



25 February 2016

Manager  
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The Treasury  
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PARKES ACT 2600

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To Whom It May Concern

### **Submission: Tax incentives for early stage investors**

1. Taxpayers Australia Ltd (Taxpayers Australia) welcomes the opportunity to submit our views in relation to Treasury's Policy Discussion Paper, *Tax incentives for early stage investors* (the discussion paper).
2. We commend the Government for proposing initiatives aimed at encouraging long-term growth of innovation and entrepreneurship in Australia.
3. We appreciate the short extension afforded to us. However, we had to work within very tight timelines in terms of our overall response. We do wish to express our concern. Treasury provided no more than nine days to respond to a proposal in a significant area of policy. This is insufficient time for stakeholders such as ourselves to engage a greater number of members in consultation. We have unfortunately limited the number of issues discussed by us in this submission as a result.
4. We consider such a short response time to be unacceptable for a government initiative that is intended to help Australia become a nation of innovators. We request that any subsequent consultation entails a more appropriate public consultation period.
5. Our submission focuses only on the definition of an innovation company.

### **About Taxpayers Australia**

6. Taxpayers Australia is a membership-based organisation. Our membership primarily comprises small to medium sized tax practices, sole tax practitioners, small businesses and individual taxpayers. We are a voice for our members in relation to law and policy matters.

## **Definition of an innovation company**

### ***Overview***

7. We recommend that the definition of an innovation company incorporates Method 1 and Method 2 outlined in the discussion paper.
8. Specifically, the definition of an innovation company should comprise the following components:
  - (i) a set of principles that defines innovation; and
  - (ii) a list of approved gateways.
9. Further, we propose that a company should be assessed and registered by Innovation Australia to be an eligible innovation company. The Australian Taxation Office (ATO) would accept this accreditation for the purposes of determining whether the company's investors are eligible for the proposed tax concessions.
10. Registration criteria would also include a list of excluded activities. If a company engages in an excluded activity above a certain threshold, it cannot be registered as an innovation company.
11. We recommend against Method 3, which would enable a company to seek a determination from the ATO on whether it qualifies as an innovation company if the other definition criteria are not satisfied. However, the company should have rights of appeal against decisions of Innovation Australia and the ATO.

### ***Principles-based component of definition***

12. The definition of an innovation company should include a set of principles (ie. Method 1 per the discussion paper). Non-prescriptive guidelines are necessary to ensure that the statutory definition will be sufficiently robust to accommodate future developments in technology and commerce (ie. innovation).
13. The discussion paper proposes a set of principles that had been considered in line with the Oslo Manual published by the Organisation for Economic Co-operation and Development. We wholly agree with using this internationally applicable set of guidelines as the basis for the principles that will be included in the statutory definition of innovation.
14. We also support the proposal to include a requirement that the innovation company would need to have the capability to commercialise the idea.
15. However, we do not agree with the proposal to include a requirement that the company will need to pursue global or broader opportunities rather than only focusing on local (Australian) markets. Companies with ideas that are genuinely innovative and which are commercially viable (in Australia) should not be disadvantaged merely because it may not be viable to pursue opportunities overseas.
16. For example, the innovation may be suitable for an aspect of the Australian environment that may not be common in other countries. Or the innovation company may not wish to commit to an overseas strategy within the first three years of operation, which is the initial start up phase – in this regard, we note that an established condition is that the innovation company must have been incorporated during the last three income years.

### ***Gateway component of definition***

17. The definition of an innovation company should also contain a list of specific gateways (or safe harbours). A company that meets one of the gateways would qualify as an innovation company without being required to satisfy the principles-based component of the definition.
18. Out of the five gateways suggested in the discussion paper, we support only the fourth suggestion, ie. participation in an approved governmental programme.
19. A company should qualify as an innovation company for tax purposes if it has been accepted into an approved Commonwealth, State or Territory programme that is designed to foster innovation and entrepreneurship. Another suitable gateway would be where a company is eligible for approved Commonwealth, State or Territory grants.
20. It would be up to the Federal Government to consult with its Department of Industry, Innovation and Science, Innovation Australia and their State and Territory counterparts to determine the programmes and grants that would be included in the list of gateways.
21. It may not be appropriate for all companies that are eligible for a particular gateway programme or grant to be classified as an innovation company. The gateway may be limited to companies that qualify for one specific component of the programme or grant. For instance, the Federal Government's Entrepreneurs' Programme has three elements. The discussion paper suggests only the Accelerating Commercialisation element of the programme as being a possible gateway.
22. We envisage that the process undertaken to approve a gateway would require the decision-makers to consider whether the eligibility criteria of the programme or the grant incorporates the principles contained in the statutory definition of an innovation company, or different principles which satisfy the intent and purpose of the statutory definition. Therefore a company that satisfies the gateway test would not be required to also satisfy the principles component of the definition.
23. The other four gateways and safe harbours suggested in the discussion paper are not appropriate:
  - (i) *The proposed research and development threshold gateway*

