KING&WOOD MALLESONS

Level 61
Governor Phillip Tower
1 Farrer Place
Sydney NSW 2000
Australia

T +61 2 9296 2000
F +61 2 9296 3999

www.kwm.com

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To Nathania Nero
Lawyer, Corporations
Australian Securities and Investments Commission
Email: csf@asic.gov.au

Maan Beydoun
Senior Manager, Investment Managers and Superannuation
Australian Securities and Investments Commission
Email csf@asic.gov.au

Dear Nathania and Maan

Consultation Papers 288 and 289, Crowd-sourced funding

King & Wood Mallesons ("**KWM**") is grateful for the opportunity to comment on Consultation Paper 288, *Crowd-sourced funding: Guide for public companies* ("**CP 288"**), including:

(a) Attachment 1: Draft RG *Crowd-sourced funding: Guide for public companies* ("**Draft Company Regulatory Guide**"); and

(b) Attachment 2: Draft legislative instrument, *ASIC Corporations (Amendment) Instrument 2017/XX* ("**Draft Legislative Instrument**"),

and Consultation Paper 289, *Crowd-sourced funding: Guide for intermediaries* ("**CP 289**"), including:

(c) Attachment 1: *Draft RG Crowd-sourced funding: Guide for intermediaries*; and

(d) Attachment 2: *Proposed Appendix 9 (CSF Intermediaries) to RG 166*.

KWM has a team of market leading specialists in licensing, financial regulation, disclosure regulation, structured products, capital markets and technology whose expertise is highly relevant to start-ups, disruptors, fintech and finreg.

Our team are consulting and collaborating with crowdfunding intermediaries, startup hubs, fintech innovators, tech-sector investors and major corporates who are interested in this space, and working actively with regulators and clients on new disclosure and regulatory models.

Our submission is limited to the specific issues raised in this paper. We would welcome an opportunity to discuss our submissions with you.

Yours sincerely

Shannon Finch | Partner
King & Wood Mallesons
T +61 2 9296 2497
shannon.finch@au.kwm.com

Frances Leitch, Solicitor
King & Wood Mallesons
T +61 2 9296 2121
frances.leitch@au.kwm.com

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1 Overview

KWM is broadly supportive of the introduction of the crowd-sourced funding ("**CSF**") regime as a good first step to permit more flexible crowd-sourced funding in Australia.

KWM is also broadly supportive of ASIC's proposal to provide draft guidance for public companies, with detailed submissions on CPs 288 and 289 below.

By way of summary, on CP 288 we submit that:

1.1 Template concept is good

A template offer document (provided that it is compliant) is helpful, to assist CSF companies and standardisation across the market (see paragraph 2).

1.2 Tensions in the regulations

ASIC's guidance and the template offer document should better align with the regulations to help CSF companies understand and comply with the regulations and the minimum offer requirements (see paragraph 2).

However, we note that the points of non-compliance indicate some of the difficulties with the current draft regulations.

1.3 Extensive disclosure

The level of information required for the offer document is extensive and may not strike the right balance in the context of small companies and individual investments capped at $10,000.

1.4 Greater flexibility would produce more effective outcomes

To the extent practicable within the regulations, ASIC should promote more flexibility in how the information is presented to ensure greater accessibility for retail investors and also the success of the CSF regime (see paragraph 2.5). If the regime produces unwieldy disclosure, it will not be perceived to be supporting innovation.

1.5 New Zealand sets a positive example

By contrast - in the New Zealand regime, there is a broad exemption from regulated disclosure, and CSF intermediaries have greater flexibility to determine what is helpful to disclose, with regulatory oversight through their licensing framework.

While ASIC's position is limited by the draft regulations – we see a good balance of flexibility and accountability in the New Zealand regime, and would encourage further review to consider refinements to the CSF regime.

1.6 Seek flexibility to calculate revenue caps with accounts preparation

ASIC should seek greater flexibility in relation to the 12 month period to be used to calculate the consolidated assets and annual revenue caps to align with how companies' typically prepare their accounts and to minimise unnecessary costs (see paragraph 2.6).

1.7 Opportunity to improve the "third party consent" relief

The proposed relief from requirements to obtain third party consent to reference information should be expanded to other publicly available documentation, beyond just 'public official documents' or publications in books and journals.

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In summary, on CP 289 we submit that:

1.8 CSF intermediary obligations and liability outcomes are disproportionate

The "checks" that ASIC suggests CSF intermediaries should make place a disproportionate cost burden and risk of liability on intermediaries. It is more onerous than obligations on underwriters of major IPO's, without the corresponding benefits.

