



Innovation Australia

Venture Capital Committee

Information Paper

Venture Capital Act 2002
Issued April 2012

A Partnership's Committed Capital

Operative provisions:

- Paragraph 118-425(1)(d) and Section 118-445, *Income Tax Assessment Act 1997* (ITAA97)
 - Division 9, *Venture Capital Act 2002* (VCA 2002)
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Purpose

This paper explains Innovation Australia's (the Board) and the Australian Tax Office's (ATO) approach to the operation of paragraph 118-425(1)(d) and section 118-445 of the ITAA97.

This paper is not financial services, tax or legal advice. Readers should seek such advice from qualified professionals for their particular circumstances.

Key Points

1. Measurement of a partnership's 'committed capital' in relation to paragraph 118-425(1)(d) and section 118-445 of the ITAA97 occurs each time an investment is made;
2. Where the partnership is connected, e.g. to a unit trust(s) the partnership's committed capital is the amounts contributed, or to be contributed in the future by the limited partners. However, the amount of the partnership's committed capital is reduced by amounts directed towards the acquisition of interests in other entities (eg., units in the connected unit trust), at the time this direction occurs.

Background

Paragraph 118-425(1)(d) ITAA97 limits a partnership registered under the VCA 2002 to investing no more than 30 per cent of its committed capital in an investee. Section 118-445 ITAA97 defines committed capital. Investments over the 30 per cent limit are ineligible investments and constitute a breach of registration requirements of Division 9 of the VCA 2002. Such investments are not 'eligible venture capital investments' and partners' shares in capital gains made in relation to such investments do not attract the capital gains tax (CGT) exemption in section 118-405 of the ITAA97.

Example for Illustration Purposes

DEF Growth Fund (the Fund) is a \$100 million venture fund consisting of twin unit trusts and a partnership. The Partnership is registered as a Venture Capital Limited Partnership (VCLP) under the VCA 2002. The Partnership will hold eligible VCLP investments and the unit trusts will hold other investments. Investors' capital is committed to the Partnership, but can be directed into the unit trusts in accordance with the partnership agreement and other associated agreements.

The Fund is about to make its first investment. The proposed investment will be \$20 million into Eric Sony & Son Pty Ltd by the Partnership. It is an eligible VCLP investment. None of the partnership capital drawn down under the Partnership agreement has been applied to units in either unit trust at this stage.

1. *s118-425(1)(d) and s118-445 are applied each time an investment is acquired*

The Partnership does not hold any investments in Eric Sony & Son Pty Ltd. At the time the investment is acquired the Partnership's committed capital, under section 118-445, is \$100 million. As the total amount the Partnership will invest in Eric Sony & Son Pty Ltd is \$20 million, or 20 per cent of its \$100 million committed capital, the investment satisfies paragraph 118-425(1)(d).

2. *Where the partnership has connected unit trust(s) those amounts that have been directed into the connected unit trust(s) can no longer be counted as the partnerships' committed capital under s118-445.*

Twelve months later the Fund is contemplating a \$5 million follow-on investment into Eric Sony & Son Pty Ltd. However, since the initial investment \$50 million of investor's capital has been directed into the unit trusts. These units are not assets of the partnership. The \$50 million is no longer available to the Partnership and cannot be counted in determining its committed capital. The Partnership's committed capital is reduced to \$50 million, ie., the original \$100 million minus the \$50 million no longer available for use by the partnership. The original \$20 million investment in Eric Sony & Son Pty Ltd remains eligible because it satisfied s118-425(1)(d) at the time it was acquired.

If the Partnership makes the \$5 million follow-on investment this will contravene paragraph 118-425(1)(d) ITAA97. Paragraph 118-425(1)(d) of the ITAA97 applies at the time the investment is acquired (i.e. 'made'), which means the proposed \$5 million follow-on investment would result in the Partnership having invested \$25 million, or 50 per cent of its \$50 million committed capital in Eric Sony & Son Pty Ltd. The acquisition of this investment by the Partnership would be a contravention of paragraph 118-425(1)(d) and a breach of the Partnership's registration requirements under Paragraph 9-3(1)(e) of the VCA 2002. Generally in this case the partnership would be required to dispose of this follow-on investment within six months or its VCLP registration would be revoked.

Note: It is an ongoing registration requirement that a partnership has at least \$10 million committed capital. Where the partnership forms part of a fund, as described above, investors capital that has been drawn into the partnership and capital still available to the partnership are both included in determining compliance with this requirement.