

Submission to Treasury:

Tax incentives for early stage investors Policy Discussion Paper

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I am an entrepreneur building my own “innovation business”, Techboard.com.au and have advised startups and invested in sweat and cash in a number of what I would regard “innovation” businesses. I am a founding member of the Western Australian Association of Angel Investors Inc. I am an observer and supporter of the Nascent Startup Community in Western Australia and Australia. I have also worked in the field in the UK (2006-2009) and seen the benefit of the UK’s EIS and SEIS schemes and have seen the impact they had on the startup and tech community in the UK, specifically Scotland.

My comments on the discussion paper will be on two areas, firstly the eligibility criteria or definition of an Australian innovation company and secondly the proposal to use the Innovation tax incentive as an additional means of protecting retail investors (arguably from the ability to generate wealth

Innovation Company Definition issues

I feel the definition is too limited and it should be more closely aligned with eligibility for other programs such as the *Accelerating Commercialisation Grants*.

Stated requirements on page 4 of the Discussion paper:

“the innovation company would need to have the capability to commercialise or bring to market and generate value from the idea”

This is something that the Investor should be the judge of. Also the investment may be needed to buy in this capability or develop the capability.

“the innovation company will need to pursue global or broader opportunities rather than having a focus on only local markets.”

The implementation strategy for many innovation businesses will have a local focus in their early life and pursuing global or broader opportunities will often only be viable on the back of a successful local rollout. At the stage of the investment the company may have stated global or broader than Australia intentions this should be sufficient to meet this criteria as evidenced in fundraising documents such as Information Memorandum, Business Plan or Investor Presentation.

“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.”

Again this is something that the Investor should be the judge of, furthermore the management team will often be bought in with the investment raised.

Perhaps the most efficient way to address these requirements is for the investor to make a declaration as to their assessment on the company and to provide some evidence (such as investment documents) to support their declaration if later audited.

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

It is suggested that approval of a company’s activities as eligible to apply for the R&D Tax incentive should operate as a gateway criteria, perhaps in combination with a number of other elements.

Stated gateway: companies that have, within the last three years, developed, acquired or licensed an idea that has been filed as a patent in multiple jurisdictions.

This gateway is problematic for innovations developed by the company due to the patenting process, where actual filing of patents in multiple jurisdictions will not occur for up to 20 months from the initial filing in Australia. It would be more appropriate to have the gateway including the filing of an application under the Patent Cooperation Treaty.

Commentary relevant to Questions 5.1 and 5.2

Under heading 5.1 of the Discussion paper it is stated:

“Investment in innovation companies is inherently risky. Many investments will lose money, while others have the potential to make large gains. It is important to consider whether direct investment should be restricted to certain investors or open to anyone with the available funds.”

The Tax law the subject of the Discussion Paper does not determine who is permitted to make direct investment. All Tax law can do is determine which investors should get tax relief and which should not. This determination will obviously impact on the incentive different classes of investors have to invest. Any investor is prepared to invest (subject to being permitted to do so by the Corporations Law) should be treated equally and fairly. Tax benefits should not just be available to the wealthy.

There are limited ways in which non-sophisticated investors can invest in unlisted startups, tech companies or “innovation Companies” as defined in the Discussion Paper including in the new mechanism currently before parliament in the form of the Corporations Amendment (Crowd-sourced Funding) Bill 2015. It is suggested that the Provisions in the Corporations Law and related instruments provide more than adequate and arguably too much protection to non-sophisticated investors.

The Tax incentives are strongly influenced by the UK's EIS scheme which I understand has no similar limitation of access to the scheme. I see no justification for adding the sophisticated investor or any alternate test for access to the scheme.

Limiting access to the innovation tax incentives will create also issues in the rollout of the Crowdsourced Funding legislation if or when passed. The legislation is specifically geared to enable investment by both sophisticated and unsophisticated investors and is likely to be utilised by many innovation companies. If the access to the tax benefits is limited to sophisticated investors platform operators trying to encourage investment via their platform will need to explain that sophisticated investors in qualifying innovation companies get these tax benefits that retail investors do not, making it much harder to encourage retail investors to invest. Why can't we keep it simple?

If government is serious about encouraging investment in the #ideasboom via such mechanisms as providing tax breaks and equity crowd-funding it should make the tax advantages in question accessible to all and leave investor protection to the Corporations Law.

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