compliance with aggregate investor caps for investments through their own platform as well as those of other intermediaries,

increasing intermediaries' compliance costs and potentially reducing the effectiveness of the aggregate cap.

6.2 OPTION 2: NEW ZEALAND MODEL

9.87 Similar to the CAMAC model, the New Zealand model has the benefits of placing the intermediary at the centre of the model as a gatekeeper and keeping pace with international developments. Additional benefits associated with the New Zealand model compared to the CAMAC model include:

- reduced complexity by removing exemptions from certain company compliance costs and fewer caps and thresholds for issuers;
- intermediaries are not restricted in fees they can charge or the interests they can acquire in issuers using their platforms, potentially increasing the pool of CSEF investors and intermediaries;
- the ability for intermediaries to charge a fee proportional to the funds raised would be consistent with existing market practice for equity capital raisings and provide an incentive for intermediaries to only list issuers they consider will successfully raise funds;
- greater flexibility for issuers to trade off the level of voluntary investor caps with the level of disclosure, compared to mandatory caps and template disclosure requirements;
- consistency between the Australian and New Zealand CSEF frameworks would reduce the barriers to CSEF participants operating in both markets, although this may also be achieved via the Trans-Tasman mutual recognition framework.

9.88 A number of the costs associated with the New Zealand model are similar to the CAMAC model, including issuers needing to comply with fundraising caps and requirements for intermediaries to be licensed, undertake limited due diligence on issuers and provide disclosure statements and risk warnings to investors. Disadvantages of the New Zealand model include:

- as the regime is not limited to small companies, there is a potential for larger companies that have previously made public equity offers using CSEF to raise additional funds,

circumventing the standard disclosure requirements for public equity offers;

- intermediary investment in CSEF issuers may raise investor expectations about the likelihood of success for companies the intermediary invests in, and may provide an incentive for intermediaries to present these issuers in a more favourable light than other issuers, including via less effective risk disclosure;

- issuers and intermediaries having less certainty on the level of disclosure necessary above minimum requirements, compared with the CAMAC approach of a template disclosure document applicable to all CSEF issues; and

- greater risk of investors losing larger amounts of funds in the absence of investor caps in an environment of a reduced level, and potentially, quality of information (as outlined in section 4.1), on which investors made their initial investment decision.

6.3 OPTION 3: STATUS QUO

9.89 For the intermediaries that currently provide online platforms for investing in start-up companies under the existing legislation, maintaining existing regulatory requirements would result in no additional costs.

9.90 Under the models operated by the existing intermediaries, some issuers are structured as proprietary companies and others are structured as public companies. These companies would continue to incur existing governance and compliance costs, with additional costs for large proprietary companies and public companies, compared to small proprietary companies, associated with requirements such as preparing annual financial reports and directors' reports[19], appointing an auditor and

19 Corporations Act, Part 2M.3, Division 1 outlines financial reporting requirements. Large proprietary companies and public companies must prepare annual financial reports and directors' reports. Under s292, small proprietary companies are only required to prepare an annual financial report in certain circumstances, including in response to a direction by shareholders with at least 5 per cent of votes in the company or by the Australian Securities and Investments Commission. Small and large proprietary companies are defined under s45 according to certain revenue, asset and employee thresholds.

conducting an annual audit of the financial reports[20], and holding an annual general meeting.

9.91 Issuers would continue to have access to existing mechanisms to raise funds, including via the wholesale and small scale offer exemptions from the need to prepare a prospectus. These exemptions allow issuers to raise funds from angel investors and families and friends without incurring the costs of preparing a disclosure document. Where public companies wish to raise funds outside the exemptions, they would also continue to have access to the use of an offer information statement in certain circumstances. These mechanisms may continue to remain adequate for some issuers. Issuers would also continue to incur costs associated with monitoring their compliance with the wholesale and small scale personal offer exemptions, as well as monitoring the issuer shareholder caps, including the 50 non-employee shareholder cap for proprietary companies.

9.92 Under the status quo, investors would continue to benefit from existing investor protections, including the receipt of disclosure documents for public issues of equity, subject to the limited exemptions, and access to audited financial reports, directors' reports and annual general meetings when they invest in large proprietary or public companies. These protections assist investors to assess the risks associated with particular investments and to monitor ongoing performance.

9.93 However, relying on existing requirements would not address the funding challenges for start-ups and the barriers to CSEF in Australia. Start-ups and small businesses seeking to raise funds would not be able to make offers to the crowd, limiting potential sources of funds. Online intermediaries would remain limited in the business models they could adopt. Investors would have access to a limited number of start-ups and small businesses they could invest in via online platforms.

9.94 Regulatory regimes to facilitate CSEF are in the process of being implemented in a number of other jurisdictions. Relying on the status quo would also mean that Australia's position on CSEF would be markedly different from a number of other jurisdictions and could be perceived to be less supportive of innovative funding mechanisms. Innovative businesses and platform providers may also have an incentive

20 Corporations Act, s301 provides that the annual financial reports must be audited in accordance with Part 2M.3, Division 3. Small proprietary companies that prepare a financial report in response to a shareholder direction under s293 do not need to obtain an audit if that direction did not ask for the financial report to be audited.

to shift their operations to these jurisdictions to more easily access start-up and growth capital. This could also hinder the growth of the Australian entrepreneurial sector.

6.4 OPTION 4: POST- CONSULTATION MODEL

9.95 The post-consultation model seeks to address key themes from the consultation process while balancing reducing barriers to and compliance costs associated with CSEF, while maintaining adequate investor protection.

