AUSTRALIAN INVESTMENT COUNCIL

# AUSTRALIA'S EVOLVING CAPITAL MARKETS

## RESPONSE TO ASIC DISCUSSION PAPER ON THE DYNAMICS BETWEEN PUBLIC AND PRIVATE MARKETS

APRIL 2025

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## ABOUT THE AUSTRALIAN INVESTMENT COUNCIL

The Australian Investment Council is the national peak body for private capital. We represent and support the leading domestic and international private capital firms operating in Australia. Our members span private equity, venture capital, private credit, institutional investors – including profit-for-member superannuation funds - and the professional services firms that provide expertise to the industry.

Our members make a substantial contribution to the Australian economy and businesses by investing in innovation, backing entrepreneurship and enabling established businesses achieve their growth ambitions. Private capital investment contributes approximately three per cent of Australia's GDP, backs more than 1,100 businesses and supports more than 600,000 full-time jobs.

Our purpose is to enable private capital to invest in Australian ideas, businesses and communities. We do this by advocating for our members, providing forums for connection, and equipping our members through education, research and information.

## FOREWORD

The Australian Investment Council appreciates the opportunity to make this contribution to the national discussion about Australia's evolving capital markets. Our submission is primarily focused on private markets, and private equity, venture capital and private credit in particular. Where appropriate, we have made some submissions about public markets.

Australia is in a global competition for capital. The global megatrends of digitalisation, decarbonisation, deglobalisation and demographic change present risks and opportunities for all countries. This is occurring at the same time as low economic growth projections for Australia, necessitating a focus on lifting GDP per capita to maintain Australia's relatively high standard of living. To grow, it will no longer be enough to be an attractive place to invest: Australia now needs to be exceptional.

Governments have clarified that economic and productivity growth – and therefore preservation of living standards – must come from private sector investment. This necessitates a healthy, high-functioning capital markets: both public (listed) and private (unlisted). When operating well, listed and unlisted capital markets promote and facilitate business investment; support wealth generation for Australians (whether directly or through retirement savings); and meet areas of unmet community need.

The Council recognises the role of regulatory oversight in healthy, high-functioning capital markets. 'Appropriate' regulatory settings, based in materiality and likelihood of risk, help protect investors and safeguard against systemic risks. Australia already has a wide range of legislation and regulations covering public and private market investments; potential future reforms need to take into account the opportunity cost of increased or more complex compliance burdens.

### IPO downturn is cyclical, and private credit poses no systemic risk

The Council notes the conclusion drawn in the Discussion Paper (DP) that the current downturn in initial public offerings (IPOs) on the ASX is cyclical. This is certainly borne out in the Figure 4 (page 14): periods of negative net listings have occurred during economic downturns such as the recession of the early 1990s, the global financial crisis of 2008 – 2009, the COVID-19 pandemic of 2020 and the current period of post-pandemic global economic downturn.

It is also important to note that activity on the ASX is not just IPOs: Australia was the most active exchange for follow-on offerings in 2023.

The Council notes the conclusion that Australia's private credit markets pose no systemic risk to Australia's financial system. This is also borne out in the sheer size of Australia's $2.259 trillion debt market, of which private credit is a minute portion. While the growth of private credit is remarkable, it is important to note that it is off a negligibly small base and is not expected to achieve the penetration it has in other jurisdictions.

These two conclusions contained within the DP and accompanying economic research would suggest that it would be prudent not to rush to change current regulatory settings.

Every piece of regulation comes with an opportunity cost: that is the diversion of resources away from productive activity.  For small and medium businesses this diversion can be so great that it makes certain businesses unviable. This would be counter-productive against a broader policy objective of a more competitive and dynamic economy.

It is important to note that a feature of Australia's private capital funds management industry is a large number of homegrown, domestic firms with strong investment track records – and small businesses in their own right.  Our regulators have a responsibility to support competition and dynamism by ensuring that regulatory regimes do not oppress smaller, domestic fund managers.

### Different investors require different protections

It is also prudent for ASIC to query whether investors require greater protection.  In answering this question, it is crucial to understand the different types of investors active in public and private markets:

- Institutional investors
- Wholesale and sophisticated investors
- Retail investors

With respect to private capital – that is, private equity and venture capital – the overwhelming majority of investors are institutional or wholesale. Institutional investors are highly experienced, seasoned investors with the capacity, capability and competence to make informed decisions. When investing - whether that be allocation of capital to a private capital fund, or a private capital fund investing in a portfolio company – there is a commercial decision being made by informed counterparties.  The Australian Financial Services Licence (AFSL) regime brings with it regulatory and disclosure compliance obligations for fund managers operating in public and private markets.

Wholesale and sophisticated investors are covered by an investor protection regime that, while less onerous than that for retail investors, offers necessary protections.  Fundamental to that regime is the capacity, capability and competence of financial advisers who make the wholesale / sophisticated classification and work with the investor on their risk appetite.  In financial advice, much reform has taken place over the past 10 or so years.

Relatively speaking, retail investment into private equity and venture capital is limited. There are higher levels of retail investor participation through direct investing into private credit funds. However, we also note the existence of an investor protection regime and recommend that this regime be reviewed to confirm whether there are any shortcomings.

### The role of regulation in Australia's capital markets

Clearly regulation and regulatory oversight plays a role in the healthy and efficient functioning of capital markets.  However, it is important to stress that the regulatory benchmark should not be zero failures.  Failures are inevitable.  Not every company will succeed and where failure occurs, there are impacts for investors, financiers, staff, customers and other stakeholders.  In setting appropriate regulatory frameworks, the following non-exhaustive list of questions are highly relevant:

- Does the current regulatory framework support a dynamic and high-functioning investment market?
- Is there a market failure to be addressed that would directly cause significant investor losses or undermine overall market confidence?
- Is there evidence to suggest that such failure is likely and material? If so, what would be the consequences and for whom?
- How and where does the existing regulatory framework fall short?
- Is new regulation the only and best solution?
- What is the opportunity cost of regulation in terms of productivity, innovation, competition, speed to market and competitiveness?
- What are the compliance costs associated with a new regime, particularly for small and medium enterprises?

The Council recognises that in order to answer these queries, regulators need access to data. It is reasonable to expect regulators to be clear about what data they require and the reasons why they require it.

### Next steps and actionable suggestions

The cost of and allocation of resources to complying with regulatory requirements continues to increase in Australia. Excessive or inefficient regulation can create an environment in which it becomes uneconomic to continue to operate. These outcomes are not in the national interest.

The DP is a thoughtful initial exploration of ASIC's observations. Before any regulatory solutions are proposed the Council encourages further work, along with a more granular evidence base, including:

- identification of areas of material risks;
- examination of current regulatory settings and where they fall short;
- specific areas of disclosure and the reasons why it is required; and
- an opportunity cost to benefit analysis of introducing new regulatory and disclosure requirements.

This would support further support a principles-based, evidence-driven approach.

The Council respectfully suggests that the next stage of policy work in this area should: answer questions such as the ones noted above; assess the existing regulatory frameworks to identify material shortcomings; and explicitly state issues that may have arisen. This could be presented to stakeholders in an Issues Paper that brings together:

- themes arising from stakeholder responses to this DP;
- the outcomes of ASIC's review of the relevant existing regulatory frameworks; and
- themes arising from ASIC's current bilateral work with market participants, which is noted in the DP.

### *Further actionable suggestions*

In addition to the next phase of policy work noted above, ASIC could also consider the following:

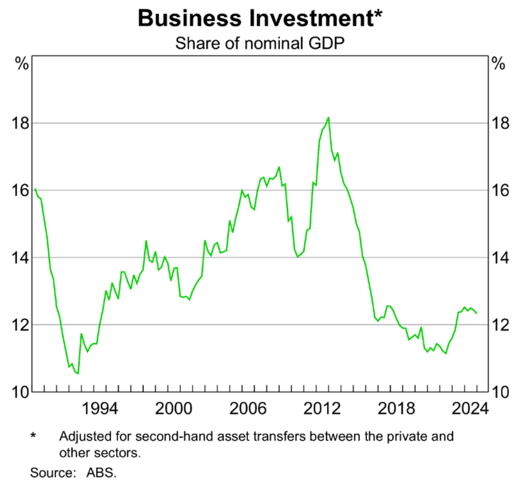
- mapping existing data that is collected, or accessible - either by ASIC or other financial regulators - in relation to private markets;
- reviewing the existing retail investor protection regime to identify any shortcomings and the materiality of such shortcomings;
- consider targeted reforms to public markets such as:
  - streamlining IPO processes;
  - facilitating the use of dual-class share structures for founder-led or tech businesses; and
  - reviewing ASX listing rules for flexibility, especially for smaller or industry-specific companies

- monitoring market developments using existing supervisory activities and reporting regimes, and regularly update stakeholders about the likelihood, scale and materiality of emerging risks as these become clearer; and
- reforming regulatory frameworks overseen by ASIC, such as RG97, that would further unlock allocation to private markets investments, notably start-ups and growth businesses, in support of Australia's productivity challenges.

## THE ROLE OF FINANCIAL MARKETS IN AUSTRALIA'S ECONOMY

Financial markets underpin the strength of Australia's economy. The efficiency of financial markets has a significant bearing on Australia's ability to attract, retain and deploy capital into productive endeavours.

Australia faces a productivity and growth challenge. The IMF projects Australia's gross domestic product (GDP) growth to be 1.6 per cent in 2025[1]. This is a downgrade from their previous projection of two per cent, driven by current global trade uncertainty. Business investment as a share of nominal GDP is well off the peak levels seen in the mid-2010s[2].




Australia is not alone in confronting the challenges posed by rising inflation, tighter financial conditions, geopolitical uncertainty and shifting investor behaviour. As International Organisation of Securities Commission's (IOSCO) 2023 report highlights, these economic headwinds are global in scope, influencing private capital markets from North America to Europe and the Asia-Pacific.[3]

Against this backdrop, Australia's capital needs continue to grow. The four global megatrends of decarbonisation, digitalisation, deglobalisation and demography present risks and opportunities. As an example, the cost of health, aged and disability care is expected to grow by more than $115 billion by 2062[4].

Australia's major political parties have tasked the private sector with driving the investment needed to boost productivity and maintain the country's high standard of living[5],[6]. To meet this expectation, Australia's public (listed) and private (unlisted) capital markets need to work efficiently and effectively.

