The vast majority of Australian companies are privately held. There are many advantages for this. Private companies face fewer regulations and lower requirements than public companies when it comes to reporting to shareholders, for example.

But new sources of funding are starting to blur the lines between public and private companies. As a result, we should consider introducing an intermediary form of corporation that sits between the two.

The difference between public and private

Private companies are not designed to raise funds from a large group of shareholders. In fact, two of their key characteristics are that they cannot raise capital from the public and they are limited to having 50 non-employee shareholders.

This is part of the reason why private companies face fewer regulations – they provide very little protection to shareholders. They are not required to hold an annual general meeting, for instance, and do not need to provide their shareholders with financial statements or comment on the company's performance. Further, a shareholder might find it very difficult to sell their shares in a private company as this may require not only finding a buyer but also getting the board of directors' approval.

Historically, when a company required more funds than 50 non-employees could provide, they would convert into a public company. Counting on a wider base of investors and owners, public companies are more heavily regulated, addressing many of these concerns.

In comes crowd equity funding

A new form of funding has come on the scene – crowd equity funding (CEF). It allows companies to raise funds from a large range of investors through an online portal. Investors receive shares in the company in return for their investment.

CEF has the potential to bridge the gap between private and public: it enables companies to access funds from many investors without going through the traditional fundraising regulation. But the current framework , with restrictions like the prohibition on private companies raising funds from the public , creates a roadblock to accessing this type of finance.

Recognising this, in 2015, the government introduced a bill to enshrine CEF in legislation. The bill limited CEF to a select group of public unlisted companies. Ultimately the bill lapsed and a new bill is expected to be introduced this year.

Limiting CEF to public companies does not take into account the important role private companies play in our economy. So the government is also assessing whether CEF should be introduced to these types of companies.

But simply extending CEFs to private companies may not be ideal either.

Why we can't just extend CEF to private companies

If the introduction of CEF to private companies is accompanied by raising the ceiling for investors and introducing more accountability in the system, the issue of investor protection will be moot. However, this could mean the death of private companies as we know it. With increased regulation, the cost of running a private company will rise. This type of business may no longer meet the need of people who are currently running closely held companies – which form the bulk of private companies.

Further, there is a need to distinguish between two types of private companies – the one that may never be interested in accessing CEF and the one that may in the future. For instance, a private company may be a useful engine to set up new general, social and environmental enterprises as this type of company is cheap and cost effective to run. However, with the growth of such businesses, access to finance may be problematic and conversion to a public company may not be an ideal either. Something in between could be the solution.

A new form of company

Any consideration of CEF should be accompanied with discussion on how to promote small and medium enterprises, and whether to do so may require the establishment of a new form of company. One that allows entrepreneurs to access CEF when they outgrow a private company, while also providing some protection to investors.

Designing such a company form will ensure Australia does not fall behind the rest of the world, and will promote a different type of entrepreneurship.

Marina Nehme receives funding from Centre for International Finance and Regulation.

Read more http://theconversation.com/equity-crowdfunding-requires-a-rethink-on-company-structure-67373