9.96 Similar to the CAMAC and New Zealand models, the intermediary would perform an important gatekeeping role. The post-consultation model would also allow Australia to keep pace with international developments.

9.97 Key elements of the corporate governance compliance regime that present a barrier for enterprises to convert to public company status would be addressed, as they are under the CAMAC model. Similar to the CAMAC model, the reduction of disclosure and corporate governance obligations on CSEF issuers diverge from the current approach under the Corporations Act. These reduced obligations for issuers are balanced by additional protections for investors, such as limits on the size of issuer companies, limits on the amounts issuers can raise, caps on the amount investors can invest and signature of risk acknowledgement statement. However, as outlined below, the issuer and investor limits are higher under the post-consultation model compared to the CAMAC model.

9.98 A benefit compared to the CAMAC model is the reduced period for which issuers must obtain a full audit of their financial accounts after losing their exempt status. Under this model, only the most recent financial statements would be required to be audited, reducing compliance costs for issuers. This approach reflects stakeholder concern that obtaining an audit for financial accounts up to five years old may be impractical and overly burdensome, as the responsible auditor would not have been appointed at the time and had access to the company to facilitate the audit process.

9.99 While investors would have reduced assurance about the accuracy of the financial statements for the entirety of the exemption period, the marginal benefit of this higher assurance for financial statements from several years prior is likely to be outweighed by the cost to the issuer of obtaining a multi-year audit.

9.100 The proposed approach to the eligibility period for exemptions from the compliance requirements would be expected to reduce the risk of regulatory arbitrage present in the CAMAC model, where a company could gain access to the exemptions for a period of up to three to five years without needing to conduct a CSEF raising. A one-year grace period for a newly incorporated or converted public company would provide a potential issuer with time to develop a CSEF proposal and conduct a raising while not being subject to potentially onerous public company compliance requirements.

9.101 Other benefits of the post-consultation model compared to the CAMAC model include:

- an increased cap on the amount of funds that can be raised via CSEF in a 12-month period, increasing flexibility for issuers who may prefer to conduct a single large CSEF raising rather than a series of smaller ones and aligning the cap with the existing ASIC class order that facilitates a limited form of CSEF[21];
- increased caps on eligibility to use CSEF, from $10 million in capital to annual turnover and gross assets of $25 million will increase the range of small and early-stage companies able to use the lower-cost fundraising option available through CSEF and increase CSEF investment options for investors;
- alignment of the eligibility caps for access to the corporate governance compliance exemptions and use of CSEF would reduce regulatory complexity;
- permitting companies that have previously undertaken a public offer to use CSEF would reduce the fundraising costs of these businesses and provide an alternative to traditional public offers;
- more certainty, and lower compliance costs, for intermediaries regarding their market licencing obligations would better facilitate secondary trading;

[21] ASIC Class Order 02/273: Business Introduction or Matching Services, which allows issuers to raise up to $5 million per 12 month period from up to 20 investors without the use of a disclosure document, rather than the $2 million limit under the small scale personal offer exemption.

- not including restrictions on intermediary fees or interests in issuers using their platforms addresses feedback from stakeholders that such restrictions would reduce the attractiveness of the CSEF market to potential intermediaries, reducing competition;

- higher investor caps would increase the amount of funds issuers could raise from the same number of investors (subject to the fundraising caps) and increase flexibility for investors who wish to invest larger amounts but who are not eligible for one of the existing prospectus exemptions;

- a reduced cooling off period of 48 hours will provide issuers and intermediaries with greater certainty about the amount raised via a CSEF offer while retaining a reasonable period for investors to withdraw after making an investment.

9.102 Drawbacks compared to the CAMAC model include:

- permitting companies that have previously undertaken public offers to use CSEF would reduce the amount of disclosure these companies would need to provide to potential investors, which may result in investors being less informed than would otherwise be the case;

- similar to the New Zealand model, intermediary investment in CSEF issuers may raise investor expectations about the likelihood for success of those companies; and

- greater risk of investors losing larger amounts of funds in the absence of aggregate annual investor caps.

9.103 Compared to the New Zealand model, benefits of the post-consultation model include:

- similar to the CAMAC model, limitation of the regime to certain small companies reduces the risk of larger companies circumventing the standard disclosure requirements for public equity offers;

- limits on the amount of funds investors may lose via CSEF while having access to reduced disclosure, which may also help maintain investor confidence in CSEF; and

- greater certainty on the level and type of disclosure required by issuers.

9.104 Drawbacks compared to the New Zealand model include:

- similar to the CAMAC model, increased complexity by removing exemptions from certain company compliance costs;
- limitations on the size of companies that may use CSEF, requiring issuers to monitor their compliance with the caps;
- inability to trade off the level of voluntary investor caps with the level of disclosure; and
- intermediaries would still need to monitor investors' compliance with investor caps for investments made through its platform.

7. REGULATORY BURDEN AND COST OFFSET ESTIMATES OF THE CSEF MODELS

7.1 OPTION 1: CAMAC MODEL

9.105 Table 3 includes estimates of compliance costs associated with implementing the model recommended by CAMAC.

9.106 The compliance costs are estimated by modelling the cost for issuers, intermediaries and investors of key relevant elements of the current regulatory framework for small businesses that currently use online platforms to raise equity, and comparing these status quo costs to the expected costs under CAMAC's framework. This approach makes assumptions about the number of CSEF issuers, intermediaries and investors over the next 10 years under both the status quo and CAMAC options.

9.107 CAMAC's proposal is expected to reduce the overall 'per business' compliance costs for issuers that participate. However, given the likely growth in the number of businesses raising funds via online intermediaries under the CSEF arrangements, the aggregate compliance burden across the economy over the next 10 years is expected to increase.