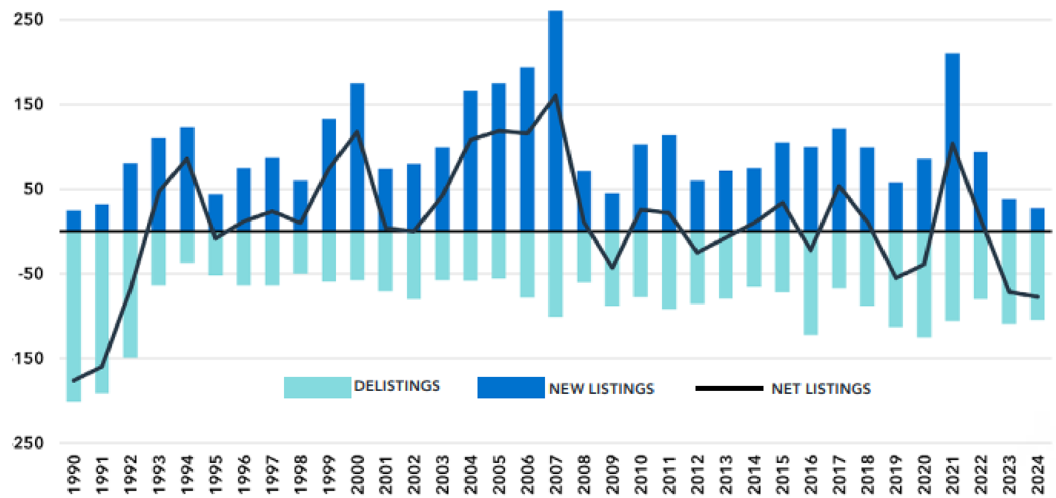
[1] International Monetary Fund 2025. World Economic Outlook Database
[2] Reserve Bank of Australia 2025. Monthly Chart Pack.
[3] International Organization of Securities Commissions (IOSCO). 2023. *Report on Good Practices for Consideration in the Regulation of Private Finance*.
[4] Australian Investment Council and EY. Funding the Future (citing the Intergenerational Report).
[5] Taylor, Angus. Speech to National Press Club, 2 April 2025.
[6] Read, Michael. Chalmers admits business must pull Australia out of its growth slump. AFR, 4 December 2024

## THE ROLE OF PUBLIC MARKETS

Australia's listed markets play a vital and multi-faceted role. From a private markets perspective, the ability to list an investee business on an exchange is an important pathway for realising the value of an investment and delivering returns to investors.

We note ASIC's conclusion that the current downturn in initial public offerings (IPOs) is cyclical. This would certainly accord with the chart on page 14 of the DP:

**Figure 4: Number of new public company listings, delistings and net listings on the ASX (1990–2024)**




Sources: Morningstar DatAnalysis and REP 807
Note: These listing numbers do not include listed investment companies (LICs), LITs and real estate investment trusts (REITs) traded on the ASX.

Periods in which net listings were negative coincided with the recession of the early 1990s, the global financial crisis of 2008 – 09 and in the lead-up to, and during, the COVID-19 pandemic. The current downturn in IPOs on the Australian Securities Exchange (ASX) correlates to a broader economic downturn which is not surprising. The level of investor support for an IPO, which is influenced by confidence, is a key determinant in whether to list or not.

It is important to note that the listed market does not suit all types of business. For example:

- businesses that require long-term, patient investment, such as infrastructure, may be better suited to unlisted markets that are not susceptible to daily fluctuations;
- businesses that require turnaround or transformation where the process of achieving a long-term positive outcome is not compatible with the shorter-term vagaries of listed markets; or
- businesses on a process of rapid expansion, at a pace that is necessary yet faster than what listed markets may have tolerance.

This is not to say that such businesses will never be suited to listed markets; often, whether the business is best supported by listed or unlisted markets is linked to where it is in its lifecycle.

It is also important to note that the daily mark-to-market nature of listed markets can be a drawback. This was evident in the extreme volatility in listed markets when country-by-country tariffs were announced by the US Government even though the final form of the policy announcement was yet to be fully known. This kind of volatility can lead to short-term decision making and undermine confidence.

## THE ROLE OF PRIVATE MARKETS

Private markets provide a much-needed source of capital to a range of businesses, from early-stage tech businesses right through to large, mature businesses undergoing major transition or long-term change.

Private markets investing, such as venture capital and private equity (PEVC), provide patient, long-term capital. Capital is deployed either directly or through intermediaries such as fund managers. While there are some large, well-known companies with PEVC investors, the majority of investment is in small and medium-sized businesses.

During the life cycle of the investment, the company receives injections of financial capital and intellectual capital such as expertise and networks. These are actively managed businesses where the investors are involved in the strategic direction and growth of the business. At the end of the investment period, the business may be listed, acquired by a strategic buyer, or acquired by another investor with the appetite and means to support the next phase of growth.

The types of businesses to which private capital is well suited include:

- early-stage businesses that require investment to move from R&D to commercialisation to revenue phases;
- smaller businesses that do not have the scale or liquidity for public market investors;
- businesses that have solid fundamentals but require considerable investment to undergo transformation or turn around performance;
- businesses, often small or medium-sized, where the financial and human capital cost of listing and being listed outweighs the benefits; and
- businesses on a rapid trajectory that need to be more agile than what they can be in the listed environment.

Often these are businesses where a higher level of risk may be required to achieve growth plans, develop product or address underperformance.

In Australia, there are many examples of PEVC investing:

- backing technologies and entrepreneurs;
- future-proofing heritage industries;
- building businesses that can credibly compete against larger incumbents;
- creating jobs, particularly in small and medium-sized businesses;
- growing wealth for businesses, individuals and communities; and
- delivering higher returns for retirees.

As mentioned above, transitioning to the listed market, either in Australia or elsewhere, may be an appropriate step at a future point in the business' life cycle.

In Australia, PEVC investments contribute three per cent to Australia's GDP on a gross value-added basis[7] by backing more than 1,100 businesses (mainly small and medium sized). This is half of the GDP contribution levels seen in the US and UK (6.5 and six per cent respectively)[8]. This presents missed opportunities for higher-returning investments and, given the tens of thousands of privately held businesses in Australia, a risk that high-potential businesses are not able to access long-term, patient capital.

There are already a range of impediments to PEVC investing reaching the levels seen in the US and UK including superannuation regulation, foreign investment processes, tax settings and the efficacy of structures that enable the pooling of capital. With the right policy settings, an additional A$60 billion in private capital could be mobilised into Australian businesses by 2030, potentially generating over 600,000 new jobs.[9] This would take Australia closer to the contribution made by PEVC investing in the US and UK.

### The role of private credit

Private credit plays an important role in Australia's overall debt markets. Private credit supplements traditional bank credit in Australia's economy to deepen credit liquidity. It works in situations such as complex business structures in need of bridging finance, where start-up or fast growth companies have difficulty borrowing from established banks or where companies are restructuring.

Types of private credit funding include:

- *Senior direct lending*: Direct lending funds provide loans to mid-market companies. The lenders raise capital directly from investors to fund a portion of the loan in a syndication or to fund the entirety of the loan with little or no syndication to the institutional loan market. The loans are held in a General Partner/Limited Partner style investment fund by the lender. They are typically illiquid, senior secured loans with a range of maturities between three to seven years and with floating coupon rates.
- *Mezzanine financing*: Mezzanine financing bridges the gap between debt and equity that gives the lender the right to convert an equity interest in the company if there is a payment default. This form of financing is commonly used by larger, more established companies to fund growth projects and to expand their businesses.
- *Distressed debt*: Distressed debt refers to bonds bought from companies experiencing cash flow issues. These bonds are usually bought at a significantly discounted rate and investors in a company's distressed debt will often end up with some control of the business. Distressed debt investors aim to ensure the businesses they invest into remain viable and have the potential for future growth.
- *Special situations*: Special situations investors rely on a one-time, atypical event with the potential to materially impact a company's value either positively or negatively. This

[7] Australian Investment Council and EY. The ABC of Private Capital, 2025

[8] Australian Investment Council and EY. Funding the Future, 2024

[9] Australian Investment Council and EY, 2024. *Funding the Future: Meeting Australia's Investment Challenge, Boosting Jobs and Turning Ideas into Thriving Businesses*

type of investing can stem from companies undergoing divestments, mergers and acquisitions, liquidations, restructures, share buy-backs, rights offerings and major legal cases.

- *Venture debt*: This type of financing is generally used by start-up companies. Investors are compensated with the company's warrants on common equity as start-ups generally do not own enough assets to provide collateral. Venture debt is usually provided to start-ups that have already successfully completed several fundraising rounds but do not have sufficient cash flows to obtain conventional loans

The growth of private credit globally is, in part, due to highly regulated traditional lenders being unable to meet the demand to provide capital support for businesses across their life cycle. As the DP has noted, private credit as an asset class has also grown substantially in Australia although it is important to note that this is off a minute base.

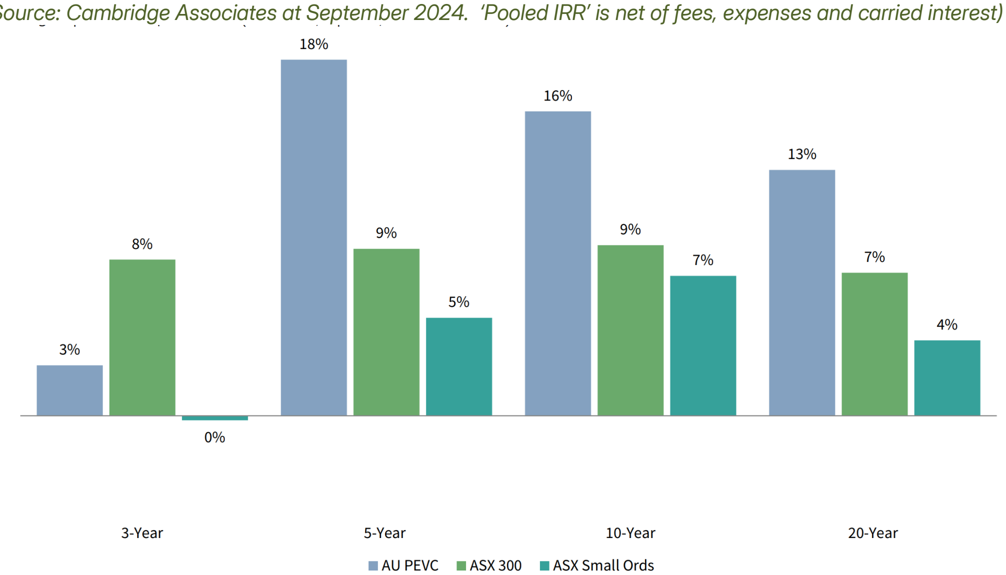
## PRIVATE MARKETS AS AN INVESTMENT CLASS

For the most part, private markets is an institutional and sophisticated investor asset class. The typical investor would be a superannuation or pension fund, sovereign wealth fund, endowment fund, fund of funds or insurance company. These are investors with long-term investment horizons and, in return, require an illiquidity premium for their investment.

According to analysis by global investment firm, Cambridge Associates, PEVC has outperformed Australian listed markets over five, 10 and 20 years. This makes it an important source of retirement income for superannuation and pension fund members.

***Figure 1: PEVC index pooled IRR vs public market equivalents over time***

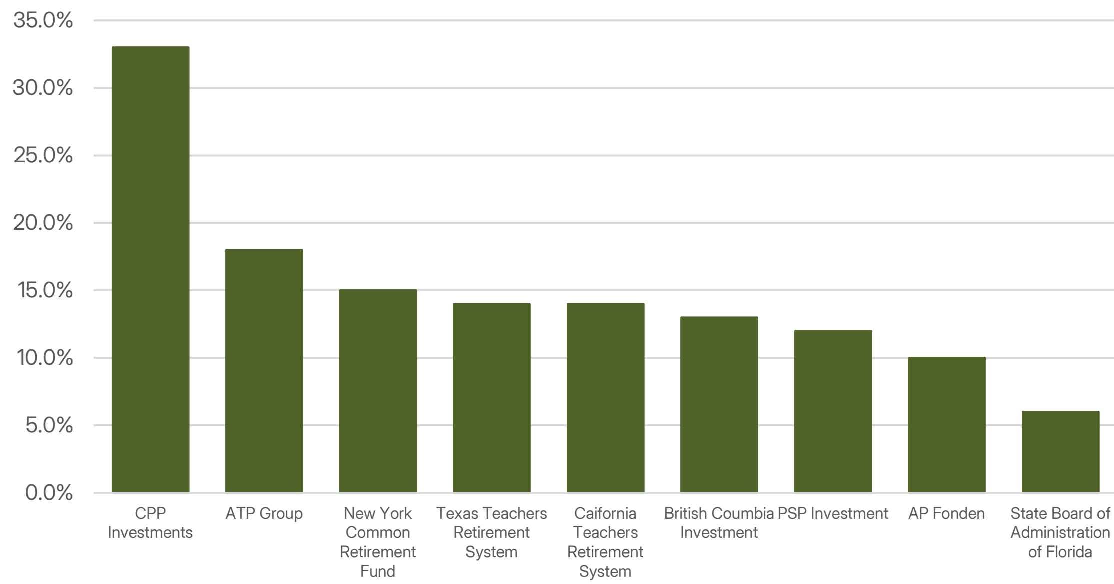
*(Source: Cambridge Associates at September 2024.  'Pooled IRR' is net of fees, expenses and carried interest)*




PEVC also provides portfolio diversification as it is not closely correlated to listed equity and fixed income. Based on internal analysis, the average correlation of PEVC compared with cash, Australian and global bonds, and Australian and global listed equity is approximately 0.08.

