



A Practical Guide to Raising Money for Companies

A courtesy guide prepared by Swaab Attorneys

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Restrictions on raising money for your company

Sometimes the promoters and directors of a company believe that they can raise money from friends and relatives without realising that they are bound by various legal restrictions.

The general rule in *section 113 of the Corporations Act 2001* is that a proprietary company cannot raise funds from the general public.

A **proprietary (or private) company** can only raise equity finance by offering its shares to:

- § its existing shareholders or
- § its employees or
- § certain classes of investor.

These classes of investor include:

- § small scale personal offers to investors (to no more than 20 investors in any 12 month period and raising no more than \$2 million in any 12 month period)
- § a person where no consideration is payable for the shares
- § listed companies
- § sophisticated investors (including high net worth individuals, financial services licensees, professional investors, and entities investing more than \$500,000).

A **public company** (usually a company with 50 or more non-employee shareholders) can raise equity funding (by issuing new shares) from all of these classes of investor. In addition a public company can invite the general public to invest, providing that it complies with the obligation to issue a disclosure document to accompany the invitation.

There are three basic types of disclosure document:

- § a **prospectus** is the standard disclosure document and has the broadest information requirements
- § an **offer information statement** has lower information requirements but can only be used for fundraising of up to \$5 million
- § a **profile statement** contains limited information and can only be used with the consent of the Australian Securities and Investments Commission.

Advertising restrictions

There are also restrictions on publicising investment opportunities.

Section 734 contains restrictions on advertising offers (except where the offer is exempt from the requirement to issue a prospectus). Usually an advertisement must contain a statement that the terms of the offer are contained in the prospectus and any application for shares must be made on the application form in the prospectus.

Section 736 provides that shares cannot be offered by unsolicited telephone calls or meetings (although email is not covered by this section).

Where documents (including a prospectus or business plan) are circulated to the public, the law relating to deceptive and misleading conduct applies.

Section 1308 of the Corporations Act 2001 makes it is an offence to include misleading statements in a Corporations Act document (including a prospectus).

Section 52 of the Trade Practices Act 1974 makes it an offence to engage in misleading or deceptive conduct relating to trade or commerce.

Section 1041H of the Corporations Act 2001 makes it is an offence to engage in misleading or deceptive conduct relating to financial services or products.

Section 12DA of the ASIC Act 2001 makes it an offence in trade or commerce to engage in misleading or deceptive conduct relating to financial services.

Licensing restrictions

If a person wants to give advice relating to a financial product (for example, recommending to a person that he should buy shares in a particular company or project) or deal in a financial product (for example, sell shares) he will usually require an Australian Financial Services Licence¹.

There are however certain exemptions to this requirement, which allow companies and their shareholders to offer shares to the public without the need to hold a licence. These include:

- § *self dealing* – where a person makes an offer to dispose of shares on his own behalf
- § *accountants* – where advice is provided to an interested party on the acquisition or disposal of shares to the extent that the advice is limited to advice relating to the shares
- § *solicitors* – where advice is provided on the acquisition of shares on the instructions of a client.

¹ See separate Swaab Practical Guide to Financial Services Regulation

Checklist for the management of and the exit from an investment

When an investor acquires a stake in a company, the investors will generally consider certain issues which arise in relation to the new investment. Some of the issues include:

Issue	Points to consider
Management	Whether a shareholder should have the right to appoint a director. Whether the directors should be given formal service agreements.
Critical Business Matters	Whether unanimous consent should be required at board or shareholder level for important matters, such as: <ul style="list-style-type: none"> § adopting or varying the business plan § changing the nature of the business § approving any borrowing by the company § creating any charge over the company's assets § entering into or amending any material contract.
Share transfers	Whether there should be restrictions on the transfer of shares in the company.
Compulsory share transfers	Whether a director (who also owns shares directly or through a company/trust) who ceases to be employed by the company, should be required to sell his shares.
Restraint	Whether there should be restrictions on shareholders from competing against the company, or soliciting customers or employees of the company, for a specified period of time in a specified geographical area after they cease to be shareholders.
Deadlock	In situations where there is a 50/50 deadlock at shareholder level and management of the company becomes untenable, should there be a provision allowing for one shareholder to acquire the shares of the other or for the company to be wound up?
Financing	Whether shareholders should be required to provide financial guarantees or additional funding in the future. Whether additional funding will be required from a lender and whether the company will be required to grant a charge over its assets as security for the loan.
Exit	Whether there should be an obligation to proceed with an exit (trade sale, share sale, IPO ²) after a specified period of time to allow the investor to cash in his investment.

² IPO means an initial public offering of shares when a company first lists on a stock exchange

The corporate team at Swaab Attorneys is committed to working with companies to help them meet their ambitions. If we can help you with any of the issues raised in this Guide, please contact either Fred Swaab or Alistair Jaque. We would be very pleased to discuss any issues with you.

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This Guide is intended to give an overview of the issues involved in raising money for companies. It is not intended to be fully comprehensive or to be a substitute for legal advice.