- Costs per issuer are expected to fall in net terms by $7,950 per year, driven largely by temporary exemptions from audit and annual general meeting requirements and reductions in disclosure costs.

- Compliance costs for intermediaries are expected to increase in line with the expected increase in businesses raising funds via CSEF. Intermediary costs that vary with the number of issuers raising funds are expected to increase by $1,550 per fundraising campaign.

- Costs per investor are expected to increase by $75 per year as a result of investors monitoring their compliance with investment caps and acknowledging risk disclosure statements prior to each investment.

Table 3: Regulatory burden and cost offset estimate table

Average annual regulatory costs (from business as usual)				
Change in costs ($million)	**Business**	**Community Organisations**	**Individuals**	**Total change in cost**
Total, by sector	$45.4 million	$0	$1.3 million	$46.8 million
Cost offset ($ million)	**Business**	**Community organisations**	**Individuals**	**Total, by source**
Agency	$46.8 million	$0	$0	$46.8 million
Are all new costs offset? ☑ Yes, costs are offset ☐ No, costs are not offset ☐ Deregulatory — no offsets required				
Total (Change in costs — Cost offset) ($million) = $0				

9.108 A regulatory offset has been identified from within the Treasury portfolio. This offset relates to a proposal to align the legal frameworks for personal and corporate insolvency practitioners.

9.109 The key assumptions that underlie this compliance cost estimate are outlined at the Appendix, Section 9.2.1.

7.2 OPTION 2: NEW ZEALAND MODEL

9.110 Table 4 includes estimates of compliance costs associated with implementing a model similar to that implemented by New Zealand, using the same costing approach as used for estimating the CAMAC model compliance costs.

9.111 A model similar to that implemented in New Zealand is expected to reduce the overall 'per business' compliance costs for issuers that participate. However, given the likely growth in the number of

businesses raising funds via online intermediaries under the CSEF arrangements, the aggregate compliance burden across the economy over the next 10 years is expected to increase.

- Costs per issuer are expected to fall in net terms by $1,750 per year. The key difference in issuer costs between the CAMAC and New Zealand model is the absence of CSEF specific exemptions from public company compliance costs.
- Compliance costs for intermediaries are expected to increase in line with the expected increase in businesses raising funds via CSEF. Intermediary costs that vary with the number of issuers raising funds are expected to increase by $1,680 per fundraising campaign.
- Costs per investor are expected to increase by $17 per year as a result of investors being required to acknowledge risk disclosure statements prior to each investment.

Table 4: Regulatory burden and cost offset estimate table

Average annual regulatory costs (from business as usual)				
Change in costs ($million)	**Business**	**Community Organisations**	**Individuals**	**Total change in cost**
Total, by sector	$58.8 million	$0	$0.3 million	$59.2 million
Cost offset ($ million)	**Business**	**Community organisations**	**Individuals**	**Total, by source**
Agency	$59.2 million	$0	$0	$59.2 million
Are all new costs offset? ☑ Yes, costs are offset ☐ No, costs are not offset ☐ Deregulatory — no offsets required				
Total (Change in costs — Cost offset) ($million) = $0				

9.112 A regulatory offset has been identified from within the Treasury portfolio. This offset relates to a proposal to align the legal frameworks for personal and corporate insolvency practitioners.

9.113 The key differences between the estimated compliance costs of the CAMAC model and the New Zealand model are the absence in the New Zealand model of the 'exempt public company' structure, the disclosure of intermediary fees and interests in issuers, and intermediaries' disclosure arrangements for investors.

9.114 In Australia, the lack of the exempt public company structure for newly registered or converted public companies using CSEF would mean that these companies would need to comply with the full range of public company obligations, such as holding AGMs, audit of financial statements and providing the option of sending shareholders copies of the annual report, which would increase compliance costs. While New Zealand does not have CSEF-specific reporting and governance exemptions, any company that falls within the required size thresholds may be exempt from certain financial reporting and audit obligations.

9.115 Key assumptions underlying the compliance cost estimate for this option that differ from those used for the CAMAC model are outlined at the Appendix, Section 9.2.2.

7.3 OPTION 4: POST-CONSULTATION MODEL

9.116 The regulatory costs of the post-consultation model have been estimated in two parts.

- The compliance costs associated with the post-consultation model (except for the AML changes), have been estimated in Table 5 using the same costing approach as used for estimating the CAMAC model compliance costs.
- The compliance costs associated with changes to the AML regime have been estimated in Table 6 to reflect that the changes will apply more broadly than just to the CSEF market (outlined below in Section 8.1).

Table 5: Regulatory burden and cost offset estimate table (excluding AML changes)

Average annual regulatory costs (from business as usual)				
Change in costs ($million)	**Business**	**Community Organisations**	**Individuals**	**Total change in cost**
Total, by sector	$48.8 million	$0	$1.5 million	$50.3 million
Cost offset ($ million)	**Business**	**Community organisations**	**Individuals**	**Total, by source**
Agency	$50.3 million	$0	$0	$50.3 million
Are all new costs offset? ☑ Yes, costs are offset ☐ No, costs are not offset ☐ Deregulatory — no offsets required				
Total (Change in costs — Cost offset) ($million) = $0				

Table 6: Regulatory burden and cost offset estimate table (AML changes)

Average annual regulatory costs (from business as usual)				
Change in costs ($million)	**Business**	**Community Organisations**	**Individuals**	**Total change in cost**
Total, by sector	$0.6 million	$0	$0	$0.6 million
Cost offset ($ million)	**Business**	**Community organisations**	**Individuals**	**Total, by source**
Agency	$0.6 million	$0	$0	$0.6 million
Are all new costs offset? ☑ Yes, costs are offset ☐ No, costs are not offset ☐ Deregulatory — no offsets required				
Total (Change in costs — Cost offset) ($million) = $0				

9.117 The post-consultation model is expected to reduce the overall 'per business' compliance costs for issuers that participate in CSEF. However, given the likely growth in the number of businesses raising funds via online intermediaries under the CSEF arrangements, the aggregate compliance burden across the economy over the next 10 years is expected to increase.

