

Birchal Submission in Response to ASIC's Public and Private Market Consultation Paper

16 May 2025

Introduction

We are grateful for the opportunity to respond to ASIC's consultation paper on public and private markets from our perspective as Australia's leading CSF intermediary.

We acknowledge ASIC's key concerns for private markets, namely opacity, illiquidity, leverage, conflicts and valuation uncertainty. Our position is that the CSF regime as it stands strikes a good balance between access and protection. It provides a current safe harbour for retail investors, including but not limited to:

- extensive disclosure obligations (including financial statements prepared in accordance with accounting standards),
- investor protections (e.g. \$10,000 limit for retail investors),
- reporting requirements,
- limitations on the inclusion of prospective financial information, and
- additional measures (e.g. related party transaction rules).

In 2022 ASIC itself described CSF as a "robust alternative for smaller companies to raise up to \$5 million in 12 months with appropriate investor protection features."¹

We note however, that the CSF regime has remained largely unchanged since its origins. This is despite the Explanatory Memorandum at the time anticipating an evolution of the regulations surrounding CSF.² As such, we have prepared some suggestions for enhancement below. We welcome the opportunity to consult further on these and look forward to the continued growth of the CSF regime.

Key recommendations

1. Expanding the Scope and Applicability of Security Classes available to the CSF Regime

Currently, companies are only able to use the CSF regime to offer ordinary shares. We believe the CSF industry can be enhanced by expanding the types of securities that can be offered e.g. bonds, Simple Agreement for Equity (SAFEs) or convertible notes.

This was within the contemplation of the Government at the time that the CSF legislation was passed, as stated in the Explanatory Memorandum.³ Both the US SEC and the UK FCA permits debt security crowdfunding in the form of SAFEs, convertible notes and peer-to-peer lending.

¹ ASIC March 2022, Report 723: Response to submissions on CP 357 Remaking relief for business introduction services Page 8.

² Explanatory Memorandum, Corporations Amendment (Crowd-sourced Funding) Bill 2016, 2.33

³ Explanatory Memorandum, Corporations Amendment (Crowd-sourced Funding) Bill 2016, 2.32

Convertible notes and SAFEs are often used as “bridging rounds” to extend a startup’s runway until their next major funding event. These securities could be more suitable for CSF companies that have already previously raised via CSF and need immediate liquidity without having to go through a full CSF raise which has onerous disclosure requirements. This method of raising capital also delays dilution of existing shareholders. We do note that convertible notes are not considered ESIC eligible investments due to their debt interest character, while SAFEs are ESIC eligible.

Recommendation

- **Regulatory Adjustments:** Amend the CSF regime to permit offerings of SAFEs and convertible notes to retail investors, with appropriate disclosure requirements to ensure investor protection.
- **Adopt standardised agreements:** Widely used industry standard templates e.g. the Australian Investment Council’s or Y Combinator’s SAFE template could be adopted to reduce the time and expense spent by companies and investors when raising.
- Consider nominee shareholder structure as set out below 2
- Consider expanding to MIS as set out below in 4.
- Consider making ESIC available to all CSF companies as set out below in 5.

2. Nominee Shareholder Structure

Currently nominee structures are not allowed under the CSF regime, which requires that each CSF investor receives ordinary shares in a CSF offer. We understand that the regime was set up in this way to protect the interests of retail investors - however, the practical implications of this requirement have surfaced several challenges which may be to the detriment of retail investors.

For example, investment opportunities that are the most attractive choose venture or private capital over CSF due to the fear that a “messy cap table” will restrict their fundraising options in future. We have observed several high quality investments who - strategically - were excited to raise through CSF, decide to pursue more traditional capital pathways for this reason, costing retail investors the opportunity to participate in the best quality deals.

Another unfortunate negative result of the practical application of this requirement is that each retail investor is a micro-shareholder, limiting their voice and influence as an investor on company decisions. A nominee structure would allow the CSF intermediary to act on behalf of all CSF investors to advocate for their interests. The CSF intermediary’s nominee entity would become a party to the company’s shareholder agreement and enters their members register as one shareholder, simplifying governance and administration. An example of where this matters is in future capital raises with professional investors who may seek to secure aggressive preferences, which make it unlikely that CSF investors will see their fair share of future returns.

We understand the matter is currently before the Administrative Review Tribunal and await the decision in that matter. In the interim, we would like to set out the benefits and protections particularly present in overseas jurisdictions including the UK that could also apply in Australia.

