10

Australia's Corporate Venture Capital Tax Expenditure Programs

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> *[Various reports] illustrate the problems faced by SMEs in raising equity capital and emphasise that this is an important issue affecting Australia. Against this background, it is generally recognised that the government has a role to play in assisting the development of the SME equity market. It is clear that without appropriate government intervention many SME investment opportunities will simply not be taken up. Over recent years, the primary way in which the government has sought to address this concern is by the introduction of tax concessions as a 'carrot' to encourage venture capital investment. Originally, these concessions were offered under the MIC program and are now offered under the PDF program.*[*]

[10.1] Introduction

In comparison to several other developed countries around the world, Australia has a relatively small and immature formal venture capital market.[1] As discussed in Chapter 6, the formal venture capital industry in Australia has struggled to evolve organically and has had to rely heavily on government support for both its establishment and

* Stephen Barkoczy, Don Maloney and Wayne Ngo, *Pooled Development Funds Handbook* (Australian Tax Practice, 2001) 10.

1 Australian Government, Financial System Inquiry, 'Financial System Inquiry' (Final Report, November 2014) 14.

the tax concessions is counterbalanced to the extent that additional revenue has been generated from investee companies.[146]

Furthermore, by substituting 'front-end incentives' under the MIC program with 'back-end incentives' under the PDF program, the Government derives a 'timing benefit' in that it only needs to provide tax exemptions to shareholders once their shares in PDFs are disposed of or dividends are paid to them. This typically only occurs several years after the original investment has been made and usually only after investee companies have become profitable.[147]

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146 Ibid 56. The Government is also likely to recoup some of the cost of the PDF tax concessions as a result of the fact that interest on any borrowings applied to purchase PDF shares is not deductible to the extent that the shares produce dividends that are exempt from tax. This result flows from the operation of ITAA 1997 s 8-1(2)(c) which denies deductions for expenses incurred in gaining or producing exempt income. By way of contrast, an investor would usually be able to claim deductions for interest on borrowings applied to acquire shares in an ordinary company that generates assessable dividend income.

147 Barkoczy and Sandler, above n 66.

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