

To: Committee Secretary
Senate Economics Legislation Committee (SELC)
PO Box 6100
Parliament House
Canberra ACT 2600

12 December 2016

Dear CSF Committee,

I have been assisting SME's to source funding since 1995 and prior to that had worked on a submission (with the help of the Hunter Technology Development Centre & Birss Consulting Group under the name Austpac Capital) to the NCSC to create an exempt market for SME's. This was lodged through the NSW Corporate Affairs Commission to the NCSC in May 1987.

All in all I have had roughly 30 years working in, thinking about and developing systems & processes for funding SME's.

Firstly there seems to be some confusion as to where ASSOBS sits. Some think we are a kind of "private equity" firm. However others, including the [World Bank](#) (see pages 18 & 46) think we are a "crowdfunding" platform. Whichever pigeonhole you prefer to put us in, there is absolute proof and no doubt that ASSOBS's model for raising funds for SME's works.

I consider the CSF Bill to be Government's **Plan "A"** and would like to propose a **plan "B"** to be seriously considered by the SELC as I have the following serious misgivings about the viability of your proposed CSF model.

1. Through my experience, equity based **crowd**funding is somewhat of a misnomer as the funds generally have not & do not come from the 'crowd'. Investors are usually people (or other companies) that know about the issuer or know one of the directors of the company.

Investors (through my experience) are those who have had 'some previous contact' with the issuer or have had some other previous 'professional or other connection' with the issuer.

It would often be a supplier, distributor, client or employee wishing to 'firm up' their relationship with the issuer by taking an investment position (often referred to as 'hard-networking').

It was a rare incident when someone 'cold' that had no previous knowledge of or connection with the company and its business, would invest.

I firmly believe (through 30 years experience) that the name Crowd Sourced Equity Funding was coined in the misguided belief that 'if you create the 'right' legislative environment so that companies can 'list' their offers to issue equity securities on an approved crowdfunding 'platform', that 'the crowd' would simply swoop on the opportunity and the issuer will raise their funds in no time. However my experience has shown that this is a long way from reality.

I believe the proposed CSF legislation would be unnecessarily complicated convoluted and costly for SME participants.

2. Cost to the SME. The very core elements of the CSF proposal such as the necessity for platform operators to hold an AFSL and also be responsible for vetting the content of an investment offer (to identify false or misleading statements) means: licensing costs, professional indemnity insurance costs, etc., all of which will need to be passed on to the SME seeking the service.

However, not wishing to dwell on the problems and costs with the CSF model, I would rather focus your attention on plan "B".

I recommend a Plan "B" should be considered. Think about the (taxpayer) cost comparison of implementing CSF as against merely changing the Class Order 02/273 from 20/12/5 to 40/12/2.

For reasons of practicality and to have a vibrant SME fund raising/job creation culture in Australia, I am of the strong belief that very little needs to change from the successful and proven usage by ASSOBS and other funding platforms that have learned (or will learn) to successfully utilise the Class Order 02/273.

One small change I would strongly recommend consists of simply changing the 20 (retail investors) to 40.

Why?

Because the amounts most SME's seek to raise is between \$300,000 to \$600,000. Under the present Class Order it is possible to raise up to about \$1.3 million before it hits a brick wall – however, should the issuer require a larger amount, this is usually enough to then fund the issuer's transition into 'proper disclosure' (a PDS) – the cost of which can be set out in the issuer's (small scale) offer document's 'use of funds' schedule.

At 40 (retail concessions) the average investment per investor would be just \$7,500 to raise \$300,000, or \$15,000 average investment to raise \$600,000.

Whereas being restricted to just 20 (retail concessions), it is just too hard to get traction in the raise at \$15,000 to \$30,000 average investment amount per investor.

From my 30 years of working in the SME funding space, I have gleaned a good understanding of what works and what doesn't.

Covering the SME funding spectrum.

We have learned that a small-scale offer under Section 708 (and assisted by a Class Order matching service operator) can be good for raising up to about \$1.2 million (before the issuer runs out of retail, sophisticated & overseas investors).

If the SME is seeking funding beyond that (\$1.2 million ceiling), they need to consider transitioning into "disclosure" (a PDS).

We now know that an ASIC registered disclosure document to raise up to \$3 or \$4 million can be produced for under \$50,000 – which can be funded from the issuer’s small scale offer.