1.9 Onerous obligations combined with extensive disclosure creates unfairness

The burden of the "checks" and corresponding liability regime is exacerbated by lengthy and convoluted prescribed disclosure.

1.10 Excessive detail in reporting obligations

The level of detailed reporting by CSF intermediaries that ASIC proposes to require, on every transaction that the intermediary facilitates appears burdensome and expensive. We have suggested an alternative approach.

2 Submissions on CP 288

2.1 KWM is generally supportive of the new regime and draft guidance for CSF companies

KWM is supportive of the new CSF regime as an important first step towards developing a CSF market in Australia, striking a balance between offering some greater flexibility to start-ups and small-to-medium enterprises ("**SME's"**) (within limits) and investor protection.

KWM also considers that it is helpful and educative to have practical guidance in the Draft Regulatory Guide, including a template offer document.

2.2 Template impact on potential costs

We agree that the template document may assist CSF companies to reduce costs. However, because the regulations require a detailed offer document, the CSF regime itself has probably increased those costs for CSF companies – in contrast to the New Zealand regime.

2.3 Template impact on standardisation

The template may also encourage standardisation across the market. This is both a positive and a negative, as it (together with the prescriptive regulation) may tend to stifle the ability of CSF intermediaries to differentiate and seek to raise market standards, by developing their own templates that may connect more effectively with investors.

2.4 Compliance with regulations' prescriptive framework is challenging

The regulations[1] set out prescriptive requirements which, we understand, is intended to provide a standardised disclosure framework and minimise the need for legal advice to interpret general disclosure tests.

The template itself demonstrates the challenges of preparing accessible and meaningful disclosure in strict compliance with this framework.

Whilst the template offer document sets out the information under the four sections specified in the regulations,[2] the content, how this information is presented, and the order in which it is presented, is not consistent with the minimum requirements specified in the regulations.

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1 *Corporations Amendment (Crowd-Sourced Funding) Regulations 2017* ("**CSF Regulations**").

In addition, the Draft Companies Regulatory Guide on the content of a CSF offer document is not consistent with the strictly prescribed order set out in the regulations, and omits some requirements.[3]

Unless the regulations are adapted to provide greater flexibility, we submit that the Draft Regulatory Guide should be aligned more closely with the regulations, to avoid leading CSF companies and intermediaries into error.

2.5 More flexible regulations would produce better disclosure outcomes

The level of detail and prescription in the regulations is likely to produce poor disclosure outcomes.

While we recognise that this is a matter for Treasury, we believe that ASIC should also be pressing for greater flexibility or doing what it can to ameliorate the rigidity of the regulations.

Flexiblity to include information in separate documents, or with links to other parts of the documents would allow key information to be more apparent. It would also allow disclosure to be more adapted to being read easily on tablets and other devices.

(a) Obscuring key information

The template offer document (which does not contain the full level of information required to be included, and which has been prepared on the assumption of skeletal factual context) is already extensive and inflexible, which may obscure key information.

For instance the key information about the offer (Section 3) appears on page 10 (of 16) of the template offer document. This means that an investor needs to find their way to the back half of the document to ascertain what is being offered, and when.

(b) Incorporate detailed information by reference

We also consider that the ability to incorporate information by reference, and to make sensible use of schedule and annexures would produce clearer outcomes.

For instance, section 2 must describe the equity and debt capital structure of the company, including all classes of securities and the rights associated with the securities.

It would not be unusual for start-ups to already have Series A or B securities, which have complex terms that would need to be described (including analysis of their ranking), potentially a debt facility that would need to be described, plus a summary of the constitution and shareholders agreement – which can be extensive.

ASIC's template offer document provides no guidance on this, but even in a full prospectus – this sort of detail could be included later in the document or incorporated by reference.

A further example is that Section 2 must contain the company's (full) financial statements (not a summary, similar to prospectuses).

As it stands, if Section 2 was prepared on a fully compliant basis, the "key information" in Section 3, such as when the offer opens, may be located on page 30 or later. This is faintly ridiculous.

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2 CSF Regulations, regulation 6D.3A.02(3).

3 See for example, Draft Regulatory Guide, RG 000.127 to RG 000.158, which sets out the detail in relation to the Section 2 information. This information does not correspond to the same ordering set out for Section 2 in the CSF Regulations.

(c) **Benefits of flexibility**

More flexibility would achieve a better balance of investor protections, education of investors, accessible information and a disclosure approach that is suitable for marketing the offer, to meet needs of both CSF investors and CSF companies.

If the disclosure is too unwieldy, it will fail to engage investors and the practical purpose of giving prospectus relief will have been defeated.

