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Association of Australian
Medical Research Institutes

SUBMISSION TO
**TAX INCENTIVES
FOR EARLY STAGE INVESTORS**
FEBRUARY 2016

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ABOUT AAMRI

AAMRI is the peak body representing medical research institutes (MRIs) across Australia. Our 45 member institutes are leaders in health and medical research, and collectively represent over 10,000 staff and students and an annual turnover of more than \$1 billion. The vast majority of our members are independent MRIs (iMRIs), that is, mission-driven charities legally independent of a university or hospital, and co-located with a hospital or healthcare provider. The remainder are university- or hospital-based medical research institutes, or an alliance of medical research partners, with a demonstrable level of independence.

Australia's MRIs work on an extensive range of human health issues, from preventative health and chronic disease, to mental health, Indigenous health and improved health services. Their research ranges from fundamental biomedical discovery through to clinical research and the translation of research findings from bench to bedside. Together, they aim to drive innovation in healthcare to improve the lives and livelihoods of people in Australia and world-wide.

RESPONSES TO DISCUSSION PAPER QUESTIONS

AUSRALIAN INNOVATION COMPANY

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

The consultation paper states that a qualifying innovation company is:

- an Australian company, which:
 - was incorporated during the last 3 income years;
 - had expenditure of \leq \$1,000,000 in the prior income year;
 - had assessable income of \leq \$200,000 in the prior income year;
 - is not an entity listed on any stock exchange; and
 - carries on a business that is defined to be eligible (where eligibility will be targeted to small, innovative companies which are likely to have difficulty accessing equity financing).

We strongly recommend that the proposed expenditure threshold for an eligible innovation company be raised to at least \$2 million. Some innovative endeavours are inherently more expensive than others (e.g. the commercialisation of medical research, requiring animal and human trials, versus innovation in information technology).

Assessable income should also only refer to commercial income and not venture capital investment or other grants. It will also be important for the incentive to be coordinated with the R&D Tax Incentive, including raising the income threshold above \$20 million.

We recommend excluding companies limited by guarantee from qualifying innovation companies.

We recommend amending the proposed principles of an innovation company as per below:

- creates a new OR IMPROVED product or service that other organisations or consumers could use;
- creates a new OR IMPROVED platform for the delivery of products and services.

We do not agree with the requirement that an innovation company must pursue global or 'broader' (whatever that refers to) opportunities rather than having a focus on only local markets. This could discriminate against truly local markets (e.g. Hills Hoist; indigenous health innovations).

Also, the discussion paper states that:

“Under this definition, the innovation company would need to have the capability to commercialise or bring to market and generate value from the idea..... The definition would also require the innovation company to exhibit high growth potential through a management team being able to successfully scale the business as it grows and maintain competitive advantages over incumbents or new competitors.”

However, it is not clear how they will be expected to exhibit this. For example, would a business plan be sufficient? **We recommend that this requirement be replaced with a requirement that the innovation company has a “management team that is experienced with a relevant track record”.**

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

The first suggested gateway criterion around the proportion of a company's R&D claims to other expenses is not necessarily an appropriate measure of innovation, especially if a company with large low margin turnover comes up with a great idea and decides to invest in R&D (e.g. generic players).

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

The UK enterprise exclusions are appropriate, with the following exceptions:

- (13) Provision of services for another business – This needs qualification since there are many innovative service providers.
- (15) Farming and market gardening – This criterion appears to be specifically geared to the UK experience. There is great potential for innovation in the farming industry, which is significant in Australia.

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?

We do not agree with limiting eligible investors to those that pass the sophisticated investor test in the *Corporations Act*. Not only does such a restriction unfairly constrain access to this important tax incentive, it potentially discourages funding for innovation companies from alternative 'retail' sources.

Part of the reasoning for this proposed restriction is to protect investors. However, there are existing protective laws in place requiring individuals or entities to disclose risks to potential investors. There are many investment propositions with significant risk attached – including many small (non-innovative) businesses. Investors in innovative companies or innovation funds should not be treated differently from investors in other companies or funds.

It is also not necessary to restrict investors so to “reduce administrative costs by limiting the disclosure requirements during fundraising”. Innovation companies can choose whether they wish to incur the additional costs associated with making share offers to retail investors. It's not necessary to restrict access to the tax offset to limit these costs.

We also strongly disagree with the reasoning that by limiting the scheme to sophisticated investors, innovative companies can “unlock commercial expertise” of these investors. Eligibility criteria should be based on the sole purpose of the scheme, that is, to attract investment into new innovative companies. Adding layers of complexity around potential supplementary roles for these investors would increase red tape and potentially discourage investment. And it certainly isn't an appropriate reason for excluding other investors.

INDIRECT INVESTMENT VIA AN INNOVATION FUND

Please note, there were inconsistencies in the numbering of questions for section 6, with the questions at the end of the discussion paper not correlating with those in the relevant question box in the body of the paper. We have used the questions provided in the question box in the body of the paper below.

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?

Yes.

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

No. Please see Qu 5.1

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

We recommend that qualifying funds should be proprietary limited companies limited by shares.

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

We recommend that they should have an appropriate track record and experience.

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?

It will be important to ensure linkages between schemes.

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?

There should be an emphasis on transparency, track record and understanding risk profile.

AAMRI MEMBERS