Despite its attractiveness from long-term returns and portfolio diversification perspectives, Australian superannuation funds have relatively low allocations to PEVC when compared with international peers. The average allocation across MySuper products is 4.4 per cent which is below allocations to the best performing pension funds internationally.

***Figure 2: Allocations to PEVC[10]***




| Rank | 1 | 7 | 4 | 9 | 5 | 8 | 3 | 2 | 10 |
|---|---|---|---|---|---|---|---|---|---|
| AUM $A (at 2023) | $643b | $151b | $317b | $282b | $464b | $259b | $271b | $414b | $346b |

***Table 1: Examples of PEVC allocations by profit for member superannuation fund[11]:***

| Super fund | Allocation (%) | Strategy |
|---|---|---|
| HOSTplus | 10.0 | Balanced |
| Australian Retirement Trust | 7.4 | Balanced |
| Aware Super | 6.0 | Balanced |
| Australian Super | 5.1 | Balanced |
| HESTA | 5.0 | Balanced Growth |
| Cbus Super | 3.0 | Growth |
| UniSuper | 2.5 | Balanced |
| REST Super | 2.0 | Balanced |

[10] Mandala research. Allocation is either per asset allocation policy or actual allocation; Performance is measured as the 10-year net annualised return (2013 – 2022).
[11] Sourced from superannuation fund public disclosures

While there is scope for superannuation funds to allocate more to PEVC, the portability of superannuation member accounts means funds need to maintain appropriate liquidity buffers.  This provides a natural 'ceiling' for allocations to private markets asset classes.

### Other investor types

Around the world, there is a growing trend among family offices and high-net wealth investors to invest in PEVC. These investors are also attracted to the returns and diversification benefits provided by PEVC.

In some cases, these types of investors wish to support businesses such as start-ups and early-stage businesses, driven by motivations such as wanting to 'give back' or to back innovation in areas of personal interest.

Retail investment in PEVC in Australia is relatively nascent. There is greater retail investor participation in private credit in Australia, although, compared with the size of the overall size of Australia's debt market, this remains relatively small.

## THE ROLE OF REGULATION AND EXISTING REGULATORY REGIMES

Regulation plays a crucial role in setting the parameters between which capital markets operate. There is a delicate balance to strike in setting appropriate regulatory frameworks between protecting investors and minimising the cost and burden for regulated entities. There is an expectation to "ensure that guidance is not unduly prescriptive, and does not limit businesses' discretion and flexibility to operate in the manner they see fit while still complying with the law"[12]

The characteristics of the investor being protected is a highly relevant consideration. As a general principle, where there are informed counterparties transacting with one another, regulation has less of a role to play. The ability to provide suitable monitoring and oversight is also a relevant factor.

Australia has numerous existing regulatory requirements that are relevant to private markets participants and to monitoring and supervision. These include (but are not limited to):

- Australian Financial Services License (AFSL) requirements;
- Australian Credit Licensee (ACL) requirements;
- Statutory, common law and equitable (including fiduciary) duties under trust law;

These regimes and duties give ASIC considerable existing power to monitor, supervise and compel private markets participants.

[12] Statement of Expectations, 2021.

There are additional regulatory obligations to protect retail investors, which is entirely appropriate. These include (but are not limited to):

- General Licensee Obligations under s 912A of the *Corporations Act*;
- Design and distribution obligations under Part 7.8A of the *Corporations Act*;
- Prohibitions Against Misleading or Deceptive Conduct

For superannuation fund members, their fund trustees are bound by the *Superannuation Industry (Supervision) Act*. The general covenants in s52(2) require the trustees to invest prudently, act in the investors' best financial interests, and avoid conflicts.

A more detailed discussion of existing applicable regulatory regimes and frameworks appears in Appendix 1.

## ASIC'S OBSERVATIONS ABOUT PUBLIC AND PRIVATE MARKETS

We note the DP makes observations in the following areas:

- Systemic risk and market integrity
- Access and investor classification
- Transparency and disclosure

### Systemic risk and market integrity

***ASIC concern***: Growth and interconnection—particularly with superannuation funds—may elevate systemic risk. [13]

***Council view***

According to the IOSCO, private capital generally presents low systemic risk due to its structural characteristics, such as its illiquid nature and long-term investment horizons. [14] Private equity and venture capital investments are largely held in closed-end funds focusing on long-term value creation and set risk-return expectations. Such features reduce their interconnectedness with the broader financial system, thereby mitigating potential contagion risks.

The Reserve Bank of Australia (RBA) has acknowledged that the private capital sector poses minimal systemic risk to financial stability, citing its low interconnectedness with the broader financial system.[15] As a result, the sector is seen as relatively low-risk in terms of contagion, which bolsters the argument that additional regulation may not be warranted at this stage. This view aligns with the IOSCO perspective that private capital's impact on systemic risk remains manageable.

[13] ASIC, pp. 16, 29
[14] IOSCO. 2023b. *Private Finance and Markets*, pp. 6–7
[15] RBA. 2023, October. *Financial Stability Review*, p. 36

*Private markets investment by superannuation funds*

Private capital has long been an essential component of the Australian superannuation system, which allocates approximately 16.6 per cent of its funds to private markets, according to The Association of Superannuation Funds of Australia (ASFA). PEVC and private credit is a subset of this allocation which also includes other asset classes such as infrastructure.

The diversification benefits of private assets, along with the potential for elevated returns and exposure to the illiquidity premium (ie: the additional return paid to investors for holding assets that are not easily tradable or convertible to cash), make them an integral part of long-term investment strategies aimed at sustainable retirement outcomes. Fundamentally, the relationship between a superannuation fund and its members is a fiduciary one, a concept recognised in statute and common law. Further, the objective of superannuation has been enshrined in legislation in the *Superannuation Objective Act 2024*.

The Australian Prudential Regulation Authority (APRA) oversees the $3.5 trillion superannuation system, ensuring that funds meet rigorous risk management and investment practices. These funds have consistently delivered an average growth rate of around eight per cent, a testament to the long-term performance of their investments—including those in the private capital market.

In addition, superannuation funds undertake comprehensive due diligence processes before investing in private markets, including background checks, performance analysis, investment strategy reviews, and a thorough evaluation of compliance, financial health, and valuation methods. Governance processes exist, such as investment committees. These efforts ensure that the sector's scrutiny of risk and valuation meets the expectations set out in existing legislative and regulatory frameworks.

Given the existing framework of regulations and the conclusions drawn by IOSCO, the RBA and ASIC's 'cyclical vs systemic' analysis, it would seem appropriate for financial regulators to maintain a watching brief by using existing supervisory activities. Further layering of regulation at this juncture risks undermining the long-term returns for super funds and investors and potentially stymying the allocation of capital to productive economic activities that are in the national interest.

*Leverage and risk management*

Regulatory assessments suggest the sector's use of leverage is generally strategic and well-managed. The DP acknowledges the importance of monitoring leverage levels,[16] but the Council notes IOSCO's observation that leverage tools such as subscription lines are primarily used to enhance liquidity management and operational efficiency, rather than to take on excessive risk.

[16] ASIC, p. 23

Subscription lines—short-term loans secured against committed investor capital—are a standard liquidity tool in private markets. They support operational efficiency and timely investment execution. IOSCO notes these facilities are typically well-managed within structured limits and not a source of systemic risk. In other words, these mechanisms are typically embedded within robust fund structures that include clear limits, governance safeguards, and risk management protocols.[17]

### *Liquidity controls*

Redemption risks in semi-liquid structures[18] are well understood in the sector. IOSCO has noticed that private capital funds use methods such as limiting when investors can take their money out (redemption gates), requiring advance warning before withdrawals (notice periods), and separating riskier assets into special accounts (side pockets).

These tools help align investor expectations with asset liquidity[19] providing a globally accepted framework for responsible access design. These mechanisms help the inclusion of sophisticated investors through diversified or pooled investment structures allowing those who may not meet the ‘wholesale' investor test to gain access to private capital markets. The approach should, therefore, be encouraged through best practice guidance, not new mandates.

### *Valuations*

The relationship between a fund manager and the limited partners investing in their fund is a fiduciary one. As part of that relationship, the fund manager is required to regularly report investment performance across a range of metrics as well as other information. Many limited partners place non-financial expectations in areas such as diversity, equity and inclusion (DE&I) and environmental, social and governance (ESG).

In Australia, where the overwhelming majority of investment in PEVC and private credit is by institutions, investment decisions are made by qualified investment professionals. They have the qualifications and experience to rigorously make investment decisions, assess performance and interrogate. They also have the means and resources to seek independent valuations. In other words, they have capacity, capability and competence.

For PEVC, there is an international valuations standard: the International Private Equity and Venture Capital Valuation (IPEV) Guidelines. The IPEV Guidelines focus on fair value measurement consistent with both International Financial Reporting Standards (IFRS 13) and US Generally Accepted Accounting Principles (US GAAP, ASC Topic 820). They define fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date," mirroring the definitions in IFRS 13 and ASC 820.[20]

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[17] IOSCO 2023, pp.40-41

[18] ASIC, p. 22

[19] IOSCO 2023, p. 37

[20] International Private Equity and Venture Capital Valuation Guidelines (IPEV). 2022. *International Private Equity and Venture Capital Valuation Guidelines – December 2022*. Fair value definition on page 13.

The IPEV Guidelines are endorsed by numerous private equity and venture capital associations worldwide, including the British Private Equity and Venture Capital Association (BVCA), Invest Europe, the Australian Investment Council, the American Investment Council and Institutional Limited Partners Association (ILPA). This widespread endorsement and longevity indicates their credibility and international recognition. These standards are not static: they were first published in 2012 and updated in 2015, 2018 and 2022.

For private credit, IFRS9 (amortised cost rather than fair value) is used as an appropriate valuation method for private credit assets. It is also used by Authorised Deposit-Taking Institutions and informs the Alternative Investment Managers Association's *Guide to Sound Practices for the Valuation of Investments.*

*Conflict management*

Potential conflicts of interest [21] are already managed through structured governance, disclosures and alignment mechanisms. IOSCO confirms these practices are industry standard across global markets.[22]

In Australia, private fund managers are typically bound by AFSL requirements. Consequently, these sponsors are subject to a range of regulatory obligations, including statutory duties under the *Corporations Act* to have adequate arrangements for managing conflicts of interest and risk management.