- Costs per issuer are expected to fall in net terms by $9,950 per year, driven largely by temporary exemptions from audit and annual general meeting requirements and reductions in disclosure costs.

- Costs per investor are expected to increase by $75 per year as a result of investors monitoring their compliance with investment caps and acknowledging risk disclosure statements prior to each investment.

9.118 Compliance costs for intermediaries would be impacted by the CSEF framework (excluding AML changes), and by the changes to the AML framework.

- Under the CSEF framework excluding AML changes, compliance costs for intermediaries are expected to increase in line with the expected increase in businesses raising funds via CSEF. Intermediary costs that vary with the number of issuers raising funds are expected to increase by $1,550 per fundraising campaign.

- Under the revised AML framework, compliance costs for existing platforms (across both CSEF and non-CSEF markets) will reduce by an average of $20,542 per year. Compliance costs for new platforms that enter the market (again, across both CSEF and non-CSEF markets) will increase by an average of $115,202 per year, although this is mainly driven by the costs incurred by new platforms that would not otherwise have been established.

9.119 A regulatory offset has been identified from within the Treasury portfolio. This offset relates to a proposal to align the legal frameworks for personal and corporate insolvency practitioners.

9.120 The key difference between the estimated compliance costs of the CAMAC model and the post consultation model is the removal of the requirement for financial statements covering the period the issuer is eligible for an audit exemption to be audited once that exemption expires, and the changes to the AML framework.

9.121 Other key assumptions underlying the compliance cost estimate for this option are consistent with those outlined for the CAMAC option, and the New Zealand option for intermediary fee disclosures and disclosure arrangements for investors.

9.122 Key assumptions underlying the compliance cost estimate for the revised AML framework are outlined at the Appendix, Section 9.2.3.

8. GOVERNMENT POLICY

8.1 OPTION 4: POST-CONSULTATION MODEL IS THE PREFERRED OPTION

9.123 Following consideration of the four options, the Government has elected to implement Option 4: the post-consultation model. This model draws on elements of both the CAMAC and New Zealand models, as well as incorporating suggestions from stakeholder feedback. It is considered to provide the most appropriate balance between reducing the barriers to and compliance costs of CSEF for public companies, while maintaining adequate investor protection.

9.124 For issuers, this model introduces less complexity into the regulatory framework than the CAMAC model by not creating a new 'exempt public company' category. It also allows businesses to raise more funding through CSEF in any 12-month period than under both the CAMAC and New Zealand models, but limits the size of companies that

may use CSEF compared to the New Zealand model. A further benefit to issuers is the reduced costs associated with obtaining an audit on their past financial accounts, when compared to the CAMAC model.

9.125 For intermediaries, this model provides more certainty and lower costs for market licencing, and more flexibility to operate under a preferred fee structure and to invest in small businesses through CSEF, than under the CAMAC model. These fees and investments must still be disclosed.

9.126 For investors, this model introduces larger investor caps than the CAMAC model. This will allow for more money to be invested in small businesses through CSEF, while still limiting the amount of funds that investors could lose. The introduction of such caps could though be more restrictive on the amount of funds an investor can invest, compared to the voluntary caps of the New Zealand model.

9.127 This model also reduces the possibility for abuse of the CSEF regime. By limiting access to CSEF to those businesses below a turnover and asset threshold it will reduce the risk of larger companies seeking to circumvent the standard disclosure requirements for public equity offers, as could occur under the New Zealand model. By requiring businesses to raise funding through CSEF within the first 12 months of joining the simplified disclosure CSEF regime, it will also reduce the risk of businesses joining the regime to gain relief from normal compliance requirements without actually using CSEF, as could occur under the CAMAC model.

9.128 As outlined above, the changes to the AML framework will apply more broadly than just the CSEF market. They will also provide additional flexibility to facilitate an efficient, effective, and appropriate licencing regime for other markets. For example, professional markets could access the modified AML regime to create a consistent approach across markets and help facilitate mutual recognition of Australian operators with cross-border activities. New and emerging market types that would otherwise need to obtain a full AML could also access the modified AML regime, as appropriate, which would encourage innovation and competition in these markets.

9.129 The post-consultation model is likely to have the highest net benefit of the options considered, and has a lower estimated aggregate regulatory costs than either the CAMAC or New Zealand models.

8.2 GOVERNMENT CONSULTATION ON THE PREFERRED MODEL

9.130 A discussed in Section 5, the development of this model was heavily influenced by the stakeholder consultations undertaken in the first half of 2015.

9.131 A subsequent discussion paper was released in August 2015 that outlined the key features of this post-consultation model. Feedback provided at this stage informed the design of the final model.

9.132 In the process of drafting the legislative amendments, the Government continued to consult with industry participants, ASIC and relevant government agencies.

9.133 The draft Bill was shared with key industry stakeholders, including a number of firms seeking to set up as intermediaries in Australia, and corporate law experts for comment in early November 2015. Stakeholders were overall supportive of the draft legislation, and of the need to introduce a regulatory framework to facilitate CSEF.

