# Submission to the TAX INCENTIVES FOR EARLY STAGE INVESTORS

To:

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## Privacy of Submission

There are no privacy concerns with this submission.

## Response to Questions

### Australian innovation company

#### 4.1 - Are there any additional principles that should be included in defining an innovation company?

In general if a 'ring fence' of properties can be determined for what an Innovation Company (IC) looks like it would be a worthy set of guidelines. Using such a definition would allow for much positive government policy to be correctly focussed whilst excluding other companies not the focus of the policy. If an appropriate description can be found then generic or throw away exclusions such as 'listed' could be removed - many go ahead innovative companies are using the ASX in order to raise capital, why should that exclude them from a bunch of positive programs that would otherwise assist them if they raised capital on the private market instead.

A simple principle should be able to survive the 'baker test' - will this allow somebody on my street who has figured out a new and innovative way to bake bread from being included. Do we want that type of business included? Under Method 1 in several of the dot points an innovative baker could be included as an IC, is that the intent?

If there was a broader principle of - "using high technology to deliver products or services to global customers" then that would exclude the baker. But it would include so much more. Innovation should be about selling things made/produced in Australia to an audience larger than us. This actually could be a better bread oven - just not the bread !

## 4.2 What gateway criteria would best define an eligible innovation company?

If there was a light-handed way to certify an accelerator where the definition of an accelerator looked a little bit like:

- competitive entry
- private funds backing the accelerator (otherwise you have government money chasing government money, plus the government isn't picking the winner)
- content based - a program that imparts learnings to the participants

then the accelerator method would be the best gateway criteria.

## 4.3 Do these criteria meet the objective of attracting investment in innovation companies, without unnecessary regulatory burdens?

No - you need a simple definition else you will need significant regulatory language to prevent people utilising the complex nature to find loopholes.

## 4.4 What integrity risks are associated with each of these criteria? How might these risks be mitigated? For example, combining multiple tests together could mitigate risks.

I think unless there is a succinct way to explain what an IC is then you may need to explain what percentage of various activities is allowed. A company could be in the business operating hotels but using some very good software, customer may not take them seriously unless they have proved the system in the field and for many startups this means running their own trials. This is one example (using an excluded activity) but will there be a percentage allowable activities?

I know lots of startups delivering accounting and legal advice in some very innovative ways - they would seem to be excluded.

## 4.5 Are investors open to a process that involves lodging a self-assessment declaration prior to making investments, in order to assist with assessing take up and eligibility?

Why does an investor need to self-assess?
Are we limiting who can invest ?
It should be the IC that would need to self-assess surely ?

## 4.6 In relation to a gateway requirement that is based on approved accelerator programs, which types of organisations should be included and what qualifying criteria should be specified?

Start-up accelerators are the best way to support entrepreneurial ventures because they provide an ecosystem for founders to quickly develop their ideas.

An accelerator typically has some of the following attributes:

- Some form of investment vehicle takes a small equity holding for an investment of cash (some will do this up front, some will do it in traches over a program, some may pay expenses on production of expense claims);
- A program over a 3 month to 6 month period that includes regular contact, routine assessment of traction and progress in the business, mentoring, introductions to customers and future investors;
- Mentors are usually the investors and they are heavily involved helping to mentor the businesses;
- A general theme – it could be tech startup in general, mining tech focussed (Unearthed in Perth), financial tech focussed (Stone and Chalk in Sydney); and
- Competitive entry process via an application and assessment process – the best Accelerators are highly sought after by entrepreneurs.

Some important issues to be discussed with respect to Accelerators are:

- Private equity or not (do we allow these to pop up in CSIRO, Universities, etc where they would be using government funds to access government funds/incetnives)?
- Do the accelerators incorporate the companies they invest in Australia or overseas (some accelerators here insist that the companies in the program incorporate in Delaware)?
- Industry involvement level – should you set a level of external industry mentorship or should you allow it to be an extension of a university where all guidance is provided by academics?
- How do you 'accredit' the accelerators without damaging what makes them valuable – their ability to act nimbly? i.e. the process to bring them into the fold has to be light-handed.

This is not incubation – this is not about life support. Accelerators do just that (accelerate); they take the business and entrepreneurs on a rapid, customer/market centric path to test the viability of the idea/business. Incubators tend to bring in an external management team to work on an idea developed internally, they tend to take longer and take more equity. These are critical success factor for creating sustainable, high-growth ventures.

### 4.7 Are there any other investment activities that should be excluded?

### 4.8 Is it appropriate for innovation companies to be restricted to companies that are Australian residents for tax purposes?

Many companies are incorporated overseas but housed here. We want to encourage companies to have a global reach. Delaware incorporation is popular and as such if this form of registration effects them as being "Australian residents for tax purposes" then this may be a detracting factor.

## Direct investment into an innovation company

### 5.1 Are there any specific requirements that should be included within the sophisticated investor test to ensure that innovation companies are benefiting from both financial and technical/commercial support?

No.
A wealthy individual from the mining sector may want to back an app company – do you really want their advice forced onto the IC?
By restricting the offset to sophisticated investors you are limiting the very thing you are trying to increase.
The offset should be accessible by an investor who has access to and capital for innovation companies.

### 5.2 Other than the sophisticated investor test contained in the Corporations Act 2001, are there alternative tests that can achieve these same objectives?

The objective is to encourage more capital to be invested into ICs. Why would you limit the source of that capital, providing the IC is accessing it legally under the Corporations Act why would this tax incentive plan try to limit or enforce what another part of the law should be doing.

## Indirect investment via an innovation fund

We invest as a small family office/individual so this section has no relevance to us at this stage but I think a valid goal should be to make it easy for investment to flow and therefore any government based approval process probably will not assist in that respect. Whilst I have no direct answers for section 6 maybe the government could take a leaf from the startup community and take it light to start with.

## 6.1 Is it appropriate for the offset to be available in the year of a cash call in the case of indirect investments through a qualifying innovation fund?

It would make sense to have the offset available when the cash has been deployed by the fund. This would avoid schemes where cash is given to a fund, offset received, then cash returned without deployment into IC.

## 6.2 What is the most appropriate corporate structure for an innovation fund? What registration requirements should exist?

This should not be limited to 'the most appropriate structure' since there a many that are valid. We are aware of investors syndicating deals using:

- unit trusts with a corporate trustee; or
- Bare trust structure.

Offset should be available to any current vehicles investors are using to pool funds.

## 6.3 Should the incentive be limited to sophisticated investors in the case of investments through a qualifying innovation fund?

No, as per section 5.

## 6.4 Should qualifying innovation funds be proprietary limited companies, unlisted public companies, or some other company governed by the Corporations Act 2001?

As per 6.2, whatever structures investors are using now would be appropriate. It should be noted that the ASIC 20/12/2 rules for disclosure exemptions will limit the number and type of individuals. It is unnecessary to go beyond these requirements.

## 6.5 Should there be requirements placed on who can manage an innovation fund?

No, as above.

## 6.6 Is it appropriate to adopt an approval process similar to the UK Venture Capital Trusts and Australian Early Stage Venture Capital Limited Partnerships?

# Integrity measures

I have no comment on the integrity measures.

## 7.1 How will the Government maintain the integrity of Australia's tax system while providing the best possible support for innovative startups?

### 7.2 How could integrity measures be designed to attract and secure investment at the right stage of innovation without creating unnecessary red tape for investors?