### Access and investor classification

**ASIC concern**: Misclassifying retail investors as wholesale clients compromises their rights and protections. [23]

**Council view**

Classification of investors is relevant to all financial products and the DP does not make clear why it would warrant special mention in the context of private markets investing. The Council would suggest more information is provided on this topic in the next phase of policy development.

It is worth noting that there is an existing framework for the classification of sophisticated and wholesale investors, under which a qualified accountant is responsible for making the classification. There is also a series of Regulatory Guides in relation to product disclosure obligations. If there are deficiencies with these frameworks, the Council suggests these be reviewed, with the customary consultation processes.

[21] ASIC, p. 22

[22] IOSCO, p. 29

[23] ASIC, p.42

Should ASIC embark on such a process, the Council suggests due consideration be given to the important role that wholesale and sophisticated investors play in providing funding to start-up and earlier-stage businesses. The size of Australia's superannuation pool and consolidation has led to a shift away from smaller cheque-size investments. Changes to regulatory settings that unduly reduce the number of wholesale and sophisticated investors in Australia could unintentionally cut off funding for businesses that have the potential to play an important economic role.

### Transparency and disclosure

**ASIC concern**: Private markets operate under lighter disclosure requirements, raising questions about transparency and oversight. [24]

**Council view**

Disclosure regimes need to address clearly identified risks that are material. They also need to be proportionate to the class of investor being safeguarded. For example, the level of protection for qualified professional institutional investors should be vastly different to retail investors who may or may not be advised.

Overly rigid disclosure obligations increase costs, can stifle capital formation and deter participation, especially for mid-sized firms central to Australia's innovation ecosystem. IOSCO found only 38 per cent of jurisdictions collect detailed private capital data, citing risks to proprietary information and excessive burden.[25] It is worth noting that while Australia has a world-class capital market, private markets are relatively less mature than the US, UK and Europe. That is to say that disclosure requirements should reflect the nuances and realties of the Australian market, including:

- Capital markets are not as deep as in larger jurisdictions and are less mature.
- Australia does not have the proliferation of bulge bracket fund managers seen in the US, UK and Europe. Global managers operate in Australia, alongside domestic managers that are smaller and have less operating infrastructure. These managers are particularly important to start-ups and SMEs.

ASIC already has substantial oversight powers under AFSL requirements including the submission of annual financial statements, audit reports, and compliance reports. These disclosures ensure transparency on operations, financial management and client fund handling. Breaches of AFSL conditions, such as mismanagement or inadequate disclosures, trigger mandatory notifications adding to the data ASIC collects on private capital activities. AFSL reporting focuses on the conduct and financial health of fund managers, bridging gaps in investor protection and market integrity.

[24] Australian Securities and Investments Commission. 2025. *Australia's evolving capital markets: A DP on the dynamics between public and private markets*. Australian Securities and Investments Commission. p. 24.

[25] IOSCO, p. 45

Additionally, some of the data that ASIC may find helpful might already be partially available through existing APRA and superannuation fund reporting regimes. The DP notes ASIC's ongoing work in assessing existing regulatory frameworks; the Council anticipates this work will also include a review of regulations that might be administered by other financial regulators.

There are also other forms of mandatory reporting and compliance such as the *Security Legislation Amendment (Critical Infrastructure Protection) Act 2022* covering cyber incidents and risk management program requirements for critical infrastructure entities, including those with private capital investments.

To assess the potential impact of further data reporting enhancements, they need to be clearly articulated. The Council would welcome clarification on the specific additional data categories ASIC would consider valuable from private capital markets (including private equity, venture capital and private credit) and the rationale.

## CONCLUSION

As the peak body for private capital investors, we recognise the growing complexity of Australia's capital markets. We acknowledge ASIC's efforts in initiating this important conversation through the release of its DP, *Australia's Evolving Capital Markets*.

Australia's economic resilience and future productivity depend on a dynamic partnership between public and private capital. These sectors are not in competition: they are complementary. Each plays a unique role in financing different stages and types of economic activity, and together, they underpin national growth, innovation, and infrastructure delivery.

The private sector has already been called on to do the heavy lifting to grow Australia's economy for the benefit of both the economy and the community. This necessitates a regulatory and policy environment that strikes the right balance between safeguarding investors and actively promoting innovation, growth and entrepreneurial risk-taking.

This DP has given the Council an opportunity to take a more holistic look at the existing legal and regulatory frameworks applicable to private markets in Australia. They are already extensive, comprising multiple statutes, common law principles and regulatory guides. They cover the obligations of allocators of capital and managers of capital. They also recognise the special protections that retail investors require which is appropriate. To date, and together with industry best practices, the Australian regulatory frameworks for capital markets has effectively served the market well.

Given:

- the volume and complexity of existing regulations;
- the conclusions drawn that the current downturn in IPOs is likely to be cyclical;
- the relative health of the secondary listed market; and
- that private credit currently does not pose systemic risk to Australia's financial system

it would be reasonable to suggest that policy work continues before further regulatory requirements are designed and developed. The Council notes that ASIC has various interrelated workstreams currently underway and would welcome seeing the outcomes of the DP process and these workstreams being brought together into an Issues Paper.

Within such an Issues Paper, the Council would welcome more detail about relevant aspects such as:

- the nature, likelihood and materiality of risks noted in the DP;
- areas in which existing legal and regulatory frameworks fall short of providing the necessary protections;
- the impact of additional regulatory requirements on: Australia's ability to attract and retain capital; a competitive and dynamic funds management industry; availability of capital for start-ups and smaller businesses; and economic growth.

As ASIC advances its review, we encourage a principles-based approach that:

- aligns disclosure requirements with the nature and sophistication of the investor base;
- recognises the structural features that mitigate systemic risk;
- reflects the distinct and desirable characteristics of private capital in an investment portfolio, namely, its long-term investment horizon, negative correlation to listed equities and fixed income; and illiquidity premium;
- avoids duplicative regulation that could suppress innovation or mid-market growth; and
- harnesses existing regulatory and legislative frameworks, APRA oversight and industry-led governance frameworks to enhance regulatory efficiency.

As Australia's private markets continue to grow in sophistication and global relevance, regulatory frameworks should focus on reinforcing investor confidence and system integrity without compromising the agility and innovation that define this asset class.

Our shared goal is a capital markets system that enables innovation, protects investors, empowers more Australians to share in the opportunities of the future economy and ensures Australia's position as a leading global investment destination.

We thank ASIC for its thoughtful DP and its recognition of the role that private capital plays in Australia's economy. The Council looks forward to working collaboratively with ASIC, on the next and subsequent stages of policy development.

# APPENDIX 1

## DETAILED RESPONSE TO QUESTIONS 1 - 15

### DEVELOPMENTS IN GLOBAL CAPITAL MARKETS AND THEIR SIGNIFICANCE FOR AUSTRALIA

**Q1. What key impacts have global market developments had on Australian capital markets? What key impacts do you anticipate in the future? Please provide examples from your experience.**

The growth of private capital in Australia fits within the overall trend seen globally. In Australia, private equity has tended to be at the small to mid-market end, with increasing interest in large-scale transactions by some domestic managers and global operators. Despite this, Australia still does not have the proportion of bulge bracket private capital operators and managers prevalent in other more established markets like North America and Western Europe. Recent interest in Australia from large global private capital operators is likely to be muted, limited by our remote geographic location and unique economic make-up which can be hard for foreign investors to understand.

Around the world, private capital is playing a more significant role in delivering national priorities. In Australia, over 1,100 businesses are backed by private capital that directly or indirectly employ 600,000 full time employees. Collectively, private equity, venture capital and private credit contributed $77 billion to Australia's economy in 2024, equating to three per cent of GDP. This is half the contribution seen in more mature markets such as the US and UK.

***Historic and current trends in private equity and venture capital***

Growth of Australian private equity markets leading up to 2022, with fiscal tightening leading to a decline in 2023, mirrors a heightened period of private equity activity in other developed markets. Broad-based economic expansion during the pandemic recovery, historic low interest rates and other accommodative policy measures drove this growth at a time when investors were less willing to invest in publicly traded companies given the period of high volatility.

International private equity firms and investors increased their participation in transactions involving Australian companies, and Australian private equity firms sourced around half of their capital from foreign investors. While much focus has been given to the mega take-private transactions that private equity has been involved in, less attention is given to the considerable investments made by private capital in small to medium businesses or in turn-around situations that are critical for innovation, employment and wealth creation. A number of 'iconic', and therefore culturally significant, Australian brands have survived only through investment by private markets investors.

Australia is also a growing hub for venture capital investing. Australia's venture capital market is diverse, with an ecosystem of angel investors and fund managers ranging in size and specialisation. While not as deep and mature as venture capital markets elsewhere in some other international centres, Australia has produced a large number of ‘unicorns’ (start-up businesses that have grown to a market valuation of more than $1 billion), predominantly in software as a service. Importantly, 75 per cent of Australian companies that have grown to be worth $100 million or more have maintained their headquarters in Australia[26].

In many ways Australia's private capital sector has stepped in to fill the gaps left by public equity markets, banks and government privatisations.

Additionally, Australia's private capital sector is an important destination for the investment of Australian and international capital by investors. The sources of fundraising activity by private capital includes:

- Australia's superannuation system and its need to diversify and invest in new assets classes;
- the growth and increasing external focus of foreign sovereign wealth funds;
- foreign (in particular European and North American) pension funds and their need to find new investments; and
- increased high net worth and ultra-high net worth investors and family offices looking to increase investment opportunities.

While each investor and investor type have different investment objectives, they all demonstrate a desire to diversify investment strategies and investment across asset classes and geographies.

In general, these investors are experienced, have access to professional advisers and have deep understanding of the risk and reward profile of different asset classes. In addition, they can often exert power (either through the terms of their investment documents or as a result of their relationships) to access business information both before investing and during the lifecycle of an investment which is tailored to their specific requirements for entering into and monitoring the investment.

***The growing role of international participants in public and private markets***

Recognising that private capital fund operators operate in a global capital market, it is critical to ensure that Australian private capital funds continue to remain attractive and competitive with foreign funds. Increased regulatory obligations could result in the withdrawal of certain players and a reduction of new entrants, leading to a reduction in the overall access of companies to funding sourced via private capital funds.

Private capital is not the primary driver of Australian public markets change. Australia and Australian companies have been an attractive investment choice for multinationals looking to expand their global footprint. Most Australian public market control transactions (i.e. takeovers and schemes) involve a strategic/corporate bidder making an offer to acquire an Australian company.

[26] Australian Investment Council, What is Venture Capital? 2020

Over the last five years approximately 50 per cent of all control transactions (by number) involve a foreign bidder. 'Mega' transactions (ie: with a value in excess of $1 billion) are dominated by foreign bidders or consortiums involving foreign bidders. In the past five years, approximately 80 per cent of all control transactions have involved strategic/corporate bidders.

What this means for Australian investors in public markets is that the opportunity to retain an ongoing exposure to that company is lost unless control transactions initiated by corporate bidders include an offer of scrip consideration in either an ASX-listed company or a CHESS depositary interest in a foreign listed company that has a secondary listing in Australia.

At the same time, some of Australia's largest companies such as BHP, Woodside, Santos and Brambles, are large international corporations that operate on a global basis. Other large Australian companies have changed domicile, moved to dual listed company structures, or shifted their primary listing to larger stock exchanges.

