Article Information

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Taxation Bill to encourage innovation and investment in early stage companies released

On Wednesday 16 March 2016, the Tax Laws Amendment (Tax Incentives for Innovation) Bill 2016 (Bill) was introduced into Parliament.

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*On Wednesday 16 March 2016, the Tax Laws Amendment (Tax Incentives for Innovation) Bill 2016 (**Bill**) was introduced into Parliament. The Bill is part of the Government's $1.1 billion National Innovation and Science Agenda, containing proposed tax incentives for early stage investors and for venture capital investment.*

The Government has consulted widely with investors, industry bodies, universities and the start-up community during the development of the Bill through the Tax Incentives for Early Stage Investors Policy Discussion Paper (see article: Defining criteria for tax incentives for early stage investors). However, notably, there was no public consultation process on exposure draft legislation. The acceleration echoes the intention to implement the measures with effect from 1 July 2016.

***Partner, David Cornwell, Partner, Alan Jessup,** and **Senior Associate, Kimberley Levi** discuss the key aspects of the Bill.*

Early Stage investors

Investors that satisfy the investor criteria, invest in an eligible Australian early stage innovation company (**ESIC**), and receive qualifying shares, will have the benefit of:

- a non-refundable carry-forward tax offset equal to 20% of the amount paid for qualifying shares, capped at $200,000 each income year, and
- the shares being taken to be held on capital account, and the benefit of a 10 year capital gains tax exemption on the disposal of the shares in the ESIC, subject to those shares being held for at least 12 months. The 12 month minimum holding period is shorter than the proposed 3 year minimum holding period. However, an investor may not disregard any capital gain and must disregard any capital loss in relation to qualifying shares in an ESIC held for less than 12 months.

Qualifying investors

Generally, the incentive will be available to all types of investors, including direct investments by corporations and individuals, and indirect investments through trusts or partnerships. The incentive is not available to:

- 'widely held companies' and 100% subsidiaries of these companies
- non-sophisticated investors who invest more than $50,000 in ESICs in an income year
- investors who are affiliates of the relevant ESIC, and
- investors who, immediately after the shares are issued, hold more than 30% of the equity interests in the ESIC, or any entity connected with the ESIC.

Whilst the incentive is available to foreign residents, the tax offset may be less attractive to foreign residents that do not have an Australian income tax liability.

Qualifying ESIC

To be a qualifying ESIC, a company must:

- be an Australian incorporated company
- have been incorporated in Australia or registered with the Australian Business Register within the last 3 income years, or incorporated within the last 6 income years and it and any wholly owned subsidiaries have incurred expense of no more than $1,000,000 in total across all of the last three income years
- together with its wholly-owned subsidiaries, have not incurred total expenses of more than $1,000,000 or assessable income of more than $200,000 in the previous income year, and
- not be listed on any stock exchange.

In addition to the above, the company must:

- satisfy a principles-based test. This assesses whether the company is genuinely focused on developing a new or significantly improving an existing idea, for the purpose of commercialisation, and show that the business relating to that innovation has the potential for high growth, scalability, can address a broader than local market and has competitive advantages
- satisfy an objective test. This is a points-based test, in which a company must have at least 100 points based on previous research and development claims, receipt of an Accelerating Commercialising Grant under the Accelerating Commercialisation element of the Commonwealth’s Entrepreneurs’ programme, acceptance into eligible accelerator programs, third party financial investors, enforceable intellectual property rights, and existing collaborative agreements with research organisations or universities to commercialise an innovation, or
- obtain a ruling from the Commissioner about whether the company’s circumstances satisfy the principles-based test.

Qualifying Shares

Qualifying shares are newly issued equity interests that are shares in a qualifying ESIC. However, shares are not qualifying shares if they constitute an acquisition of an ESS interest under an employee share scheme.

ESIC reporting requirements

ESIC’s that receive investments from one or more investor entities in a financial year must provide information in the approved form about those entities to the Commissioner 31 days after the end of the financial year.

We will issue a further commentary if and when the Bill has been passed.