Raising Money in Australia

Irrespective of why or how, raising money in Australia is a heavily regulated activity, with severe penalties for people who don't play by the rules. There are rules for both the party raising the money, as well as those assisting them.

People seek to raise capital in a number of different contexts. In its simplest form, people 'pool' their capital with others to carry out a particular venture (for example, to buy a property or start a business). More sophisticated structures may involve setting up a unit trust to hold an asset or raising money into a company to carry on a business.

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The starting position is that you must not raise capital without first preparing a **regulated disclosure** document.[2] However, there are a number of exceptions to this general rule.[3]

Small-scale private offerings

A small-scale private offering is the most common form of capital raising that does not require a regulated disclosure statement. A capital raising will qualify as a small-scale offering if you do not raise more than $2,000,000, from no more than 20 investors, in any rolling 12-month period.[4] For this reason, these provisions are often referred to as the **'20/12/12 Rule'**.

Offers made under the small-scale private offering exemption are generally done through an informal **Information Memorandum** or 'IM'.

When counting the number of investors you exclude a number of people, including those who have agreed to invest at least $500,000, those who receive the **offer outside Australia**,[5] any **officers** of the company, and those who have provided a **qualified accountant's certificate** evidencing they have earned more than $250,000 for the last 2 years[6] or have net assets of at least $2.5 million (i.e. a 'sophisticated investor'[7] or a 'wholesale client'[8]).

There is no restriction on the number of people that you can make the offer to, as long as the offer does not result in more than 20 investors in any 12-month period. However, you cannot advertise the offer to the public.[9] Each offer must be a **personal offer**[10] that can only be accepted by the person to

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[1] These rules are largely found in the *Corporations Act 2001* (Cth) (the **Act**) and associated regulations. Specifically, Chapter 6D and Chapter 7 of the Act.
[2] Section 727 of the Act prohibits the offer of Securities to Investors without disclosure, and section 703 of the Act provides that you cannot contract out of the fundraising provisions.
[3] Chapter 6D of the Act contains what are widely referred to as the 'fundraising provisions', which regulate the way in which capital can be raised in Australia without issuing a formal disclosure document.
[4] Section 708(1) of the Act.
[5] Section 708(5)(b) of the Act.
[6] This can include the income of entities controlled by the person.
[7] For the purposes of Chapter 6D of the Act.
[8] For the purposes of Chapter 7 of the Act.
[9] Section 734 prohibits advertising of small-scale offers.
[10] Defined in section 708(2) of the Act.

whom it is made. Furthermore, you must have reason to believe they are likely to be interested in the offer as a result of some **prior connection**. These people are generally restricted to family, friends and known business associates.

There is also an anti-avoidance provision that can apply where multiple entities are set up by the same controllers to keep the raising in each entity below the 20/12/12 thresholds.[11] Under these rules, ASIC may determine in writing that a number of different bodies are closely related and that their transactions should be aggregated for the purposes of the fundraising provisions. For this purpose, *"an entity controls a second entity if the first entity has the capacity of determine the outcome of decisions about the second entity's financial and operating policies".*[12]

<u>ASIC's power to modify the rules</u>

ASIC has the power to vary how the fundraising provisions apply to an individual or group of individuals.[13] A notable variation in this regard includes relief for business introduction services for managed investment schemes, which applies to registered managed investment schemes with fewer than 20 members seeking to raise up to $5 million.[14]

Other exemptions

There are a number of other exemptions from disclosure. These include (subject to certain requirements) offers made:

- To sophisticated or wholesale investors;
- To financial services licensees;
- Through financial services licensees;
- To professional investors;
- To people associated with the offeror;
- To certain present holders of securities;
- That include issues or sales for no consideration;
- Under a compromise or arrangement under Part 5.1 of the Corporations Act;
- Under a Deed of Company arrangement;
- As part of a Takeover; and
- For debentures in certain bodies.[15]

The type of entity raising the money

The type of entity through which you are raising money will also impact on what regulations apply.

A private company (i.e. 'proprietary limited') cannot have more than 50 non-employee members, and cannot raise money other than through an excluded offer that does not require regulated disclosure. This means that a regulated offer document cannot be used to raise money for a private company.

A public company (whether 'listed' or not) is able to raise money from the public and there is no restriction on the number of members. However, if the public company does not qualify for an exemption, then it must prepare a regulated disclosure document.

A unit trust is another popular vehicle for raising money, particularly for holding long-term investment assets such as property. This is because the income and capital gains are not taxable to the unit trust, but rather flow through to the unit holders, who pay tax in their own right. A unit holder may qualify for

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[11] Section 740 of the Act.
[12] Section 50AA of the Act.
[13] Section 741 of the Act.
[14] ASIC 22-267MR.
[15] For a full list see section 708 of the Act.

capital gains tax concessions on any gains, and a super fund will only pay tax at the rate applicable to the fund (which may be nil). However, using a unit trust as an investment vehicle can bring you into the managed investment scheme rules, as discussed below.

Managed investment schemes

When money is pooled in an unincorporated joint venture, or is raised into a unit trust, then the **managed investment scheme** (**MIS**) provisions must also be considered.[16]

Similar rules regarding capital raising apply to an MIS, including exceptions for small scale offerings. However, in addition to the capital raising regulations, the scheme itself may be required to hold an Australian Financial Services Licence (**AFSL**), have a responsible entity that must also hold an AFSL, and potentially also require a licensed asset custodian.

As a general rule, if none of the units issued by the unit trust require a regulated disclosure document to be prepared, then the unit trust itself is not likely to fall within the MIS provisions and therefore will not require a licence. However, if the people behind the unit trust promote such schemes on a regular basis or as part of their business, then this alone may cause the MIS provisions to apply.

Types of disclosure

If regulated disclosure is required for a capital raising, then it may take the form of a number of different documents.[17] The four different disclosure documents are:

- Prospectus;
- Short form prospectus;
- Profile statement; and
- Offer information statement, or 'OIS'.

Each document has different requirements and applicable thresholds.

Assisting someone raise capital

The activity of assisting another person raise capital is also subject to strict regulation.

You must not carry on a business of providing **financial services** to others unless you hold an appropriate AFSL. An AFSL can cover particular **types of services** (e.g., advising, dealing, etc.) in respect of particular **types of financial products** (e.g., shares, units, derivatives, etc.) to be provided to particular **types of clients** (e.g., wholesale clients and retail clients).

In order to obtain an AFSL you must demonstrate that you have the necessary training and experience to undertake the activity. You must also have insurance.

An alternative to holding your own AFSL is to become an **authorised representative** on another person's AFSL. In this case you will need to satisfy the licence holder that you have the necessary qualifications and experience. This generally takes the form of passing the RG146 examinations in the relevant areas. You are also then restricted to only advising on or dealing with financial products on the licence holder's 'approved list'.

What next?

Lawyers are able to assist a person raising capital without holding an AFSL provided that their involvement is part of or ancillary to providing legal services. An accountant may become involved in a limited range of financial aspects, such as providing financial information and reports and other

[16] These provisions are in Chapter 5C of the Act.
[17] Section 705 of the Act.

accounting services. However, in either case, this would not include promoting the offer or providing ‘financial services’ to the client.

If you would like to speak to someone about raising money, call us on 1300 654 590 or email us at wehelp@andreyev.com.au.

Further information can also be found on our website at www.andreyev.com.au.