These changes have occurred over a long time but are nonetheless a fundamental driver in altering the composition and size of Australia's public equity markets. There is no reason to believe that these trends will not continue. Importantly it highlights that Australian capital markets operates in a global context that necessitates that Australia's regulatory settings are in-line with its global peers to ensure Australia remains competitive on the international stage and attractive to both foreign and domestic capital.

While there has been much focus on the role of private capital and private markets supplanting public equity markets, the fact remains that the bulk of delisting activity in Australia that has been delivered by M&A has been undertaken by corporates rather than by private markets investors.

### Q2. Do you have any additional insights into the attraction of private markets as an issuer or an investor?

Public equity markets are not able to serve the capital needs of all businesses, and this is proving even more so in the increasingly volatile global environment marked by increased risk aversion and uncertainty, where public equity markets' short-term focus and global interconnectedness present an unnecessary distraction to businesses and management that needs to focus on maximising growth and stability. This may also be because of the nature of the business, its stage in the growth cycle or because of the size and scale of the business.

In particular early-stage companies, growth companies, small and medium sized enterprises (SMEs) and companies in distress are often in the greatest need of capital but are locked out of traditional sources of capital from both public markets and banks.

There are many examples of Australian businesses that operate at a scale considered too small or immature to access funding and capital through well-known routes such as listed markets and traditional lenders. There are also a number of larger businesses with long-term, patient capital requirements. These are businesses that operate in a space fulfilling a need from an Australian consumer product and service point of view. These businesses are also employers of a large number of Australians. Their survival and growth is possible by accessing alternate sources of capital typically in the form of private equity or private credit.

For companies seeking capital, private capital has benefits noted below.

***Access***

Early stage, growth companies, SMEs and companies in distress situations have difficulty attracting funding from traditional sources. They are not able to meet the requirements of either the public markets or banks. The development of Australia's private capital markets through venture capital investors, growth investors, private equity and private credit have provided an array of new or additional funding sources. If these businesses are not able to access funding from private capital, they either cease to be viable or move offshore in search of capital. These are perverse outcomes when considered against the backdrop of a broader public policy intent to retain talent, grow innovative businesses, stimulate private investment, and build a diversified Australian economy.

***Patient capital***

Private equity tends not to seek immediate returns, rather the investment horizon is focused on building a business or turning around a business with capital and time provided to allow that growth to be achieved.

***Flexibility***

Private investors can structure their investment in a non-listed company in a variety of different ways which provides flexibility to both the company and investors.

Investors will seek to ensure maximum returns for a considered risk profile, and private markets are able to provide tailored solutions for investors with a specific investment strategy. Institutional and anchor investors have the ability to negotiate appropriate governance and investor consent levers, which provides them with greater control and lowers the risk profile for their private funds investments. This is something which is not largely available on the public market without a considerable investment ticket size or to small scale investors.

***Support for business by active management***

Private equity brings not just capital to the table as an investor, but also deep management, 'hands-on', business and governance expertise and experience along with a network of business advisors to support rapid transformation or growth of the business.

When private capital acquires or becomes an investor in a company, it often leads to a step change in the company's operating disciplines and governance structures with private equity supporting the adoption of more rigorous formal governance regimes. In particular many portfolio companies benefit from the use of non-executive directors, enhanced financial reporting, auditing and risk control arrangements and uplifts in the overall risk environment. A number of private equity funds look to ASX 200 governance structures and processes to bring this rigour. Private equity fund documents are also rigorously negotiated with global, institutional investors and superannuation funds that drive a demand and expectation for detailed reporting frameworks and governance arrangements similar to, and in some cases more protective than, retail client protections under the Corporations Act.

### *Wealth realisation*

For founders and family-owned businesses, bringing in a private capital investor, whether by way of a buy-out or as a minority investor provides an opportunity for wealth realisation, succession planning and partial or full exit.

As an investor, private markets often offer higher potential net returns compared to public markets, attracting experienced investors seeking alternate sources of returns via their investments. The benefits of private markets also provide access to the expertise of fund managers and the promise of diversification, which is particularly attractive to investors during volatile market conditions.

### Q3. In what ways are public and private markets likely to converge?

Public and private markets are neither distinct nor oppositional but instead operate on a continuum. Public and private markets are both providers of capital, but for businesses at different points in their life.

A business may start as privately funded, for example, angel funded then venture capital funded, then private equity backed. It may then become public markets funded, by way of a public listing as that business matures. Afterwards, it could become private markets funded again, as a result of business performance deterioration, to fund growth needs, or other drivers. The funding market that a business interacts with typically reflects the phase of maturity that business is operating through.

In particular it should be noted private capital investors (like private equity, superannuation funds etc) may have exposure to, and can be active participants in, public equity markets in a variety of ways, including by:

- being shareholders of listed companies;
- undertaking or participating in control transactions for listed companies; and
- acting as sponsors for IPOs.

In each case, the private capital investor is subject to the regulatory regime set out in Chapter 6 of the *Corporations Act* and the ASX Listing Rules.

In addition, private capital entities may themselves be listed on public equity markets or provide listed investment vehicles. These structures give investors benefits including exposure to private markets investments, the benefit of experienced investment professionals managing the investment, investment diversification, and potential liquidity by being able to trade in the securities of the listed company or investment vehicle.

### *Valuations*

Valuation methodologies applied across public and private markets are different, due primarily to differences liquidity, investor time horizons and other external factors.

### *Liquidity*

Public markets offer liquidity, meaning investors can (generally) readily buy and sell shares. Liquidity is a trade-off for less-than-accurate valuation or pricing, however it remains attractive because this offers flexibility to investors. Private market investments are illiquid, they cannot be readily bought or sold. This is factored into valuations often as a discount.

### *Information availability*

Factors influencing public markets valuations that are often not relevant to the value of the underlying business include:

- public markets offer liquidity, meaning investors can (generally) readily buy and sell shares. Liquidity is a trade-off for less-than-accurate valuation or pricing, however it remains attractive because this offers flexibility to investors. Private market investments are illiquid, they cannot be readily bought or sold. This is factored into valuations often as a discount.

- market sentiment and investor psychology, including bullish or bearish sentiment in the general market or specific sectors can sometimes drive prices up or down (sometimes irrationally and regardless of a company's actual performance);

- the sometimes temporary and unpredictable impact of macroeconomic factors, including a proposed government policy or political statements that is indirectly related to the underlying business of the company, can trigger short-term market reactions can create valuation swings that do not directly corelate with immediate changes in the company's intrinsic value;

- the impact of corporate actions (for example stock splits or share buybacks) can influence share price without necessarily changing the overall value of the underlying business;

- market trends or sector momentum which may trigger price increases simply due to the sector's popularity, even if individual company performance doesn't fully justify it. Conversely, strong companies in an out-of-favour sector might be undervalued;

- public market investors often focus on short-term performance and have shorter term expectations. This bleeds into market pricing and resulting valuations outcomes. Private markets investors link their timing to longer term horizons, often to points in time when the underlying business value can be realised.

- public markets attract a diverse range of investors, from retail to institutional, with varying risk appetites. These appetites are reflected in daily trading volumes and more volatile intraday pricing/valuations. Private markets are dominated by institutional investors, who often have specialised expertise and different return expectations over longer periods of time..

Private market valuations are based on long established and accepted methods such as multiples of EBITDA, comparable company analysis and discounted cash flow models. They seek to strip out the "noise" and reflect what a business could be realised for in an orderly sales process. In Australia, the AIC encourages its members to adopt the principles set out in the International Private Equity and Venture Capital Valuation Guidelines to assist in sharing transparent and consistent data with investors on a periodic basis, and fund managers also comply with the Australian Accounting Standards.

Further comfort around private markets valuations can be gained from the audit and review of valuations performed by private markets practitioners. Valuations are subject to independent review and sign off by the independent financial statement auditor. They must confirm that the valuation presents the "fair value" of the investment as is required by relevant accounting standards. In addition, valuations processes are subject to process and controls audits, normally performed as a GS007 agreed upon procedure, which is generally required by private capital market investors.

### Q4. What developments in public or private markets require regulatory focus in Australia in the future?

The current global volatility has significant implications on the attractiveness of public capital:

- *Increased risk aversion:* high volatility increases perceived risk, which can drive companies and investors away from public markets and towards preferring the relative stability of private markets.
- *Uncertainty and pricing*: volatility can make IPOs difficult to price, deterring companies from going public, and fluctuations in share prices can also create challenges for companies in maintaining their market capitalisation, potentially leading to delisting.
- *Short-term focus*: increased volatility often encourages a short-term focus among public market investors, which can be detrimental to companies seeking long-term growth. In contrast, private capital's long-term investment horizons support a focus on investment theses that maximise growth and stability.
- *Interconnectedness*: global financial markets are highly interconnected, meaning that shocks in one region can quickly spread to others. This exposure to global volatility increases the overall risk of public markets. Geopolitical events, economic downturns, and global crises can trigger significant market volatility, leading to a decline in public market activity.

***Private funds are currently extensively regulated via existing statutory obligations***

ASIC has existing broad powers under current statutory regimes. There is no apparent legislative gap requiring urgent government legislation or new regulator intervention given operators of private markets funds (whether as trustees, general partners, managers or promoters) are extensively regulated by virtue of obligations flowing from their AFSL (or authorisation of the operator as an authorised representative under an AFSL). These statutory obligations include:

- the duty to provide financial services 'efficiently, honestly and fairly';
- the duty to ensure disclosures in marketing and offer documentation are 'clear, concise and effective'. Notably, there is no direct US equivalent to the Australian 'efficiently, honestly and fairly' and 'clear, concise and effective' statutory standards;
- duties (supplemented by ASIC guidance) requiring adequate human, technological and financial resources, including in relation to competency;
- the statutory duty to avoid misleading or deceptive conduct;
- unfair contracts provisions in the *Australian Securities and Investment Commission Act 2001* (ASIC Act), which was recently modified to make it an offence to enter into an 'unfair contract' with a 'small business' (which could potentially cover certain arrangements with non-institutional wholesale client investors);
- strict duties for the timely reporting of significant breaches of financial services laws;
- obligations in relation anti-money laundering and counter-terrorism financing (AML/CTF); and
- insider trading and market manipulation measures.

We understand a key concern of ASIC is the need for greater visibility of market activity. In October 2021, a range of new regulations was introduced and now apply to regulate private (and other) funds. In particular, the 'reportable situation' regime replaced the traditional breach reporting regime. Under the 'reportable situation' regime, an operator (as an AFSL holder) is required to notify ASIC within 30 days of any 'reportable situation'.

The concept of a reportable situation is much broader than the types of incidents that would have been required to be reported to ASIC under the prior breach reporting regime. The threshold for reporting is set at a much lower level, meaning operators are now required to notify ASIC much earlier than previously required and in respect of a broader range of incidents that are 'deemed' reportable.

This extends to a stricter requirement to report situations when investor disclosure has not met the statutory standard (of ensuring statements are not misleading or deceptive), including in potential situations involving a small degree of impact on investors. As a result, the recently modified regime provides ASIC with greater visibility of market conduct and an opportunity to require remedial action or take other enforcement action.

As noted in ASIC's DP, given the current and near-term size of the private credit sector, the sector is not sufficiently large as to represent a systemic risk requiring further regulation. In any event, private credit funds are required to report to APRA each year on the level of credit activity in line with their obligations under Financial Sector (Collection of Data) Act 2001 (Cth) (FSCODA). This provides the regulator with a level of visibility of market activity.