9.134 However, stakeholder views were more varied on some of the details of the legislation. A number of concerns and queries around how the gatekeeper role of intermediaries will operate were raised. Stakeholders also considered that some of the eligibility criteria to use CSEF, particularly the requirement that issuers not have the purpose of investing in other entities, may be too restrictive and may hinder the normal growth process of a start-up, which may include integrating subsidiaries as it grows. In response to this feedback, the legislation has been amended to only capture entities that have a substantial purpose of investing in other companies.

9.135 Stakeholders also considered that commencement of the framework nine months following Royal Assent was too long a delay. In response to this feedback, the period was shortened to six months. However, given ASIC will be required to make technical changes to their systems and to issue guidance to support the legislation, it would be impractical to shorten this any further.

9.136 In accordance with the Corporations Agreement 2002, the Government also consulted with, and received the approval of, the states and territories for the proposed legislative amendments.

9.137 The Government released the draft regulations for consultation in December 2015, outlining, among other matters, minimum disclosure requirements for CSEF issuers, prescribed checks that intermediaries must undertake on issuers and the wording of the risk warning and risk acknowledgement. Stakeholders were generally supportive of the

disclosure requirements, with some suggesting more information be included. Stakeholders were also generally supportive of the requirements for the prescribed checks, but some sought further clarification on the conduct of the checks. Several stakeholders also made suggestions on the wording on the risk warning and acknowledgement. The Government is considering this feedback and will finalise the regulations once the Parliament passes the Bill.

9.138 The Corporations Amendment (Crowd-sourced Funding) Bill 2015 was introduced into Parliament on 3 December 2015. The Bill was referred to the Senate Economics Legislation Committee, which received submissions and held public hearings before tabling its report on 1 March 2016. The Committee considered matters including eligible CSEF issuers, the issuer fundraising cap, disclosures and consents, intermediary obligations, investor caps and the cooling-off period. The Committee recommended that the Bill be passed, with the Government to carefully monitor the implementation of the CSEF framework and review it two years after enactment. The Bill lapsed with the calling of the 2016 election.

9.139 In March 2016 as part of its FinTech Statement, the Government indicated that it was considering two potential amendments to the CSEF framework: increasing the eligibility cap from $5 million to $25 million and reducing the cooling-off period from five working days to 48 hours. Following further consultation, including with its FinTech Advisory Group, the Government decided to proceed with these amendments.

8.3 IMPLEMENTATION AND EVALUATION

9.140 The preferred model will be implemented through legislative amendments and regulations to the Corporations Act, regulatory guidance published by ASIC and ministerial exemptions in relation to AML obligations. It is proposed that the Bill will be reintroduced into the Parliament in the Spring 2016 parliamentary sitting period. The regulations will be considered by the Federal Executive Council following the Bill's passage through the Parliament.

9.141 The new laws will commence six months after the Bill receives Royal Assent. This will allow time for industry to consider the new laws and adjust their business models, including obtaining the necessary AFSL or AML licences if required.

9.142 In the 2015-16 Budget, ASIC received $7.8 million over four years to implement, monitor and enforce the new framework. During the transition period ASIC will produce regulatory guidance to help industry

transition to the new laws. ASIC will also develop a new CSEF authorisation category within the AFSL and will assess and consider applications for AFSL and AML licences as required, including data reporting obligations for licensees to assist in ongoing evaluation of the CSEF market.

9.143 The Government and ASIC will continue to monitor the CSEF market to ensure that the changes to the law are operating as intended. By making it easier and less costly for small public companies to raise equity financing through CSEF, the Government would expect that the number of businesses exploring this funding avenue will increase.

9.144 As outlined in Section 5, the Government is also considering extending CSEF to proprietary companies.

9. APPENDIX

9.1 SUMMARY OF CAMAC REPORT

9.145 CAMAC released its report on CSEF in June 2014. CAMAC found that the current law makes it difficult for CSEF to be used in Australia, and that change to the Corporations Act would be required if CSEF were to be facilitated in Australia.

9.146 CAMAC considered four options for facilitating CSEF in Australia.

1. Adjusting the regulatory structure for proprietary companies

9.147 This option would involve increasing or uncapping the number of permitted offers under the small scale personal offers exemption for public offers by proprietary companies and substantially increasing the number of permitted shareholders of a proprietary company.

9.148 There was support for both elements of this option from a number of stakeholders that made submissions to CAMAC's discussion paper.

9.149 However, CAMAC did not support this option, as it would involve a shift away from the purpose of proprietary companies as closely held entities, with consequently lower compliance requirements.

2. Confine CSEF to limited classes of investors

9.150 This option would involve limiting the classes of investors that could invest in CSEF, for example, to sophisticated, experienced and professional investors, as currently defined in the Corporations Act.[22] The definition of sophisticated investors could also be changed to a self-certification system, similar to that used in the United Kingdom.

9.151 Stakeholders did not support this option. CAMAC also noted that this option would 'deliver crowd funding without the crowd', and may not allow many businesses to raise a meaningful level of capital.

3. Amend the fundraising provisions for public companies

9.152 This option would involve amending the fundraising requirements for public companies contained in Chapter 6D of the Corporations Act, including the required level of disclosure.

9.153 Many stakeholders were of the view that this option would leave in place substantial governance and compliance requirements for public companies that would be overly burdensome for start-ups and small enterprises likely to use CSEF. CAMAC concurred with this view.

4. Introduce a new legislative regime for CSEF

9.154 CAMAC recommended the creation of a specific regulatory structure for CSEF, as outlined below

Recommendations

Corporate form

9.155 CAMAC recommended the creation of a new category of public company, to be known as an 'exempt public company'. Exempt public companies would be relieved of some of the compliance requirements of public companies for a period of up to three to five years. Such companies would be exempt from the following requirements:

- continuous disclosure;
- holding an annual general meeting;
- executive remuneration reporting;

22 *Corporations Act 2001*, s708.