2.6 The time for calculating the caps should be more flexible

To be eligible to make CSF offers, a company must meet the consolidated assets and annual revenue caps under the CSF regime.

ASIC's proposed guidance states that in calculating the revenue cap, the company must "use the 12-month period ***immediately prior*** to the time when your company's eligibility is being determined."[4]

This has the (perhaps unintended) consequence that companies will have to conduct accounting processes to determine their revenue and assets at the "test time", which may not even be month-end.[5]

While we note that this forms part of the legislative scheme – the impracticality is obvious. However, if there is flexibility to modify this through ASIC relief, the "test time" could refer to the 12 month period prior to the most recent "month-end" before the time when the company's eligibility is being determined, which would align more appropriately with typical management accounting practices.

2.7 Extending relief for references to third party statements

There is a long-standing issue with the scope of the relief from the requirements to obtain consent to reference third party information in a regulated offer document, which is not limited to CSF but which is reflected in the Draft Legislative Instrument. It has, historically, been limited to 'public official documents' or publications in books and journals (or comparable publications).

This has been causing issuers to incur costs to ascertain whether publicly available information comes from a permitted source – for instance, information on government websites; information on company websites; information in other companies published reports.

Given the rise of websites and online publishing and the decline in use of "books and journals", it should be permissible to broadly reference and use publicly available information provided that there is appropriate attribution. Clear attribution permits both the source and character of the public information to be identified.

3 Submissions on CP 289

3.1 CSF intermediary obligations and liability outcomes are disproportionate

The burden on CSF intermediaries to suffer liability as if they had deemed knowledge of deficiencies in disclosure, if their checking processes are thought not to be sufficiently rigorous is profoundly unfair – especially given this is more onerous than the liability for CSF companies and their directors.

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4 Draft Regulatory Guide, RG 000.19 (a) (emphasis added).

5 *Corporations Amendment (Crowd-sourced Funding) Bill 2017* (Cth) ("**CSF Act**"), Schedule 1; section 738H(1) provides, "*company is an eligible CSF company at a particular time (the **test time**) if all of the following conditions are satisfied in relation to the company at the test time: …. (d) the company complies with the assets and turnover test (see subsection (2))*."

This is made worse by ASIC's guidance that suggests that checks are more extensive than early industry consultation with Treasury had suggested was intended.

The process ASIC describes in paragraph C.53(c), in particular, is the verification process typically used by skilled legal advisers and companies for prospectuses – and it is a time consuming and extraordinarily expensive exercise. It is an inappropriate and impractical standard to apply to CSF intermediaries. They are not likely to be paid substantial fees (but would need to be, if they are to assume this sort of cost structure) – in contrast to underwriters of IPO's, who do not carry this burden.

3.2 Onerous obligations combined with extensive disclosure creates unfairness

The combination of unwieldy and lengthy disclosure requirements with the obligations on CSF greatly exacerbates the position described above.

For instance, it is hard to see how any CSF intermediary could satisfy themselves that the prescribed disclosure is clear, concise or effective – other to read that requirement as "*or as much as it can be in light of the prescribed requirements*".

If CSF disclosure were to be more like the slide-pack style disclosure for private placements or "low-doc" rights issues, then perhaps the burden of the regime would not be so out of proportion. However, there is little difference between the CSF offer document that the regulations will produce and a prospectus.

3.3 Purposive guidance is needed

Assuming the final regulations will reflect the prescriptive approach to content requirements, we believe that ASIC guidance should be demonstrating that they should be interpreted with a "light touch" and a sense of proportion to the sums of money involved.

Otherwise, we are concerned that the purpose of the CSF regime may be defeated.

3.4 Reporting obligations appear strangely detailed compared to other licensees

The level of detail required in the reporting obligations for CSF intermediaries in CP289.D.59 is extraordinary, and we expect that it will be costly for the intermediaries to provide this level of detailed reporting.

We have not assessed whether there are other licensees that have been subjected to that level of scrutiny of every transaction that they facilitate, other than on an individual audit basis – but it seems disproportionate.

We suggest that the ability of ASIC to individually audit these sorts of details, from time to time, would represent more balanced regulation.

4 Conclusions

Notwithstanding that we have expressed some concerns regarding a few aspects of ASIC's guidance, above, we remain generally supportive of the introduction of the CSF regime and the flexibility and market engagement, as well as the educational opportunity, that it may offer to start-ups and SME's, as well as investors.

We would welcome further discussions in relation to ASIC consultation on the CSF regime. Please do not hesitate to contact us should you wish to consult with us further in relation to our submissions.