Given the extensive regulation of private funds in Australia through a suite of established statutory obligations and the highly negotiated contractual framework of obligations (see response to Question 4), increasing regulatory obligations will not necessarily increase investor protections. Rather, it risks creating an environment where larger private capital operators (with larger middle and back-office operations available to service such obligation) survive at the expense of the small to mid-market operators.

This may lead to a perverse outcome where mid to larger businesses will continue to be able to access capital across both public and private markets, however small to mid-businesses will be starved because they cannot access capital from public markets and their source of private capital, being the small to mid-market private capital operators, will struggle to continue to operate.

### *Industry guidelines appear to be operating effectively*

Depending on the fund, a private fund is often distributed to both institutional investors and investors participating via private wealth advisory channels. Each such channel demands a high standard of disclosure and governance to be adopted by a fund.

Industry bodies have been effective in developing 'best practice' guidelines that are adopted by the particular sub-sector. These include the Council and ILPA.  Many private equity fund operators volunteer to adopt the International Private Equity and Venture Capital Valuation (IPEV) guidelines and various ILPA guidelines and many real estate fund operators volunteer to adopt the European Association for Investors in Non-Listed Real Estate Vehicles (INREV) Guidelines on valuation as these become expected industry benchmarks among institutional investors and private wealth advisory firms.

Even though guidance notes and templates from these bodies are not mandatory in Australia, most private equity fund managers report in accordance with some or all elements including key financial metrics. This is in response to investor requests as well as simply to improve transparency of performance based on a consistent platform of measurement and disclosure.

### *Impact on international competitiveness of funds sector*

Legislating specific conduct and disclosure obligations would put Australia out of step with other similar jurisdictions and unnecessarily impact the ability of operators to raise investor funding.

In 2023, the US SEC attempted to introduce new requirements relating to transparency and investor protections, but this was struck out in its entirety by the US appeals court.

We believe it is not possible to develop and implement broad rules which introduce requirements for investor protections, performance measurement and reporting that can be meaningfully applied across all private market participants. The variations between fund strategies are too diverse, and such rules will result in misleading and unintended outcomes.

### *Wholesale only gate*

The Government has received extensive submissions across industry, ASIC and consumer groups following the consultation paper published by the Department of Treasury in

August 2023. We understand there is no present intention to modify the tests for status as a wholesale client. This is on the basis that, on balance, the tests continue to be appropriate to drive whether a fund is required to be registered and regulated under the Corporations Act regime applicable to retail investors.

## HEALTHY PUBLIC EQUITY MARKETS

### Q5. What would make public markets in Australia more attractive to entities seeking to raise capital or access liquidity for investors while maintaining appropriate investor protections?

The Council fundamentally supports vibrant and thriving public markets so noted with interest the various insights ASIC gained from stakeholders around their decreasing attractiveness. From an investor perspective, research from the Australian Investor Relations Association suggests retail investor holdings have increased by more than 20 per cent over the past two decades, with 1.3 million new holdings added between 2019 and 2023[27].

Nevertheless there are some factors impacting the value proposition for listed markets, most of which are explored in detail in Report 807. These include:

- regulation and the associated risks to companies and boards;
- the changing nature of companies and the economy;
- the reduction in the need for liquidity;
- the operation of the Australian public markets; and
- the diversification of the Australian public markets.

It would be reasonable for companies to consider these and other factors, as well as the significant cost of IPO listing fees, against the value delivered.

#### *Regulation and the associated risks to companies and boards*

At its core, the Australian regulatory landscape around the capital markets (both public and private) is appropriate and has served the Australian market well, especially during the global financial crisis in 2008 – 2009 and the COVID-19 pandemic. They achieve a balance between maintaining appropriate investor protections, while removing unnecessary "red tape", in a way which is the envy of many other jurisdictions.

As such, the Council does not believe the Australian regulatory settings are a primary driver behind the declining number of public companies and so does not require wholesale review or amendment although it is noteworthy that the Australian market practice as it relates to capital markets transactions differs from that in most other sophisticated capital markets. The Council is not advocating for additional regulation to alter market practice but there are regulatory factors that can and should be considered. These will not solve the dilemma in themselves but should assist:

[27] Australian Investor Relations Association, Media release: AIRA Releases White Paper - Trends in Retail Investor Participation and Engagement, 27 November 2024

### *Risk period*

As many have noted, the standard market practice in Australian IPOs requires investors to be "on risk" for a greater period than most other capital markets between pricing / confirmation of allocation and admission of the IPO candidate to trading on a public market, usually following a 'front end' bookbuild structure. For some transactions, this can be as much as six weeks where no consultation has been undertaken with ASX before lodgement of the prospectus with ASIC. The period, and associated risk, is driven by many factors including (i) the need for an exposure period whilst ASIC reviews the prospectus after lodgement (ii) the need to provide retail investors and their advisers with sufficient time to consider the prospectus and associated documentation, (iii) ASX's admission requirements and (iv) issuer's need for certainty of pricing and funds (via underwriting) before the prospectus is lodged with ASIC and the transaction becomes public.

It will help issuers and their underwriters if this period can be reduced and minimised. It can be achieved through a "back end" bookbuild structure but that does not meet issuer's requirements for certainty of funds and pricing and so has generally only been utilised for the largest IPOs. Moving to a market practice of back end bookbuilds as the default will ultimately require underwriters and other market participants to take the lead but ASIC should consider if some regulatory levers might be altered to assist.

### *Pre-vetting of prospectuses and exposure periods*

A notable feature of the Australian market is that ASIC does not formally review prospectuses prior to lodgement. The policy and practical reasons behind this have been explained by ASIC but the existence of a seven-day exposure period (which can be extended by another seven days) has the potential to delay IPO processes significantly and introduce uncertainty, especially for underwriters and participants who are on risk during that period. Were ASIC to pre-vet prospectuses or provide certainty around exposure periods, the Council believes it would assist.

### *Use of greenshoes*

It is generally rare in the Australian market for an IPO to utilise any form of market stabilisation or 'greenshoe' in the immediate period after IPO. Market stabilisation may not be a significant factor in increasing IPOs but ASIC and ASX could make the regulatory process around greenshoes more streamlined. At present, there is no formal regulatory relief around greenshoes but a standard form of "no action" relief is relied on. It will remove one additional hurdle if there was clear class relief that could be relied on to remove the cost and time associated with seeking individual relief.

### *No use of dual class structures*

Australia is one of the few major markets where listing of companies with dual class structures are rare and generally not accepted. We note ASX's proposal to allow dual-class listings and would support ASX (and ASIC) in their consideration of the introduction of such a regime. The use of dual listed structures has been accepted in offshore markets for many years (especially the US) and is employed by many founder-led technology and media companies. If dual class share structures are important for listing candidates, serious consideration should be given to how such a regime could be facilitated, noting the market will ultimately determine their viability in Australia.

### *Personal liability for directors*

Anecdotally, the regulatory and reputational risks associated with being a public company director have become too great, deterring many from the role.

The Council is not advocating for a reduction in the onus placed on officers. However, we note that while the regulatory landscape is clear and justified, many potential company directors are just not willing to take the risk. The fact that Australia has become a primary jurisdiction for securities class actions only adds to the personal risk for company directors.

### *ASX Listing Rules*

To its credit, ASX regularly considers changes to the listing rules to ensure they remain fit for purpose and has often removed rules which are no longer needed. That said, it is clear the regulatory burden on listed companies is significant and the "one size fits all" nature of the listing rules (with some limited exceptions) means that the burden is too great on smaller companies or those in specific industries.

By way of example, many ASX listed biotechnology companies also have NASDAQ listings given the availability of capital in the US. Where those companies raise capital, it is often driven by US investors who seek warrant coverage with features such as cashless exercise. The ASX Listing Rules are very prescriptive when it comes to options with limited scope of waivers, and this has caused transactions to fail. If investors don't receive their standard suite of warrant terms, they often walk away. While we agree ASX needs to enforce the ASX Listing Rules with rigour, there are some elements where it could be more flexible and consider waivers where, to date, none have been available.

The Council believes that, once listed, the regulatory settings around secondary capital raisings works well and it remains a key attraction of the Australian public markets. Australia is relatively rare in supporting secondary equity capital raisings.

### *The changing nature of companies and the economy*

Companies in some newer industries are less capital intensive than traditional industries. For these companies, raising capital quickly and efficiently from the public markets may not outweigh the downsides of being listed, notably the regulatory burden and costs of being listed.

Also, some companies have capital needs that cannot be satisfied by the public markets, often because they are too small, too large or because the illiquidity in their shares (or share price performance) will not support a capital raising. In that regard, the private markets provide a natural and viable solution.

### *Reductions in the need for liquidity*

The Council believes that the rise in private capital has provided a real alternative to the public markets. Both play an essential role in undertaking and facilitating investments in

Australian corporates and furthering the Australian economy. The Council notes that the private markets present different risks for investors and the broader economy but believes that these risks can be mitigated and that the regulatory settings to address these risks are appropriate.

### *The operation of the Australian public markets*

The ASX has always positioned itself as a market ideal for companies too large for venture markets but too small for exchanges such as NASDAQ. That strategy has proven successful to a degree with some US and NZ companies particularly choosing to list on ASX.

In recent times, a number of dual listed or US companies have chosen to delist from the ASX because the expected benefits were not realised. It is probably timely to reconsider the value proposition for listing, particularly for smaller companies.

### Q6. Do you agree that a sustained decline in the number, size or sectoral spread of listed entities would negatively impact the Australian economy? If so, can you suggest ways to mitigate any adverse effects that may arise from such changes?

The Council firmly believes that Australia's economy and communities would be best served by an efficient and effective capital market that enables businesses to access the funding necessary for sustainable growth, while providing investors with opportunities to create wealth. This applies to listed and unlisted equity markets as well as listed and unlisted debt markets.

The consequences of a sustained decline in the number, size or sectoral spread of listed entities could include:

- a smaller and less diverse universe of listed companies. From a price perspective, this ultimately means that prices for shares are not reflective of their inherent value. Rather, prices become an increasing function of the forces of supply and demand, with the same (or larger) pool of capital seeking investments in a small pool of opportunities;
- investors are less diversified in their investment mix, which in turn leads to greater risk and not necessarily reflective of their risk appetite;
- investors will need to look to alternatives, such as offshore markets or alternative investments such as private equity, infrastructure funds etc;
- companies will need to look elsewhere to raise capital, likely through the private markets.

To support the availability of capital for productive economic activity, there are measures that could be taken to promote the attractiveness of public and private markets. Suggestions for public markets have been made above. To increase the economic contribution of private markets, ASIC could consider the following:

- reforms to RG97 and the performance test in the Your Future, your Super legislation which incentivises investment by superannuation funds into listed markets. This has led to an inefficient allocation of members' funds; and

- introduction of a Limited Partner Collective Investment Vehicle (LPCIV), which would provide fund managers with an internationally recognisable vehicle for pooling domestic and international capital. With Australia becoming increasingly reliant on international capital, an LPCIV would reduce the friction that currently exists with trusts.

**Q7. To what extent is any greater expectations of public companies, compared to private companies, the result of Australian regulatory settings or the product of public scrutiny and community expectations of these companies?**

Most laws and regulations apply equally to public and private companies. From a regulatory perspective, there does not seem to be any material advantage or disadvantage conveyed upon listed or unlisted companies.