- half-yearly reporting; and

- appointing an independent auditor and having their financial report audited, until the company has raised more than $1 million through CSEF or any other prospectus exemption and expended $500,000. On expiry of its exempt status, the company would be required to have a full audit, covering any period where its financial affairs were not audited.

9.156 CAMAC recommended that eligibility to become, and to remain, an exempt public company be limited to companies with turnover below $5 million per annum and capital of less than $5 million. Exempt status would also expire automatically after three years, subject to a limited exception that may extend the exempt status for up to two further 12 month periods. Shareholders would be required to agree to the proposal via a special resolution. CAMAC's rationale for limiting the period a company could retain exempt status was to balance the benefits of reducing compliance costs with the costs to investors of reduced transparency.

9.157 Existing companies seeking to become an exempt public company would also need to be eligible to conduct a CSEF offer. CAMAC proposed that companies that are complex or listed, have already conducted a regulated offer under Chapter 6D, blind pools and companies with substantial capital (with a suggested cap of $10 million), should not be eligible to conduct a CSEF offer.

Fundraising

9.158 CAMAC proposed a framework for CSEF fundraising that included a number of specific requirements for issuers, online intermediaries and investors.

Issuers

9.159 Issuers would be required to be a public company or exempt public company offering new, fully paid shares, with the following requirements:

- eligible issuers could not be complex or listed companies, have already conducted a regulated offer under Chapter 6D, a blind pool or a company with substantial capital (with a suggested cap of $10 million);

- comply with template disclosure requirements that would be less onerous than existing requirements;

- comply with a cap of $2 million on the amount that could be raised via CSEF or the small scale personal offer exemption in any 12-month period;

- issuers and intermediaries, and their respective directors and officers would not be able to lend to investors to acquire the issuer's shares via CSEF;

- issuers would be prohibited from paying any fees in connection with the offer, except to the intermediary and professional service providers;

- investor funds would not be able to be transferred to the issuer until the offer is completed, including reaching the subscription threshold outlined in the disclosure document, and the expiration of a cooling off period for investors and opt out rights where there is a material adverse change in the issuer's circumstances while the offer is open[23]; and

- comply with existing material adverse change provisions for regulated public offers[24], including the ability for investors to opt-out of previously accepted offers, and advise the intermediary of the corrected information.

Intermediaries

9.160 CAMAC proposed that intermediaries would be required to:

- hold an AFSL and meet licensing obligations, including membership of an external dispute resolution scheme and insurance requirements;

- undertake limited due diligence on issuers who use the intermediary's platform;

- provide generic risk warnings to investors;

- check compliance with the proposed investor cap per issuer;

- provide facilities for communication between issuers and investors;

23 *Corporations Act 2001*, s724.
24 *Corporations Act 2001*, s724.

- where they have been notified by an issuer of a material adverse change, notify that change to all investors who have previously accepted the offer, and publish the corrected information on its website; and

- would be required to hold investor funds until the issuer's offer has been completed, and hold the funds in accordance with existing client monies requirements.[25]

9.161 Intermediaries would be prohibited from:

- having a financial interest in any issuer that is undertaking a CSEF raising on its website;

- being remunerated according to the funds raised by an issuer conducting a CSEF raising on its website, or in securities or other interests in the issuer;

- offering investment advice or lending to CSEF investors; and

- soliciting crowd investors, with the exception of the intermediary advertising its existence and displaying key details relating to each capital raising, but including 'showcasing' particular offers on its website.

Investors

9.162 CAMAC also made the following recommendations in relation to investors:

- investor caps of $2,500 per investor per 12-month period for any one CSEF issuer and $10,000 per investor per 12-month period in total CSEF investments;

- CSEF issuers could raise funds under the small-scale personal offers exemption, with any funds raised to count towards the proposed $2 million per 12-month period issuer cap;

- no investor caps for investors meeting the definition of a sophisticated investor, and any funds raised from such

25 *Corporations Act 2001*, s981B.

investors would not count towards the proposed $2 million per 12-month period issuer cap[26];

- acknowledgement of a risk disclosure statement;
- access to cooling off rights for a period of 5 working days; and
- bans on directors and other associates of the issuer selling a significant proportion of their holdings within 12 months of any CSEF offer by that issuer.

9.2 REGULATORY BURDEN ESTIMATE ASSUMPTIONS

CAMAC Model

Compliance cost	Query	Estimate
Costs for public companies		
Preparation and lodgement of annual report	Cost of preparing annual report for a start-up or small business.	$4,000
Audit	Cost of having the financial statements of a start-up or small business audited on an annual basis. Cost of having financial statements of the exempt period audited once eligibility for exemption expires	$20,000 $20,000
Annual general meeting	Cost of a start-up or small business holding an annual general meeting.	$7,500
Issuers		
Labour cost associated with an issuer monitoring compliance with fundraising limits for disclosure exemptions under the status quo or the issuer cap under the CAMAC model.	Hours per year spent on monitoring. Hourly rate of the staff member that would undertake the monitoring.	4 hours $65.45 per hour.[27]
Legal advice on eligibility to issue under CSEF	Hours required. Hourly rate.	20 hours $107.68[28]

26 *Corporations Act 2001*, s708.

27 Based on ABS labour rates in the RIS guidelines, including employer costs.

28 In the absence of reliable data on charge-our rates for small legal firms, estimate obtained from Hays data on salaries for legal staff, assuming a senior associate at a small private practice with a $120,000 annual salary corresponding to an hourly rate of $61.53. A 1.75x multiplier is applied to approximate charge-out costs, based on the approach for labour rates in the RIS guidelines.