It would be inappropriate to legislate a standard threshold, as the appropriate benchmark would vary between industries. However, a company's level of research and development expenditure may be one relevant factor in determining the eligibility of a company to be an innovation company.
  - (ii) *The proposed accelerator programme gateway*

This would create a large unnecessary administrative burden on the accelerator industry. It would also be more difficult and costly for the Government to register and regulate accelerators for these purposes than to register and regulate Federal and State/Territory Government programmes.
  - (iii) *The proposed financial investors gateway*

Previous third party financing arrangements have no bearing on whether a company is innovative.
  - (iv) *The proposed patent gateway*

A patent does not in itself indicate whether a company is innovative or whether it has the capability or intention of commercialising an innovation. However, patents and

other intellectual property held by the company may be one relevant factor in determining a company's eligibility to be an innovation company.

### **Registration with Innovation Australia**

24. Innovation Australia should be given the statutory power to register a company as an innovation company.
25. This power would be well within its purview, given that its current powers include, *inter alia*, the administration of the Research & Development Tax Incentive and the oversight of the Federal Government's Entrepreneurs' Programme.
26. The ATO should administer the tax concessions available to investors in innovation companies but it should not be responsible for determining whether the company meets the definition of an innovation company.
27. We envisage that the accreditation process would comprise the following steps:
  - (i) Innovation Australia would assess an applicant company to determine whether it satisfies either the principles-based limb or the gateway limb of the statutory definition.
  - (ii) A successful applicant would be registered with Innovation Australia as an innovation company.
  - (iii) The ATO would accept the Innovation Australia registration as evidence that the company is an innovation company.
  - (iv) The ATO would then assess the company against other tax concession criteria that do not relate to the definition of an innovation company – for example, the proposed rules relating to incorporation, income, expenditure and listing.
  - (v) The ATO would endorse innovation companies that meet all necessary criteria as being a company in relation to which investors can access the tax concessions.
28. Our proposed process is modelled on the manner in which the ATO currently grants charity tax concessions in conjunction with the Australian Charities and Not-for-profits Commission (ACNC). The ACNC is responsible for registering a charity. The ATO then accepts the registered charity status of the organisation and endorses the charity for specific tax concessions.

### **Exclusions**

29. We agree with the proposal that there should be a list of excluded activities. If a company's participation in at least one excluded activity exceeds a particular threshold, it cannot qualify as an innovation company.
30. In principle, we agree with using the list of excluded activities from the United Kingdom's Seed Enterprise Investment Scheme as a basis for the Australian list of exclusions.
31. However, we suggest that Innovation Australia be given the responsibility for refining the list so that it is appropriate for the Australian scheme and business environment.
32. The list of excluded activities would form part of Innovation Australia's registration criteria.
33. The appropriate threshold above which an innovation company cannot engage in excluded activities should be determined by Innovation Australia as part of its assessment criteria. The threshold may vary depending on the applicant's industry, the type of excluded activity or the dollar amounts involved.

### Concluding comments

34. Thank you for this opportunity to contribute to the development of the Government's important strategies for encouraging Australian innovation and entrepreneurship.
35. This submission has been limited in scope to the definition of an innovation company due to the short consultation period. We are keen to be involved in any ongoing consultation in relation to other topics canvassed in the discussion paper. In particular, if there is any exposure draft legislation that ensues out of the discussion paper, we wish to register our interest in being involved in that consultation.
36. If you would like to discuss this submission further, please contact our Business Services Manager, Ms Lisa Greig, on 03 8851 4555 or [lgreig@taxpayer.com.au](mailto:lgreig@taxpayer.com.au).

Yours sincerely

A handwritten signature in black ink, appearing to read 'Moti Kshirsagar', written over a horizontal line.

Moti Kshirsagar  
Chief Executive Officer  
Taxpayers Australia Ltd