In addition to the above, there are also numerous benefits and protections for retail investors in the use of a nominee structure:

- Attracting the highest quality companies who see the strategic value of CSF equity. An example is Revolut, which recently achieved a valuation of £65 billionB, delivering major windfalls to the early-stage CSF investors, with potentially hundreds of new millionaires.⁴

⁴ <https://techfundingnews.com/revolut-rejects-65b-valuation-in-secondary-share-sale-what-is-the-target-ticket-size-for-the-company/>

- Additional opportunities for liquidity for retail investors. For example if a large buyer wants to buy all of the CSF shareholders out in a secondary transaction this is enabled much more simply.
- Increased shareholder power for retail investors. Retail investors have more opportunity for leverage as a collective, with a higher cumulative shareholding making them an influential party in corporate actions and resolutions.
- The administration of ownership and tracking the share price is vastly simplified.
- Protection against potential negative outcomes for example, excessive dilution by directors and major shareholders.
- Greater simplicity and compliance with the reporting obligations - reporting is shared to the nominee who then distributes to all shareholders, instead of each individual investor approaching each of their individual investments for this information. The nominee can also help enforce reporting obligations and reduce information disparity.

Recommendation

We urge ASIC to reconsider and confirm its position on nominee structures in CSF due to the increased benefits and protections this would afford to retail investors.

3. Secondaries Market

While CSF has created new pathways for startups to access capital, it presents a significant challenge for investors - liquidity. Investors often find themselves locked into their investments, with no clear way to exit until the startup either lists on a public stock exchange or is acquired. This lack of liquidity limits flexibility and can deter potential investors despite the appeal of early-stage opportunities.

Current hurdles to improving liquidity in CSF include regulatory and licensing constraints. Firstly the CSF AFSL only permits primary offers, meaning they do not cover secondary trading of securities. Secondly, there are disclosure requirements that restrict on-sale of securities within 12 months of issue. Unless on-sale relief under section 708A of the Corporations Act applies, sellers must provide a compliant disclosure document, creating a significant barrier to informal or peer-to-peer trading.

Australia continues to lag behind comparable jurisdictions when it comes to facilitating secondary market liquidity for CSF securities. In contrast, countries like New Zealand and the United Kingdom have established more advanced frameworks to support post-CSF trading. These include mechanisms such as periodic auction-based secondary sales and innovative regulatory sandbox programs developed by the UK Financial Conduct Authority (**FCA**) to encourage market experimentation and flexibility.

Particularly in the UK, CSF investors have been able to realise their value when multiple small CSF shareholders get bought out by a VC or PE firm as discussed above in the nominee structure section. CSF platforms are not required to have a formal market licence due to the nominee shareholding model. They must however provide retail investor protections such as requiring disclosure of risk warnings and valuation basis for pricing and requiring CSF platforms to conduct an appropriateness test on whether the securities are appropriate for retail investors.

On the other hand, the US permits secondary CSF security trading in a more regulated manner. The US SEC has a similar 12 month on-sale restrictions as Australia, and requires platforms to apply for a broker-dealer registration to operate an Alternative Trading Systems. Creating a secondary marketplace will reduce the risk for investors, encouraging greater investment.

Recommendation

- Introduce a dedicated regime for post-CSF secondary trading, including:
 - permission for CSF intermediaries to operate or integrate with a trading venue specifically for CSF securities;
 - the introduction of standardised on-sale relief for CSF securities with 6-12 month restrictions; and
 - introducing a sandbox regime to allow platforms to trial secondary liquidity solutions without full compliance costs, creating a collaborative and accountable relationship with CSF platforms and ASIC.
- A dedicated regime could also be utilised for ESOPs, providing liquidity to early staff members of successful companies.
- Expand the low-volume markets regime to allow for more liquidity opportunities.

4. Enhancing the Managed Investment Scheme Regime

Currently, only unlisted public and proprietary companies are eligible to complete a CSF Offer. There is an opportunity to allow Managed Investment Schemes (MIS) to leverage the CSF infrastructure.

CSF platforms in the UK & US, have significantly grown their retail investor audience by allowing the introduction of MIS, giving access to private opportunities at a much later lifecycle and closer to exit potential. The EIS100 Fund offered by Republic is a good example of a MIS which offers CSF investors passive exposure to the VC asset class at scale.⁵ Investments into the EIS100 fund aims to invest in approximately 100 campaigns that are fundraising on the Republic platform assuming the campaigns are ESIC eligible, 70% funded and have at least 100 investors.

The popularity of ETF investing in Australia has surged, largely because it offers a lower-risk alternative to picking individual stocks.⁶ Like ETFs, sector-specific funds such as the Trepont Fund, a deeptech focused fund on US-based OurCrowd's CSF platform, provides diversified exposure within targeted markets, offering a MIS that may attract retail investors.⁷

MIS could provide opportunities for retail investors to achieve greater diversification in their investment portfolio which would provide the opportunity for a more robust investment strategy similar to that afforded to wholesale investors, but at a retail ticket size.