Development of databases and systems to monitor amounts issuers have raised	Cost involved in an issuer establishing any systems and processes to monitor the funds it has raised under various disclosure exemptions.	$10,000
Costs of preparing an information statement for investors	Total cost of preparing an information statement for issuers using current online equity fundraising platforms. Total cost of preparing a template disclosure document under CSEF regime.	$7,500 $5,000
Intermediaries		
Applying for and obtaining an AFSL	Cost of applying for and obtaining an AFSL.	$100,000[29]
Annual labour costs to comply with an AFSL	Staff hours per year. Hourly rate of staff members responsible for compliance.	104 hours $112.82[30]
Other annual costs:	Annual costs associated with ongoing compliance with licensing requirements. - professional indemnity insurance; - annual return audit; - annual licensee review; - client file reviews; - ongoing training for responsible managers; - maintaining compliance plans, procedures and systems; and - various memberships and lodgements.	 $15,000 $4,000 $3,000 $5,000 $2,000 $16,500 $1,000[31]
Provision of application form and disclosure statements	Average time to complete per issuer. Hourly rate of the staff member undertaking the process. Putting in place systems and processes.	0.5 hours $65.45[32] $10,000
Monitoring of issuer and investor caps	Hours per year spent on monitoring per issuer using the platform. Hourly rate of the staff member that would undertake the monitoring. Cost of establishing systems and processes.	4 hours $65.45[33] $10,000

29 Sourced from previous Treasury analysis of costs associated with applying for an AFSL.
30 Sourced from previous Treasury analysis of costs associated with AFSL compliance.
31 Estimates obtained from AFSL Compliance, http://www.afslcompliance.com.au/index.php/popular-information11/item/48-what-does-it-cost.
32 Based on ABS labour rates in the RIS guidelines, including employer costs.
33 Ibid.

Due diligence on issuers and management	Average time to complete per issuer. Hourly rate of the staff member that would complete the due diligence. Number of associates of the issuer on whom due diligence would need to be completed.	5 hours $65.45[34] 4 people
Provision of facilities for issuers and investors to communicate	Average time to monitor communications facility per issuer. Hourly rate of the staff member that would undertake the monitoring. Cost of establishing the facility and associated monitoring processes, per issuer.	4 hours $65.45[35] $1,000
Investors		
Monitoring compliance with investor caps	Average time to complete prior to each investment.	0.5 hours
Consideration and signature of risk acknowledgement statement	Average time to complete prior to each investment.	0.15 hours

New Zealand Model

Compliance cost	Query	Estimate
Intermediaries		
Disclosure of fee structures and interests in issuers	Average time to complete per issuer. Labour cost. Cost of establishing systems and processes.	2 hours $65.45[36] $10,000
Putting in place mechanisms to ensure appropriate disclosures depending on the level of any voluntary investor caps	Average time to complete per issuer. Labour cost. Cost of establishing systems and processes.	8 hours $65.45[37] $20,000

34 Ibid.
35 Ibid.
36 Based on ABS labour rates in the RIS guidelines, including employer costs.
37 Based on ABS labour rates in the RIS guidelines, including employer costs.

AML changes

Compliance cost	Query	Estimate
Costs for intermediaries		
Costs of applying for an Australian Market Licence, including preparation to meet substantive requirements	Hours of legal services required for new operator under current requirements. Hours of legal services required for new operator under proposed reduced requirements. Hours of legal services for existing exempt operator under proposed reduced requirements. Hourly rate for legal consultant.	2925 hours (1.5 years) [38] 1950 hours (1 year) 975 hours (0.5 years) $128.21 per hour[39]
Proving eligibility for reduced AML obligations	Hours of legal services required Hourly rate for legal consultant.	75 hours (2 weeks) $128.21 per hour[40]
Ongoing obligations for domestic markets — complying with supervision and monitoring requirements	Hours of work per year required by finance analysts. (under existing requirements – reduced requirements assumed to result in a 15 per cent reduction). Hourly rate.	4072.5 hours[41] $80.00 per hour[42]
Ongoing obligations for domestic markets — recordkeeping and disclosure of transactions and financial reports, plus maintaining written procedures regarding recordkeeping	Hours of work per year required by finance analyst. Hourly rate. Hours of work per year required for Director review Hourly rate. Hours of work required for Committee/Board approval Hourly rate.	150 hours (4 weeks) $80.00 per hour 37.5 hours (1 week) $128.21 per hour 15 hours $128.21

38 Sourced from previous Treasury analysis on Australian Market Licence modification and exemption power (OBPR ref: 16839).

39 Estimates of wage rate are for a legal partner at top tier firm $250,000 (per annum) salary. Hourly wage rate is based on an assumed average work week of 37.5 hours. Source: 'The 2015 Hays Salary Guide: salary and recruiting trends', https://www1.hays.com.au/salary/output/pdf2015/HaysSalaryGuide_2015-AU_legal.pdf

40 Ibid.

41 Sourced from previous Treasury analysis on Australian Market Licence modification and exemption power (OBPR ref: 16839).

