HOW-TO CROWD FUND: Q&A WITH XINJA'S CEO

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Last year Australia passed legislation to allow certain companies to access crowd-sourced funding (**CSF**). The CSF regime allows companies to raise funds from retail investors, the so-called 'mum and dad' investors, of up to $10,000 per retail investor each year. This source of funding was previously inaccessible to most start-ups and SMEs due largely to the onerous disclosure obligations which often make this avenue expensive and time-consuming. In contrast, the CSF regime is intended to provide an innovative, accessible and cost effective way for companies to source capital, with the entire CSF process conducted via an online equity crowdfunding platform.

Our client Xinja Holdings Limited (**Xinja**) was the first cab off the rank and recently closed its CSF offer raising in total close to AUD 2.5 million from 1,222 investors. We think that is an impressive effort, so we sat down with Xinja's CEO, Eric Wilson, and asked him some questions that we thought would be of interest to other businesses considering raising money through CSF.

Q: WHAT MADE YOU DECIDE TO RAISE FUNDS VIA CROWD FUNDING?

A: We said from the word go we would open an equity crowdfunding round as soon as it became legally possible in Australia and that's what we did - we were in fact the first raise that opened. The reason being, we are building a bank with our customers, and part of that is giving them a chance to own a piece of the action in order to benefit from any success we have. Plus we had seen equity crowdfunding run in other markets for neobanks with some success as a means not just of raising money but further engaging their customers.

Q: WHAT ARE YOUR VIEWS ON WHAT TYPES OF BUSINESSES WOULD BE SUCCESSFUL IN A CROWD FUNDING RAISE?

A: The point about equity crowd funding is not so much the vertical as the opportunity for ordinary people to invest in early stage companies, so there is no reason why this would not work across many industries, as long as the offer is compelling and the business case is sound.

Q: WHAT DO YOU THINK IS KEY TO RUNNING A SUCCESSFUL CROWD FUNDING CAMPAIGN?

A: It's important to have a strong base of enthusiasts or a marketing budget that will allow you to reach a relevant audience. The offer document must be compelling, which means a lot of rigour around building and substantiating the business case. You need to be ready to talk to potential investors and answer their questions in detail. You also have to be very responsible about explaining the risks. In many cases these people are not seasoned investors but ordinary Australians parting with hard-earned cash so we felt a significant responsibility to make sure they understood what they were doing, had read all the relevant documentation and were not investing what they couldn't afford to lose. A good platform or user experience that makes the process easy and transparent is also a must.

Q: WE KNOW THE REQUIREMENT TO PUT RISK WARNINGS ON ALL FORMS OF MEDIA (INCLUDING TWITTER) WAS SOMETHING YOU HAD TO CONSIDER IN REGARDS TO YOUR MARKETING MATERIAL – WERE THERE ANY OTHER TIPS OR HINTS YOU WOULD PROVIDE TO A COMPANY LOOKING TO CROWD FUND?

A: I think the main thing to remember is that it isn't "just money" you are raising. It is real people's savings, their efforts, and in many cases their hopes and dreams. Don't take the responsibility for those things lightly. This is absolutely not free money. Work closely with your intermediary, but don't be afraid to get them to reach out to ASIC on your behalf, or indeed do it yourself if you are uncertain or need guidance. We found ASIC to be very reasonable and rational in the way they handled our crowdfunding, but remember there are rules, they are there for a reason, be sure to follow them. Finally I would make sure you understand that people don't just magically turn up and give you money in a crowd fund, we had been talking to potential customers and investors through various channels for nearly 6 months before we did the crowdfunding. Crowdfunding is just the vehicle. All the other work still needs to be done.

SOUNDS GREAT, SO HOW DO I GET STARTED?

If you are considering raising capital through CSF, the first step is to ensure that your company is eligible. Importantly, at this point in time CSF is only available to public companies, so a proprietary company will need to convert into a public company before it can make a CSF offer. This will require a 'special resolution' of the company's shareholders and may necessitate the adoption of a new constitution and a restructure of the board (to be eligible a majority of the company's directors must ordinarily reside in Australia and a public company must have at least 3 directors). Some other things to think about are:

- OFFER PRICE: It may be necessary to conduct a share split in order to be able to offer marketable parcels of shares. In Xinja's experience more than 50% of its investors invested $500 or less, and more than half of those investors invested only $250.

- RETAINING A SHAREHOLDERS AGREEMENT: If your company has a shareholder's agreement, you will need to consider whether to keep it in place or terminate it and rely solely on the company's constitution. Strictly you may make a CSF offer subject to a shareholder's agreement, but many of the usual mechanics of a shareholder's agreement may become unworkable if there are hundreds of shareholders involved. It may make more sense to incorporate any rights that shareholders wish to retain (such as pre-emptive rights on share issues) into the company's constitution.

- OFFER DOCUMENT: While a company doesn't need to prepare a 'prospectus' and lodge it with ASIC, the CSF regime requires an offer document to be prepared and prescribes certain information that must be included in this document. As Eric indicated in our Q&A session, you will need to present a sound business case to entice investors, which will involve demonstrating where the value in the offer lies. This document must be clear and concise and must not contain any false or misleading statements.

- MARKETING CAMPAIGN: It seems a key to Xinja's success was its well thought-out marketing campaign. While in Xinja's case investors aged 55 - 64 invested the most on average, investors aged 25-34 invested most frequently on average. This may make social media an attractive option to drum up interest for a CSF offer, but be aware that almost *any* statement published about a CSF offer (even one yet to be made) must contain a risk warning and refer the reader or listener to the offer document.

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