Speech by

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MEMBER FOR CALOUNDRA

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PARTNERSHIP AND OTHER ACTS AMENDMENT BILL

Mr McARDLE (Caloundra—Lib) (5.33 p.m.): Venture capital or equity capital for seed, start-up, expansion, management buy-out and buy-in and turnaround opportunities are currently available in Australia, but the major obstacle to attracting foreign venture capital investment has been the treatment of limited partnerships as companies under Australian taxation laws. Limited partnerships are favoured internationally as investment vehicles for venture capital investments and generally enjoy flowthrough taxation treatment overseas.

As I stated, a limited partnership by contrast was treated in the same way as a company in that it was treated as a taxable entity and the partnership itself has therefore paid tax on its income and capital gains at the corporate tax rate—currently 30 per cent per annum. The distribution of income from a limited partnership was treated as a dividend. When profits were distributed to a non-resident partner, dividend withholding tax was payable at the rate of 30 per cent, reducible to 15 per cent if paid to a resident of a country with which Australia has a double tax agreement unless a dividend was fully franked. In addition, the interest of the partner in an Australian limited partnership is an asset for capital gains tax purposes, the disposal of which would give rise to Australian capital gains tax consequences.

In 2002 the federal parliament enacted the Venture Capital Act and the Taxation Laws Amendment (Venture Capital) Act. These acts make key changes to the existing taxation regime, both for limited partnerships registered under the acts and their partners. These changes potentially benefit overseas investors investing in Australian companies directly or indirectly through such limited partnerships in two fundamental respects: one, flowthrough tax treatment and, two, tax exemption on capital gains for limited partners. With regard to flowthrough tax treatment, venture capital limited partnerships and Australian venture capital fund of funds and limited partnerships which are appointed as a general partner of a VCLP or AFOF are no longer treated as companies for tax purposes. Instead, the income profit gains and losses of the VCLP or AFOF flow through to its partners without payment of tax at the partnership level.

With regard to tax exemption on capital gains for limited partners, the limited partners or VCLP or AFOF which make gains or profits on the disposal of investments which meet the criteria under the acts are exempt from tax on those capital gains or profits. The bill currently before the House changes the Partnership Act 1891 to acknowledge the federal government legislation and to put in place an incorporated limited partnership which will allow venture capitalists, basically from overseas, to access the Australian market and provide a further avenue of funds for Australian businesses.

The introduction of the Commonwealth legislation and the amendment to the Partnership Act are not of themselves going to be sufficient to draw funds into this country. The tax concessions set out in the tax act and the Venture Capital Act are primarily directed towards attracting overseas capital into Australia and provide the framework for structures that are recognised as world's best practice for raising private equity funds.

The proposed concessions are intended to provide the industry with an ability to compete on a more level playing field with their counterparts in the UK and the US but, if the measures will see the inflow of capital that is predicted, this may depend on other factors including the ability to source significant quality investments, demonstrating significant returns on capital and generally demonstrating overseas that Australia is a good place to invest.

Ultimately, foreign capital will flow into Australia if investors believe that the potential return from Australian investments outweighs those of other jurisdictions. Although the provisions of the Venture Capital Act and the tax act go a long way to redressing the imbalance in the tax treatment that exists between Australian and alternative markets, naturally if we are to attract capital there are to be reasons for people with the capital to want to turn their mind to Australia. Invest Australia lists 10 good reasons to invest in Australia, and I acknowledge them for same. I do, though, refer to only a few today due to shortness of time.

Firstly, the Australian economy is the most resilient in the world, with the average annual real GDP growth of 3.5 per cent since 1998 exceeding most other OECD economies including the UK, Germany and Japan. The OECD forecast of 3.7 per cent growth in Australia in 2004 and four per cent in 2005 compares very favourably to the average OECD growth of three per cent and 3.1 per cent respectively. Additionally in 2003, net public debt in Australia was 3.1 per cent of GDP compared to an average for OECD countries of 49 per cent which included Japan at 79 per cent, the UK at 47 per cent and the US at 32 per cent.

Secondly, Australia has a dynamic financial services sector, with Australia's pool of investment funds under management being the fourth largest in the world and valued at $434 billion. Australia attracts more private equity funds than any other country in the Asia-Pacific region, accounting for 24 per cent of all private equity invested in the region, and is also a major capital market in the region, with an annual average growth of 12.7 per cent per annum over the last seven years.

Thirdly, Australia's telecommunication and IT market is the third largest in Asia and the 10th largest in the world whilst Australia is ranked first in the Asia-Pacific region and ninth world wide in e-business readiness. Australia is ranked fourth in the world for the adequacy of its communications infrastructure.

Fourthly, Australia is the No. 1 place in the world where expatriate staff want to live and work. Australia's cost of living is much lower than that of many other countries including the US, the UK, Germany, Japan, China, Hong Kong, Singapore and Canada. The majority of foreign investment in Australia does not require approval. Where approval is required, almost all foreign investment proposals are approved by the Foreign Investment Review Board. As a consequence, we now have in place a taxation regime, a vehicle regime and development which can assist the venture capital industry to move forward.

In fact, there are 189 organisations in Australia at present that do supply equity capital. In the six years between 1996 and 2002, $4.7 billion was invested through the industry in 1,285 investments through 1,006 investee companies. The challenge now is to attract overseas funds and that, of course, will not be easy. Venture capital is traditionally a risky business, and as a consequence the returns need to be higher than normal. In a recent article in *Business Acumen Queensland* Phil Dickie quoted Bob Vines, the managing director of George Patterson Partners, when he used the phrase ‘Challenger state'. To paraphrase the article, Challenger brands are pushing the boundaries beyond current perceptions. It is to this goal that we must aim for so many reasons.

If we turn to some of the statistics in relation to Australia's economic position in the world, there is real scope for positive feeling that venture capital could flow into this country. Australia is the 13th largest of the world's economies, rivalling other markets such as Brazil, Korea and India. Finance and insurance is the third largest sector in Australia's economy, generating almost eight per cent—or $53 billion—in GDP. The finance and insurance sector has had an annual growth rate since 1984-85 to date of 5.3 per cent, which is well above the combined average of all industries at 3.7 per cent. As such, the economic credentials of Australia are there, and we certainly have the financial capacity to undertake the task before us. However, what overseas investors may be seeking is the type of project or product that is more attractive than—or at least as attractive as—that of other countries, in particular the United States, Japan, Germany, the UK and many of the European or continental countries.

There is a challenge ahead, and legislation at both federal and state levels is an important step in that process. Time will tell whether the financial input will be strong when compared to the United States, but it is hoped that this is a start of a new procedure for seed capital in this country.