42 Estimates of wage rate are for a finance manager based in Sydney $156,000 (per annum) salary. Hourly wage rate is based on an assumed average work week of 37.5 hours. Source: 'Hudson: Salary Guides 2015: Accounting & Finance, Australia', http://au.hudson.com/portals/au/documents/Salary%20Guides/SalaryTables2015-Aus-AF.pdf

Compliance cost	Query	Estimate
Ongoing obligations for domestic markets — providing information to market participants	Cost per document Number of documents (one per participant)	$100 30
Ongoing obligations for domestic markets — provision of annual compliance report to ASIC	Hours of work per year required by finance analyst (under existing requirements – reduced requirements assumed to result in a 15 per cent reduction). Hourly rate. Hours of work per year required for Director review (under existing requirements – reduced requirements assumed to result in a 15 per cent reduction). Hourly rate. Hours of work required for Committee/Board approval (under existing requirements –reduced requirements assumed to result in a 15 per cent reduction). Hourly rate.	150 hours (4 weeks) $80.00 per hour 37.5 hours (1 week) $128.21 per hour 15 hours $128.21
Ongoing obligations for domestic markets — providing information to regulator, including notification requirements.	Hours of work per year required by Compliance Board directors (under existing requirements — reduced requirements assumed to result in a 15 per cent reduction). Hourly rate.	400 hours $128.21 per hour
Ongoing obligations for domestic markets –maintaining technological resources to operate market at required standards.	Yearly (additional) technology maintenance costs.	$5,000
Ongoing obligations for foreign markets	Proportion of costs relative to domestic licensed market.	50 per cent

Chapter 10
Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

Corporations Amendment (Crowd-sourced Funding) Bill 2016

10.1 This Bill is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview

10.2 The Bill establishes the regulatory framework to facilitate CSF offers by small unlisted public companies, provides new public companies that are eligible to crowd fund with temporary relief from reporting and corporate governance requirements that would normally apply and creates new exemption powers to provide emerging financial markets with a more tailored regulatory and licencing framework.

Human rights implications

10.3 The Bill engages the right of freedom of expression under Article 19(2) of the International Covenant on Civil and Political Rights (ICCPR).

10.4 New section 738ZG under item 1 in Schedule 1, Part 1 of the Bill restricts the advertisement of CSF offers except in prescribed circumstances.

10.5 The restriction on advertising is part of the investor protection provisions included in the Bill. Restricting the advertisement of CSF offers except as prescribed is intended to ensure that investors make decisions to invest in CSF interests based on full and accurate information.

10.6 To balance the need to protect investors with the need to enable the flow of information, there are a number of exemptions from the advertising restrictions. The first is to allow advertisements relating to

CSF offers as long as the advertisement includes a statement that the investor should, in considering whether to invest in the offer, consider the CSF offer document and risk warning.

10.7 The provision provides for advertisements that direct potential investors to the CSF offer document and risk warning on the intermediary's platform to obtain further information about the offer that will enable them to make an informed decision on whether to invest.

10.8 There is also an exemption from the advertising restrictions to permit media businesses reporting on CSF offers in the ordinary course of their business to refer to CSF offers as long as they are not aware that they are breaching the advertising restrictions.

10.9 The CSF regime also provides for a specific communications facility that intermediaries are required to maintain while an offer is open so that investors can obtain information about an offer.

10.10 The advertising restrictions put constraints on the freedom of expression under the ICCPR but do so to protect investors. The provision balances the need to allow full freedom of expression with the need to protect investors participating in CSF offers. The provisions strike an effective balance by enabling the dissemination of information while also ensuring investors are directed to an appropriate source to obtain further information about the offer.

Conclusion

10.11 The Bill is compatible with human rights as it seeks to protect retail clients from advertisements that could induce them to make investment decisions without having all the necessary information.

10.12 To the extent that the Bill restricts the freedom of expression, this is justified because it is a reasonable, necessary and proportionate consequence of protecting investors by ensuring they can access sufficient information about the CSF offer.

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Schedule 1: Main amendments

Bill reference	*Paragraph number*
Part 1, items 1, 2, 3, 4, 5 ,6, section 9	2.55
Part 1, item 2, section 9	3.26
Part 1, item 6, item 12 in the table in section 611	3.83
Part 1, item 6, item 13 in the table in section 611	3.84
Part 1, items 7, 8, 9 and 10, heading to Part 6D.2, section 703B, section 704, and section 706	2.9
Part 1, items 7, 8, 9 and 10, heading to Part 6D.2, section 703B, section 704, section 706	4.5
Part 1, items 11 and 12, heading to Part 6D.3 and section 725A	2.10, 4.6
Part 1, item 13, subparagraph 734(7)(c)(i)	6.76
Part 1, item 14, paragraphs 738H(1)(a), (b) and (c)	2.14
Part 1, item 14, paragraph 738H(1)(d)	2.14
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Part 1, item 14, paragraph 738H(2)(b)	2.24
Part 1, item 14, paragraph 738G(1)(c)	2.31
Part 1, item 14, paragraph 738G(1)(d)	2.35
Part 1, item 14, subsection 738G(2)	2.36
Part 1, item 14, subsections 738L(6) and 738N(1)	2.43
Part 1, item 14, paragraph 738G(2)(c)	2.44
Part 1, item 14, subsection 738G(3)	2.46
Part 1, item 14, paragraph 738G(1)(e)	2.52
Part 1, item 14, section 738B	2.8
Part 1, items 14 and 25, section 738C and paragraph 766A(1)(ea)	3.8
Part 1, item 14, section 738L	3.9
Part 1, item 14, section 738A	2.6, 4.4
Part 1, item 14, subsection 738L(5)	3.27
Part 1, item 14, section 738Q	3.28
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Bill reference	***Paragraph number***
Part 1, item 14 and 34, subsection 738Q(3) and item 245E in the table to Schedule 3	3.31
Part 1, item 14, subsection 738Q(4)	3.33
Part 1, item 14, subsection 738Q(5)	3.36
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