The daily mark-to-market nature of public markets lends itself to daily examination of a company's share price. While there is a belief that that share price reflects the financial value of a business, the listed market allows for other influences to weigh in that may or may not be rational. These influences are often referred to as 'animal spirits'. As was seen in recent weeks, speculation about the impact of US trade tariffs had an immediate and volatile impact on global listed markets that was not entirely rational, given the tariffs had merely been announced and not enacted. That volatility was fuelled on a single day by inaccurate information disseminated on a social media platform.

For some companies, particularly small and medium-sized ones, irrational listed market behaviour can be devastating. Where companies are undergoing long-term transformation or transition, or are investing in long-term projects, the short-term lens of listed markets is asynchronous. Even for companies that are well managed and financially robust, the resources required to address market sentiment could otherwise be used to deliver on the company's core business and strategic plans. It is understandable that, for some businesses, the unlisted market is more aligned to their strategy and growth plans.

## PRIVATE MARKET RISKS AND MARKET EFFICIENCY AND CONFIDENCE

**Q8. Are Australian regulatory settings and oversight fit for purpose to support efficient capital raising and confidence in private markets? If not, what could be improved?**

Private market sponsors and issuers are subject to stringent regulatory settings and ASIC has a broad range of oversight and enforcement powers in respect of these settings.

Given the importance of the private markets to the Australian economy, regulators need to be as accountable for the opportunity cost of regulation and regulatory probes as they are for the benefits. Every piece of regulation diverts resources away from productive activity, especially for small and medium businesses. It is crucial to properly assess and demonstrate (a) a material and real need for new regulation that (b) can't be adequately mitigated by the existing settings.

### *Existing regulatory settings*
Private fund managers in Australia typically require an AFSL (either directly or through the use of an authorised representative arrangement as permitted under section 916A(1) of the *Corporations Act 2001 (Cth*). Consequently, these sponsors are subject to a range of regulatory obligations, including statutory duties under section 912A to:
- do all things necessary to provide financial services efficiently, honestly and fairly;
- have adequate arrangements for managing conflicts of interest and risk management; and
- comply with financial services laws (spread across the Corporations Act, the ASIC Act, and other Commonwealth, State or Territory legislation that covers conduct relating to the provision of financial services).

In addition, for funds structured as unit trusts, which applies to the vast majority of private funds in Australia, the trustee is subject to statutory, common law and equitable (including fiduciary) duties which are both broad and onerous.

Examples of applicable regulations within the *Corporations* Act include:
- governance obligations, including directors' and officers' duties (Chapter 2D);
- ongoing disclosure requirements (principally in Chapter 2M);
- offers of securities, including protections where information asymmetries exist (Chapter 6D); and
- misleading or deceptive conduct and insider dealing (Chapter 7).

### *Existing regulatory oversight*
In respect of these settings, ASIC has significant rights and powers in respect of oversight and enforcement.

ASIC has a broad range of compulsory-information gathering powers, in respect of AFSL holders and Australian companies in general, including the power to require the provision of documents and information, the power to require attendance at an examination to answer questions or provide assistance, and the power to compel assistance with an investigation.

These powers are supported by the expanded reportable situations regime, applying to both AFSL holders and Australian credit licensees and which, through the concept of deemed significance, requires market participants to report a wide range of breaches which would not have been reportable under the previous regime. Although used more sparingly, ASIC also has the power to apply for and execute search warrants. As such, ASIC is able to (and does) undertake surveillance and commence investigations into suspected breaches of law.

### *Approach to changes to regulatory settings and oversight*
The Council asks ASIC to consider its existing powers and how these may support its oversight responsibilities.

Private markets are designed primarily for investment by institutional investors who are sophisticated and able to evaluate investments and associated risk and can determine and negotiate any required risk mitigants.

In respect of wholesale funds, the Council acknowledges that other, comparable offshore regimes, in particular the US, the European Union and the United Kingdom, impose more stringent periodic reporting obligations on private capital sponsors. However, these are more mature, larger and deeper capital markets. Given the current size of private capital investment in Australia, the Council considers current regulatory settings are appropriate.

As noted by ASIC, setting aside limited and specific avenues such as employee equity schemes and crowd-sourced funding, retail investors are principally exposed to private markets indirectly through intermediaries; in particular, superannuation funds and registered managed investment schemes.

These intermediaries are also sophisticated investors with professional advisers who are already subject to extensive regulatory settings and oversight.

When considering the need for further regulatory requirements, the Council asks ASIC to take into account that Australia competes with a broad range of other jurisdictions, not only for offshore investors but also from our own superannuation, sovereign and other institutional investors, who are increasingly looking offshore. Regulatory approaches should support investor confidence and system integrity without compromising the agility and innovation of private markets.

There is also the cost of that comes with each piece of regulation, that tends to have a disproportionate impact on smaller and medium-sized funds. It would not be in the best interest of a dynamic and competitive funds management market to increase the barriers to entry through regulation unless it was absolutely warranted.

As such, the Council suggests the following questions are relevant:

- Does the current regulatory framework support a dynamic and high-functioning investment market?
- Is there a specific market failure to be addressed that would directly cause significant investor losses or undermine overall market confidence?
- Is there evidence to suggest that such failure is likely and material? If so, what would be the consequences and for whom?
- How and where does the existing regulatory framework fall short?
- Is new regulation the only and best solution?
- What is the opportunity cost of regulation in terms of productivity, innovation, competition, speed to market and competitiveness?
- What are the Compliance costs associated with a new regime, particularly for small and medium enterprises?

To this end, the Council would support and encourages further and extensive industry consultation to diagnose the range of symptoms it has outlined in the DP, before preempting a prescription for issues that may not exist or could be adequately mitigated using existing settings.

**Q9. Have we identified the key risks for investors from private markets? Which issues and risks should ASIC focus on as a priority? Please explain your views.**

The DP is a constructive first step in articulating a range of potential issues and concerns. Subject to our specific commentary below, the Council considers that ASIC has identified the relevant factors.

It is also relevant that participants in Australia's private markets are predominantly institutional investors that are highly sophisticated and able (supported by sophisticated legal and commercial advisers) to recognise, understand and if required, take steps to mitigate key risks associated with their investments. These investors generally have robust due diligence, and governance processes and structures in recognition of their fiduciary responsibilities. Existing regulatory and legislative regimes provide a complex framework by which market participants need to abide.

***Information 'opacity' and treatment of investors***

In respect of opacity and unfair treatment of investors, although acknowledging that there can be an information asymmetry between sponsors/issuers and investors in private markets, we consider that this is a risk which is largely managed in practice by market participants, with investors insisting on an ever-increasing range of periodic reporting.

In respect of the specific examples of unfair treatment highlighted in this question, we do not consider the granting of preferential redemption rights to be a widespread risk, noting that many private funds are closed-ended (ie: they do not provide for investor-initiated redemptions) and for open-ended funds, fund documents will typically prescribe detailed rules for ordering and satisfying redemption requests.

It is not uncommon for fund sponsors to enter into side agreements with particular investors, particularly where there are legal and regulatory requirements that are unique to the investor but not applicable to others investing in the fund. This does not constitute unfair or preferential treatment.

Potential for misclassification of retail investors as wholesale investors is dealt with elsewhere in this submission.

***Conflicts of interest***

The risk of conflicts of interest is also adequately addressed, both through existing legal and regulatory settings, as noted in this submission, and through contractual dealings between informed counterparties. In the context of private funds, it is standard practice for any actual or potential conflict of interest to require approval by the investors or an advisory committee comprising a cross-section of investors.

### *Liquidity risk*

In the context of private markets illiquid investments, and their expected outsized returns to reflect this illiquidity, play an important role for investors as part of a balanced portfolio reflecting the timing of their cash needs. There is also an active market for secondary sales, of which investors seeking earlier liquidity can avail themselves.

### *Valuations and leverage*

These risks are already managed through the existing matrix of legal and regulatory settings, as outlined above, together with self-regulation by private market participants. For example, institutional investors are increasing their focus on, and the pressure applied to sponsors and issuers in respect of, valuations, driven in part by APRA's focus on valuations by Australian superannuation funds.

In this regard, typical private fund terms will include (and require the sponsor to comply with) procedures to regulate valuations, often based on industry benchmarks; it is common practice for investors to insist upon strict parameters and increasingly, to require regular, detailed reporting on the use of leverage in fund structures.

### *Market oversight and surveillance powers*

ASIC has extensive information gathering and surveillance rights and these could be used to support ongoing consideration of how material and likely risks, if they exist in private markets, could be addressed. Following that process, whether specific changes to regulatory settings could be imposed in a way which recognises the role of the private markets and balances the need to ensure Australia remains a competitive and attractive destination for private market investment.

### Q10. What role do incentives play in risks, how are these managed in practice by private market participants and are regulatory settings and current practices appropriate?

The types of misalignment behaviours implied in the question are well managed in practice by the operation of a range of regulatory and other factors. These include:

- the current matrix of legal duties and regulatory requirements imposed upon sponsors, issuers and their respective directors and officers;
- the ability of sophisticated institutional investors to protect their own interests; and
- the influence of commercial and reputational pressure on appropriate practices.

### *The role of existing regulations and practices on driving good practices*

Protection negotiated by investors typically aligns with sponsors' and issuers' legal and regulatory duties, and the two work in tandem to mitigate risk. Below are some examples of how this works in practice.

### *Performance fees*

The principal economic incentive for private fund sponsors and their executives is carried interest (also referred to as performance fees). It is common in this market for performance fees to be based on overall fund performance and for there to be clawback where overall or later performance does not justify earlier calculations and payments. It is also worth noting that institutional investors / limited partners will simply not participate in future fundraising if incentives lead to misalignment.

Interests are further aligned by the common requirement that sponsors and their key executives co-invest in or alongside the fund and are therefore exposed to the consequences of risky behaviour alongside their investors.

As noted by ASIC management fees also provide for a material economic incentive to those operating funds but these are based predominantly on the commitments made to the fund (rather than fund performance) and so do not have the same impact on behaviours and risk.

***Conflicts of interest***

Conflicts of interest can potentially create misaligned incentives; for example, when one fund managed by a sponsor sells an asset to a continuation or other fund managed by the same sponsor. However, this is not an unfamiliar risk to institutional investors, who typically have fiduciary responsibilities, and there are well-worn governance practices for mitigation and management. This includes obtaining investor or investor advisory committee consent, which is a process involving the sponsor presenting detailed information to the investors on how the conflict has been managed and mitigated.

***Valuations and leverage***

Market practice, driven by informed and expert institutional investors, dictates that assets are valued based on industry-standard practices and/or sponsor valuation policies which are disclosed to investors in advance and to which material amendments often require some form of investor consent or consultation. For example:

- many private equity fund sponsors adopt the IPEV guidelines and various ILPA guidelines;
- many real estate fund sponsors adopt the European Association for Investors in Non-Listed Real Estate Vehicles (INREV) guidelines; and
- many private credit sponsors use IFRS9, which is also adopted by ADIs and is contemplated by the Alternative Investment Management Association's Guide to Sound Practices for the Valuation of Investments, as an appropriate valuation method for private credit assets.

The widespread adoption of these types of guidelines and methodologies influences has led to their recognition as industry benchmarks among institutional investors and, subsequently, private wealth advisory firms.

With respect to the use of leverage, institutional investors are alive to this issue and seek to mitigate the risk by insisting on strict parameters around the use of leverage in fund documents and regular investor reporting. The Council notes the recent use of NAV facilities by fund sponsors, although this remains far more prevalent offshore than in Australia.

