

## Submission to the Australian Securities and Investments Commission

### Consultation Paper 289 – Crowd-Sourced Funding: Guide for Intermediaries

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#### Introduction

This submission addresses issues raised by the *Consultation Paper 289: Crowd-Sourced Funding: Guide to Intermediaries*. Some of the suggestions that have been provided are of a policy nature.

If any of the responses require further explanations, please contact Dr Marina Nehme at the UNSW Australia, Law Faculty at [m.nehme@unsw.edu.au](mailto:m.nehme@unsw.edu.au).

#### General Observations

The Consultation Paper 289 and RG000 provide a good picture and guidance regarding the role that CSF intermediaries must play. The obligations imposed on intermediaries have to balance the intermediary's gatekeeper role and the profit-making side of the business. This is important in light of the fact that the majority of CSF intermediaries around the world have not been generating any profit, which means that they are at risk of failure.<sup>1</sup> This may especially be the case in Australia due to the small size of the market the intermediaries will be operating in. The reality remains that the majority of Australian companies are excluded from raising funds through this form of finance.

The observations made in this submission can be summarised in the following manner:

- Having a one stop shop for the rules regarding conflict of interest may be ideal;

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<sup>1</sup> Eleanor Kirby and Shane Worner, *Crowd-Funding: an Infant Industry Growing Fast* (Staff Working Paper of the International Organisation of Securities Commissions Research Department, SWP3/2014, 2014), 25-26; Eric Chaffe and Geoffrey C Rapp, 'Regulating Online Peer to Peer Lending in the Aftermath of Dodd-Frank: In Search of an Evolving Regulatory Regime for an Evolving Industry' (2012) 69(2) *Washington and Lee Law Review* 485, 506.

- An upgrade of ASIC's registers may be needed to ensure the efficiency and ease of the checks that CSF intermediaries have to comply with; and
- The data reporting obligation is welcomed but ASIC should also adopt a policy of releasing some of this data to the public. This should further be clearly stated in the RG.

### **Conflict of Interest**

ASIC has to clarify the conflict of interest obligation attached to CSF intermediaries especially in instances where the platform has never acted as a financial services provider in the past. The CSF intermediaries have a clear conflict of interest that arises due to their for-profit business model and their gatekeeper role. The conflict will be exacerbated if they are also providing financial product advice.

The consultation paper notes that the CSF intermediaries must comply with the AFS licensees' obligation regarding managing conflicts of interest. In doing so, the proposed regulatory guide refers to RG 181 and provide some supplementary guidance regarding this matter.

To ensure further clarity regarding this matter, the RG000 should at least have a table summarising the key elements that CSF intermediaries need to consider when dealing with conflict of interest situations. This will make it easier for intermediaries to fully understand this part of their obligations. The table can put the key obligations/responsibilities that intermediaries should meet with a link to RG 181 for more information.

Additionally, if an intermediary is also providing financial product advice, ASIC may need to conduct a random audit of the advice provided by the intermediary. This would ensure that the intermediary is compliant with its obligations and that the risk management systems that are in place are appropriate especially during the first year of the establishment of the intermediary. This could be done as part of ASIC's education and surveillance powers. Such a review is needed to ensure that any conflict of interest, which would be prominent in such instances, is managed and dealt with appropriately.

### **Conducting reasonable checks**

As part of its role as gatekeeper, an intermediary has to conduct checks regarding the issuers. These checks are important to ensure the quality of the issuer. The checks that need to be conducted are clear in the RG000. For the checks to be of 'reasonable standard', the checks will rely on information in ASIC's registers or on ASIC's website.

However, ASIC keeps multiple registers. Further, the media releases on ASIC's website are sometime hard to navigate. Accordingly, a review of the way intermediaries access the registers and the information on ASIC's website is needed. A first step would be for the RG

to contain information regarding the types of registers that need to be checked (including the enforceable undertaking register). Additionally, a new register may need to be created that summarise the history of a person who has in the past or is currently acting as a director or officer of a company. This will provide information to intermediaries of whether the officer they are dealing with has previously been involved in the management of a failed company. The cost of accessing some of the registers may also need to be reviewed.

## **Data Reporting Obligation**

The data reporting obligation that ASIC is putting forward is crucial to ensure the transparency of the CSF intermediary market. Further, the information that is currently being proposed is very reasonable and does not add an unreasonable burden on intermediaries. They may in fact provide more legitimacy to the intermediary's business model.

I note that the Consultation paper provides in paragraph [59] a list of data that ASIC would like to collect. This information should be added to the list that is already present in the RG000 in paragraph [RG 000.173] (including information regarding remuneration).

Additionally, it would be ideal if some of this data such as information regarding unsuccessful offers and information regarding the type of investors attracted to the platform becomes public knowledge.

The reason behind this is that a close look at the information provided by existing intermediaries around the world indicates a lack of transparency: intermediaries only publicise and promote their successful projects and do not provide information regarding unsuccessful CSF projects. The information provided by a platform is targeted toward enhancing the image of that organisation so as to attract more business, rather than being a true representation of the investments made through CSF.<sup>2</sup>

Such selective disclosure is caused by the inherent conflict of interest that an intermediary faces when acting as gatekeeper and promoting its own business. This selective disclosure may also send the message to the average investor that all businesses promoted by the platform are successful. The reality is that there is a limited flow of information that consumers can rely on to make their purchase decisions and assess the trustworthiness of the platform.

By making some of the data collected available to the public, ASIC would provide investors and businesses with additional information to consider before joining a CSF intermediary.

## **Conclusion**

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<sup>2</sup> Karima Bouaiss, Isabelle Maque and Jerome Meric, 'More than Three's a Crowd ... in the Best Interest of Companies! Crowdfunding as Zeitgeist or Ideology?' (2015) 10(1) *Society and Business Review* 23, 23-24.

The proposed RG regarding intermediaries is very informative and uses unambiguous language to detail the obligations and responsibilities of intermediaries.

Further details regarding conflict of interest may need to be incorporated within the RG. Information regarding the relevant ASIC's registers that an intermediary may need to check would be helpful to make sure a clear message is sent regarding the checks that need to be conducted. The creation of an officer's register (with a history of the person's management of companies) may ensure the integrity of the system and provide valuable assistance to intermediaries' assessment regarding the viability of the issue.

Lastly, the data reporting obligation included in the RG is very important. ASIC should make sure that such information is available to the public to enhance the transparency of the system and provide further guidance to investors and issuers regarding the intermediary.

**Marina Nehme**

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