I would be happy to spend some time with your advisers and/or Treasury to relate to them what works and what doesn’t and outline my reasons/experience and demonstrate some modeling as to why 40/12/2 (2 meaning \$2 million) can work efficiently as a funding engine.

No traction without tax relief on business investment capital:

Whichever path the Government chooses to better facilitate crowdfunding in Australia, I do not believe it will gain a lot of traction unless the new crowdfunding legislation, if and when it is introduced, is coupled with taxation relief on business investment capital.

Extension of Class Order 02/273:

Finally, I also strongly suggest that the Class Order sunset date, 1st April 2017, be extended by the ASIC for a further period.

Sincerely,

Tony Puls

Tony Puls – Background:

Tony is the founder of the Australian Small Scale Offerings Board Limited (ASSOB). ASSOB employed Paul Niederer as its CEO from 2008 through to early 2015. ASSOB is where Paul & many others gained the knowledge and expertise in funding start-ups and early-stage companies. ASSOB has since sold the Australian Licence.

Tony was the “Process” person at ASSOB. His expertise was in taking the capital seeking client from the “client capture” stage right through to the issue of share certificates/holding statements stage.

Born in Melbourne, Tony Puls has, over the years, been a strong advocate for regional development through business growth.

In 1987 Tony was involved in a regional consortium that lodged an application through the New South Wales Corporate Affairs Commission to the National Companies & Securities Commission (NCSC), before it became the ASIC, to create a type of stock market for SME’s.

He has been involved in a number of studies including the Industries Commission’s “Availability of Capital” study commissioned by Paul Keating in 1991; Financing Growth 1995; Informal Equity Investment 1997; Investment Readiness Study 1997, Study of a Growth Equity Market for Australia 1997 as well as having been invited by the Australian Securities and Investments Commission (ASIC) in 1997 to contribute

comment to the final drafting of a Class Order providing the exemptive relief on which ASSOB intermediaries and their Clients rely.

ASSOB has been the largest and most successful facilitator of early stage SME capital raising in Australia. It has unique insight into this area and runs sophisticated software. Since 2006 ASSOB has assisted around 300 Australian SME's to raise over \$140 million in capital. It fills a very real need to raise patient capital for SMEs unable to obtain, or unwilling to service, funding from banks or other lenders.

Tony is seen as the founding father of equity-based crowdfunding globally and provides consulting services to other regions wanting to establish a "powered by ASSOB" platform. Equity-based crowdfunding is somewhat disruptive to the traditional sources of business funding and provides a politically attractive way of stimulating regional development, economic growth and job creation without straining the public (taxpayers) purse. For his many years of ground-breaking work in crowdfunding, Tony has recently been awarded a life membership to the Crowdfunding Institute of Australia (CFIA).

CAMAC REPORT & some of my comments (As previously submitted to Bruce Billson):

1ST Para, page 20:

CSEF, it was argued, could be one means for dealing with what was claimed to be this systemic market failure to fund early stage companies by widening the investor base to include the retail crowd. Also, a successful initial fundraising campaign through CSEF may assist in any subsequent further financing from more traditional sources, such as venture capital or business angel investing, if this is necessary. **Furthermore, if this initial funding yields positive results, then the companies that gain traction in the market may eventually graduate to listing their securities on public exchange markets to raise more substantial sums of capital.**

This is an often wrongly-held perception, the reality is "today's stock exchanges don't raise money, they only play pass the parcel."

5th Para, page 45:

It is unclear how much demand, or interest, there will be from crowd investors for this form of fundraising, if facilitated, and whether any initial enthusiasm will be sustained over time, particularly given the losses of invested capital likely to be experienced by many crowd investors.

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2.3.2 Proprietary companies

Current barriers

As explained in detail in Appendix 2 of this report, the current barriers to the use of CSEF by proprietary companies are:

- the shareholder cap (such companies may have no more than 50 non-employee shareholders), and

- the prohibition on public offers of equity in these companies (with limited exceptions).

The limited exceptions from the offer restrictions include the small-scale personal offers exemption and offers to sophisticated investors (including very large minimum subscription offers). However, such offers do not come within the general concept of CSEF, as they lack the necessary element of offers to the crowd.