## RETAIL INVESTOR PARTICIPATION IN PRIVATE MARKETS

### Q11. What is the size of current and likely future exposures of retail investors to private markets?

The Council does not track the size and the future exposure of retail investors to private markets. However, it is likely that the size of retail investors' direct exposure to private markets is small relative to their exposure to public markets.

In practice there are only a few avenues available for 'retail' investors to invest or otherwise participate in private markets. The primary forms of direct retail investment into private markets are through:

- employee equity schemes;
- crowd-sourced funding; and
- other limited exceptions, including small-scale offerings, and participation from persons that meet the senior manager test.

There is a lack of up-to-date public data on the utilisation of employee equity schemes, with the only data noting that in 2016-17 there were 187,000 individuals under upfront employee equity schemes and 74,800 in deferred schemes. Since the current scheme was introduced in 2018, as of 2024, crowd-sourced funding has facilitated the distribution of approximately A$315 million across 427 offerings in aggregate.

Additionally, there is an emerging trend, which started offshore, of private fund managers accessing retail capital by way of feeder funds. This occurs through a regulated intermediary (structured as registered managed investment schemes and typically operated by a third party service provider as responsible entity). As such these investors are sufficiently protected by the legal and regulatory settings applying to registered schemes, in particular but not limited to Chapter 5C of the Corporations Act 2001 (Cth) ("Corporations Act").

***Superannuation funds***

The Council notes the participation of individuals in private markets via their superannuation funds. The Council does not support the suggestion that superannuation fund members are retail investors as they would be when making direct investments into financial products. Investment decisions are being made by qualified investment professionals who take a range of considerations into account when constructing portfolios.

It is also worth noting there is an extensive range of legislative and regulatory requirements governing superannuation funds and member outcomes. This includes the *Superannuation Objective Act 2024, Superannuation Industry (Supervision) Act 1993,* and fiduciary responsibilities under statute and common law.

### *Q12. What additional benefits and risks arise from retail investor participation in private markets?*

Over the long-term, private markets investing has delivered attractive returns over and above listed markets. In principle, retail investors should be able to generate wealth through having a broad range of investment options covering a range of risk appetites.

That said, private markets investing has unique characteristics that may not suit all retail investors. For example, the investment horizon is long-term, meaning that capital is 'locked up' for longer periods. This is offset by investments delivering an illiquidity premium, that is not available in public markets.

For fund managers, providing product suitable for retail investors is a considerable commercial decision. It requires:

- designing investment products that have more 'evergreen' characteristics;
- employing appropriate resources to comply with the existing regulatory requirements for retail investment products; and
- allocating resources to activities such as investor education and relations.

Private markets as a retail investment class is in its infancy around the world. The Council supports policies that facilitate access to affordable, high-quality financial advice so that retail investors can take a holistic approach to wealth creation and management.

### *Employee equity schemes*

Employee equity schemes assist business of all sizes to issue capital to employees that are often retail investors. The benefits include:

- attracting and retaining talent;
- aligning employees' interests with the success of the company; and
- encouraging innovation and entrepreneurialism as the company's employees will invariably have contributed to the company's rise in value.

However, they pose certain drawbacks, such as:

- the investment is often tied to continued employment with the company;
- limited opportunities to sell the securities and realise value (i.e. typically restricted to a sale of the company or following an IPO); and
- securities cannot be easily valued, which may produce uncertainty for employee shareholders.

In 2022, the relief granted to employee equity schemes was expanded under Div 1A of pt 7.12 of the Corporations Act, giving disclosure relief for service providers and related persons under the scheme, increasing the monetary cap per scheme participant to A$30,000 per year (for schemes which require payment to participate) and allowing share purchase and loan plans, among other changes.

### *Crowd-sourced funding*
Crowd-sourced funding provides an avenue for early-stage companies to access retail investors. The benefits include:

- broader access to capital through a range of investors without prohibitive regulations or financial burdens, such as preparing a prospectus; and
- portfolio diversification for retail investors, offering investment opportunities that are typically reserved for sophisticated or professional investors.

The risks of crowd-sourced funding include:

- the overall riskiness of the investments, as start-ups have a high risk of failure and the potential to cause significant financial losses for retail investors;
- it is difficult for investors to assess the true value and the potential of an early-stage business; and
- the investment is illiquid, causing investor capital to be locked within the company for extended periods (similar to employee equity schemes).

These risks are recognised and provided for under Part 6D.3A of the Corporations Act.

### *Personal offers and senior managers*
Retail investors may also invest in private companies through personal offers under s 708(1) of the Corporations Act, or if they are senior managers of the entity in accordance with s 708(12). Similar benefits and risks exist to participants as in employee equity schemes and crowd-sourced funding, as noted above.

**Q13. Do current financial services laws provide sufficient protections for retail investors investing in private assets (for example, general licensee obligations, design and distribution obligations, disclosure obligations, prohibitions against misleading or deceptive conduct, and superannuation trustee obligations)?**

Retail investors' direct participation in private equity and venture capital is uncommon, and there is some participation in private credit. The regulatory framework protecting retail investors who directly invest in private assets is comprehensive and already includes appropriate guard rails. In addition, forms of retail investors' investments are substantially shielded from risk and uninformed decision-making due to the design and distribution obligations, and prohibitions against misleading or deceptive conduct.

## Obligations protecting retail investors
### *General licensee obligations*
The general licensee obligations under s 912A of the Corporations Act provide a broad suite of protections to retail investors. Notably, this includes the requirement that licensees act "efficiently, honestly and fairly", fulfil fiduciary duties, manage conflicts of interest, and comply with their licence conditions.

The scope of the general obligations is wide, requiring licensees to comply with a high, and at times protectively vague, baseline of conduct. For example, courts have found that the words "efficiently, honestly and fairly" either each take an ordinary meaning (see ASIC v

Westpac Securities Administration Ltd (2019) 272 FCR 170, 267 (O'Bryan J)), or are grouped compendiously as a single concept to mean that when one of these duties is being performed, the licensee is balancing and considering the other duties: see Story v National Companies and Securities Commission (1988) 13 NSWLR 661, 672. The wide scope of these obligations serves to benefit retail investors from licensees improperly inducing retail investors or making illegitimate representations.

### *Design and Distribution Obligations*

The design and distribution obligations under Part 7.8A of the Corporations Act, introduced in 2021, provide an effective forward-looking layer of protection to retail investors. Issuers must identify an appropriate target market for their financial product and ensure distribution aligns with this market. This involves the issuers making a Target Market Determination, preventing the mis-selling of shares to investors which may not be suitable for them.

### *Prohibitions against misleading or deceptive conduct*

Retail investors are significantly protected by the broad prohibitions against misleading or deceptive conduct, which safeguards retail investors by ensuring they receive truthful disclosure about the details of a product's risks, benefits, fees, and significant features. This helps to inform rational decision-making before the investment. Additionally, bad actors are effectively deterred from engaging in false or misleading conduct due to the penalties available for any contravention, including pecuniary damages of A$220,000 for an individual and A$1.1 million for body corporates, injunctions, compensation orders, and disqualification of a person from managing corporations.

### *Crowd-sourced funding*

Part 6D.3A of the Corporations Act provides an extensive regulatory regime for crowd-sourced funding to operate. The key features of this regime which safeguard retail investors from undue risk include:

- the requirement that the crowd source funding platform hold an Australian Financial Services Licence (s 738C);
- mandatory disclosure documents (ss 738J-738K); and
- investment caps, cooling-off rights, and strict liability provisions (ss 738ZC-738ZD).

### *Superannuation trustee obligations*

Investors in APRA-Regulated Superannuation Funds are typically retail investors, but in relation to indirect private market investments, are sufficiently protected by existing superannuation regulation. Superannuation trustee obligations are expressed as covenants under s 52 of the Superannuation Industry (Supervision) Act 1993 (Cth) ("SIS Act"). The general covenants in s 52(2) of the SIS Act adequately protect retail investors by requiring the trustees to invest prudently, act in the investors' best financial interests, and avoid conflicts.

### Key Disclosure Obligation Exemptions Under Section 708

#### *Small-scale offer exemption (s 708(1))*

The small-scale offering is limited to 20 investors in any 12-month period and is subject to a small financial limit of A$2 million in aggregate over that period. This restriction lowers the risk for retail investors who are making a smaller capital investment than sophisticated or institutional investors and can only be accessed by personal offers.

#### *Senior manager exemption (s 708(12))*

The senior manager exemption efficiently works to limit the administrative burden on senior managers or bodies or those closely related to them from needing disclosure. Senior managers are in a position to know a company's strategy and financial position in detail and should not be regulated as heavily as a typical retail investor.

#### *No consideration exemption (s 708(15))*

This exemption operates when there is no monetary consideration or only nominal consideration provided in the share offering. It is beneficial for allowing companies to issue shares to employees in situations where disclosure is unnecessary, such as shares for compensation or as a performance bonus.

While there are other exceptions under s 708, including for takeovers and schemes of arrangement, retail investors are adequately protected by other exemptions of the Corporations Act.

#### *Employee equity schemes*

The disclosure exemptions in s 708 and Div 1A of pt 7.12 of the Corporations Act assist in facilitating the operation of employee equity schemes in Australia. The schemes encourage innovation and entrepreneurialism as the company's employees will invariably contribute to the company's rise in value. They are an important attraction and retention tool, especially for start-up businesses.

Retail investors are protected through features including, for offers that require payment to participate, the monetary cap (limiting offers to A$30,000 per year per person) and the requirement for a short form disclosure document, among other things.

## TRANSPARENCY AND MONITORING OF THE FINANCIAL SYSTEM

### Q14. What additional transparency measures relating to any aspect of public or private markets would be desirable to support market integrity and better inform investors and/or regulators?

Most wholesale client funds already have the benefit of extensive transparency and disclosure measures as an outcome of their negotiations with institutional investors. Currently the level of disclosure and reporting is investor driven, where institutional and anchor investors will negotiate a desired minimum framework within the fund documents for wholesale client funds.

This is in addition to the disclosure measures prescribed under existing regulatory frameworks for license holders and for those offering investment products to certain investor classes (eg retail investors).

When considering whether there is a requirement for further transparency measures, it is reasonable to consider factors such as:

- the likelihood, scale and materiality of the risk(s) being sought to address;
- the adequacy of existing regulatory regimes, requirements and powers;
- the costs, including opportunity cost, versus the benefit of additional requirements; and
- the impact of additional burdens on competition and dynamism within the regulated sector.

The DP notes that ASIC is conducting a review of different classes of industry participants' compliance with financial services laws. This is a sensible step and the Council would suggest ASIC complete this work and provide stakeholders with an update on substantial themes before making any determinations about future regulatory developments.

**Q15. In the absence of greater transparency, what other tools are available to support market integrity and the fair treatment of investors in private markets?**

In general, the suite of existing statutory obligations provide an adequate framework to support the market integrity and fair treatment of investors (see question 4).

There are a range of other tools available to support market integrity and fair treatment, including:

- *Investor education*: ensure ongoing broad based financial education and financial literacy programs are supported to assist retail investors developing understanding of risk, balancing risk and reward profile, understanding the importance of investment diversification and liquidity (and its limits in both public and private markets). This is particularly important in circumstances where there seems to be a proliferation of opportunities presented to retail investors in the crowdfunding space and via new (and unregulated) platforms that allow investors to trade in unlisted securities;

- *Financial advice*: significant work is underway in connection with ensuring access to quality and affordable financial advice. The Council supports efforts to ensure the continued development of Australia's financial advice sector so investors have adequate access to quality financial advice, and to help appropriate investors access a wide variety of investment asset classes.