

Australia's Venture Capital Investment Vehicles

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*Australia's venture capital investment vehicles are highly regulated by legislation. High levels of regulation of venture capital investment vehicles also exist in many ... other jurisdictions ... The high level of regulation is not surprising, given that generous tax concessions apply under the relevant schemes pursuant to which such vehicles are established.**

[9.1] Introduction

Over the years, a range of different kinds of investment vehicles have been used to form venture capital funds in Australia. The three main kinds of vehicles that have been established for this purpose have been companies, limited partnerships and, to a lesser extent, unit trusts. Each kind of entity is quite different from a legal perspective and has its own distinct tax regime that gives rise to different tax treatment for both the entity and its members (i.e., the shareholders, partners and beneficiaries). Companies, for instance, are treated as separate taxpayers that are distinct from their shareholders, but operate subject to an 'imputation system', which is designed to alleviate double

* Stephen Barkoczy and Daniel Sandler, *Government Venture Capital Incentives: A Multi-Jurisdiction Comparative Analysis* (Australian Tax Research Foundation, 2007) 176.

This is a preview. Not all pages are shown.

The key point to note about MITs is that, under Div 275 of the ITAA 1997, trustees of MITs can choose to have gains and losses made on certain assets (including shares) taxed under the CGT regime.⁸³ Allowing MITs to have gains and losses taxed under the CGT regime provides certainty about their tax treatment⁸⁴ and places them in a similar position to superannuation funds which have, for many years, also had their gains and losses taxed under the CGT rules pursuant to special rules contained in Div 295 of the ITAA 1997 (see [8.3]). The fact that the CGT rules apply to MITs also ensures that eligible investors are able to benefit from discount capital gains that flow through to them.

MITs are also subject to special withholding tax rules (which are also in the process of being amended).⁸⁵ Under the current rules, trustees of MITs are required to withhold tax on 'fund payments'⁸⁶ made to entities whose address, or place of payment, is outside Australia.⁸⁷ Withholding tax is imposed at the rate of 30%, unless the recipient's address or place of payment is in an 'information exchange country'⁸⁸ in which case a lower rate of 15% applies.⁸⁹

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Australian Private Equity Handbook (CCH Australia, 2012) 176. Note, however, that the Board of Taxation has stated that 'the MIT structure is not always an appropriate vehicle for investment in venture capital as it does not allow the MIT (or, more specifically, the venture capital managers) to be actively engaged in the investee's business venture': Board of Taxation, *Review of Taxation Arrangements Under the Venture Capital Limited Partnership Regime: A Report to the Assistant Treasurer* (June 2011) 17.

- 83 ITAA 1997 ss 275-105, 275-115. Where they do not make this choice, the gains and losses will generally be taxed on income account: s 275-120. It is also worth mentioning that the MIT regime contains special rules that apply to carried interest payments: s 275-200. Under these rules, such payments are generally treated as assessable income of the recipient.
- 84 In particular, as has been noted, it provides 'an effective safe harbour' against the ATO Taxation Determinations discussed at [8.3.3]: Humphrey, above n 82, 183.
- 85 The current rules are contained in Subdiv 840-M of the ITAA 1997 and operate in conjunction with Subdiv 12-H in Sch 1 to the TAA. The Tax Laws Amendment (New Tax System for Managed Investment Trusts) Bill 2015 (Cth) proposes to amend these rules to ensure that they tie in appropriately with the new MIT regime that is being introduced by the Bill. For this purpose, a new Div 12A will be inserted into Sch 1 to the TAA, which contains special withholding tax rules for payments made by AMITs.
- 86 Fund payments are, broadly, distributions of the trust's net income for the year less excluded amounts (namely, dividends, interest and royalties, capital gains and losses in relation to CGT assets that are not taxable Australian property, and foreign source amounts): TAA Sch 1 s 12-405.
- 87 TAA Sch 1 s 12-385.
- 88 Information exchange countries are listed in reg 44E of the *Taxation Administration Regulations 1976* (Cth) and comprise countries with which Australia has DTAs and Tax Information Exchange Agreements.
- 89 *Income Tax (Managed Investment Trust Withholding Tax) Act 2008* (Cth) s 4. No income tax is payable in respect of payments that are subject to MIT withholding tax: ITAA 1997 s 840-815.

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