The basic flaw here is the belief that “if we can just be legally able to put an offer to the “crowd” at large, we will raise all the start-up funds we need.” “The bigger the crowd we can put our offer in front of, the more funds we will raise.” This is simply not reality.

CAMAC position

At present, proprietary companies would not be able to engage in CSEF to any significant degree, given the shareholder cap of no more than 50 non-employee shareholders and the prohibition on proprietary companies making public equity offers (with limited exceptions).

Any start-up enterprise using a proprietary company to seek funds from the crowd would be limited to utilising the small-scale personal offers exemption (no more than 20 investors in 12 months contributing no more than \$2 million, or \$5 million in some circumstances) or the exemptions for offers to sophisticated, experienced, professional or overseas investors. These options, however, are still subject to the shareholder cap and would not permit the scope of fundraising contemplated by CSEF. ***It would if the Class Order was simply changed to 40/12!!***

ASSOB had addressed this for proprietary companies by developing its own Corporate Governance Policy for early-stage Pty Ltd companies wanting to raise up to \$500,000:

Condition 1

ASSOB requires that at least one (1) Director has or has had either: previous experience in a management position of a substantial company and/or has been educated or proficient in corporate governance and/or can demonstrate having had prior experience as an officeholder of at least two (2) companies (listed or unlisted) that are still operating.

A) Previous Experience in a management position of a substantial company.

- Evidence that a Director has been employed in a Management Position of a **substantial company**.
- Evidence that the company is a **substantial company**.

To be deemed a substantial company, the company must have a minimum of two (2) traits as listed below:

Public Company

Profitable Company

Five employees or more
Recipient of a Commercialisation Australia Grant
Has received investment from an Angel Investor
Has been in operation longer than 2 years
Has received an R & D grant

OR

B) Course qualification:

- Evidence that a Director has taken a course at Chartered Secretaries Australia (CSA); or
- Evidence that a Director has taken a course at Australian Institution of Company Directors (AICD); or
- Evidence that a Director has taken an equivalent training session or completed a course in company secretarial and/ or corporate governance.

OR

C) Practical qualification:

- Evidence that a Director has been an Officeholder of at least two (2) companies (listed or unlisted) that are still operating. To be deemed as still operating, the Company must still be submitting BAS returns. Please supply last BAS return submitted.

Who is the Officeholder who satisfies either A, B or C?
Please provide evidence to satisfy this condition.

Condition 2

ASSOB requires that a Pty Ltd entity has a minimum of two (2) directors who are not immediate or related family members.
Are the current directors independent from each other?

Condition 3

Lastly, the Corporate Governance Framework Policy (as attached for you now) must be signed by this company.

If they are raising more than \$500,000 they can then afford the \$18,000 p/a approximately extra audit, compliance and reporting requirements.

On one view, a start-up or other entity with a simple business model could prepare a prospectus or an OIS relatively easily and inexpensively, depending on the type of start-up activity involved.

Can we have a rough determination of the costs for raising funds as an Exempt Public:

ASIC - Register a new Exempt Public \$ or,
ASIC - Change existing Pty Ltd to Exempt Public \$
Cost for engaging the licensed intermediary \$.....
Cost of preparing offer document \$.....
Who will be responsible for and Cost to produce holding statements/share
certificates etc. \$.....
Cost of managing Register of Members \$.....
Cost of communications to shareholders, meetings etc. \$.....
Fee charged on funds raised \$.....

Will the money go directly to the issuer from the investor or will there need to be
a custodial trust account that the money passes through??? \$..... cost??

What other costs might there be???

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3.2.4.

CAMAC considers that an exempt public company should be permitted to raise
equity under the exemptions in s 708 in addition to any fundraising it might
undertake pursuant to the CSEF mechanism.

***This is an extremely important point in the event that CSF fails to gain any
significant traction.***

***As a complimentary measure and a possible Plan "B" I strongly suggest that
the Class Order 02/273 be lifted from the current and restrictive 20/12 to the
more beneficial 40/12 and that the Class Order be extended well beyond the
sunset date of 1st April 2017.***

***As mentioned previously I would be happy to run some modeling in front of
the Committee on a 40/12/2 Class Order (yes '2' - \$2 million) - \$5million is
unattainable and impractical - only needs to be \$2 million. Beyond that it
transitions into a public company offer under full disclosure***