This could be achieved by enhancing the MIS regime or amending the CSF regime to create a cohesive and lowered risk investment environment for early-stage and innovative businesses and emerging investment managers.

Recommendation

The CSF offer document requirements could be amended to include scheme-specific disclosures including roles and MIS specific risks. Alternatively, a simplified version of the product disclosure statement (PDS) could be used. This would ensure adequate consumer protection whilst reducing the administrative burden.

⁵ <https://europe.republic.com/eis100fund>

⁶ <https://www.morningstar.com.au/etfs/chart-of-the-week-etfs-have-never-been-more-popular>

⁷ <https://www.ourcrowd.com/companies/trepont-fund>

5. Expanding ESIC to all CSF companies

Under the Corporations Act, a company will qualify as an Early Stage Innovation Company (ESIC) if it meets both:

- the early stage test - covering incorporation date, expenditure, assessable income, and listing status; and
- either one of the (a) 100 point innovation test or (b) principles-based innovation test.

The 100 point test is considered a simpler test to determine a company's eligibility, and is an objective test and should be self assessed. A company can request a ruling from the ATO as to whether it qualifies under the principles-based innovation test, however this can take a long time.

In reality, most start-up companies will incur legal costs to secure independent advice from tax lawyers who provide eligibility opinions as to the company's ESIC eligibility. Retail investors, a core audience in CSF raises, lack clarity or confidence in navigating the complexity of ESIC eligibility. If a company is later deemed ESIC ineligible, they may lose access to tax incentives.

Recommendation

Our view is that companies that meet the early stage test and which qualify for CSF should automatically be granted ESIC status which will:

- Simplify ESIC eligibility: Enables CSF intermediaries to determine ESIC eligibility, and to educate retail investors on the benefits of the enhanced ESIC regime
- Increase capital flow: Encourage more investment into early stage businesses by offering attractive tax incentives like the 20% offset and CGT exemptions.
- Incentivise retail investors: Levels the playing field by giving retail investors confidence in a company's ESIC status without having to undergo their own assessment, and providing them with access to more ESIC opportunities.

6. Wholesale certificate validity for 2 years instead of 6 months

For CSF offers where an investment application is made by a wholesale client, they must supply an accountants certificate which is valid for a period of 6 months. However, where other investments are made (for example, under Chapter 7 of the Corporations Act 2001) an accountants certificate is valid for up to 2 years.

This discrepancy arises because reg 7.6.02AF of the Corporations Regulations does not make it clear whether the modification to the renewal period for accountant certificates applies to accountant certificates provided for the purpose of CSF Offers. ASIC's website currently states that under Chapters 6D and 7, accountant certificates are valid for up to two years after they were issued.⁸

Recommendation

Amend reg 7.6.02AF to include Chapter 6D.3A. This will allow for wholesale certificates provided for an investment into a CSF offer to remain valid for a period of 2 years.

⁸ <https://asic.gov.au/regulatory-resources/financial-services/financial-product-disclosure/certificates-issued-by-a-qualified-accountant/>

7. Stronger enforcement on annual reporting obligations

Under the Corporations Act, companies with CSF shareholders are required to prepare an annual financial report and directors' report in accordance with Australian accounting standards and lodge these reports with ASIC by 31 October each year. These disclosures are essential to protect retail investors and ensure transparency and accountability from companies that raise capital through the CSF regime.

As a CSF intermediary, Birchal takes these obligations seriously. Each year, we conduct an audit of all companies that have previously raised funds via our platform to assess their compliance. In our most recent audit, conducted in January 2025, we found that approximately 60% of companies had not lodged the required reports with ASIC.

To support compliance, Birchal:

- sends reminders to all CSF companies prior to the 31 October deadline, advising them of their annual reporting obligations.
- contacts companies again in January the following year, after our audit, if they have failed to lodge their reports, reiterating their legal responsibilities.

Despite these efforts, we frequently receive queries from investors who:

- cannot contact the company they've invested in; and
- cannot access the company's annual report, leaving them with no visibility into the performance or status of their investment.

This lack of transparency undermines confidence in the CSF sector, and contradicts the regime's intent to create a well-regulated, retail-accessible investment environment.

As discussed above, we believe that allowing a nominee structure would result in much higher compliance with these reporting obligations. In the absence of allowing a nominee structure, we recommend stricter enforcement.

Recommendation

We believe stricter enforcement of this obligation will build confidence in the integrity of the CSF market, as well as ensure transparency and accountability from CSF companies. We would recommend that ASIC increase communication to CSF companies regarding their reporting obligations, and implement penalties where there is persistent non-compliance.