6 March 2020

Senate Select Committee
Financial Technology and Regulatory Technology
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Parliament House
Canberra ACT 2600

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Questions on Notice – Financial Technology and Regulatory Technology

Dear Senate Select Committee

Thank you for the opportunity to provide further information in relation to the questions raised at the Committee's hearing on Financial Technology and Regulatory Technology in Sydney on Thursday, 20 February 2020.

The Committee requested that the Australian Investment Council address four additional issues in relation to:

1. The early stage venture capital limited partnership (ESVCLPs) and venture capital limited partnership (VCLP) framework
2. ASIC's intervention powers
3. Opportunity Zones, and
4. Australian Regional Investment.

1. ESVCLP and VCLP Framework

What ongoing institutional structure should Australia have in place to improve the competitiveness of ESCVLPs and VCLPs?

It is our view that for Australia to achieve an investment environment for FinTech and RegTech that is competitive with other jurisdictions, it is critical for the investment framework to:

- have clear parameters
- be conducive to domestic and international investment, and
- align with best practice in other jurisdictions.

The key step for achieving this is to implement the Johnson Review recommendations for the introduction of a Limited Partnership Collective Investment Vehicle within the next two years.

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Recommendation 1: *Prioritise amendments to the ESVCLP and VCLP framework*

Johnson recommendations

Australia's retention of a Trust system as an investment vehicle is misaligned with the use of collective investment vehicles (CIVs) in other jurisdictions.

The 2009 Johnson Review into Australia as a Financial Centre to recommended the introduction of two new CIVs to grow Australia's capacity to attract inbound investment into our economy. These two CIVs, known as a corporate collective investment vehicle and a limited partnership collective investment vehicle, are yet to be implemented. We understand that work on the Limited Partnership CIV is yet to even commence.

Implementing CIVs as a priority will reignite Australia's competitiveness as an investment destination as investors are familiar with this form of investment vehicle. This in turn will increase the pool of capital for investment which will have the flow on benefits of economic growth and attracting talent.

Recommendation 2: *Implement an internationally competitive Collective Investment Vehicle framework*

The Australian Investment Council recommends that the Government finalises the recommendations in the 2009 Johnson Review to implement a globally competitive investment regime that uses collective Investment Vehicle framework.

What recommendations does the Australian Investment Council for refinements to the ESVCLP and VCLP regime?

The list of outstanding measures in the ESVCLP and VCLP framework is in Appendix 1.

These are categorised as priority 1 or 2 to indicate the level of urgency for implemented each item.

2. ASIC's product intervention powers

What are the Australian Investment Council's views on ASIC's product intervention powers?

ASIC's new product intervention powers designed to protect consumers from excessive fees, could also have the indirect effect of introducing greater risks for investors into innovative FinTech and RegTech companies, which ultimately impacts on the ability of those businesses to raise capital from investors.

The broad nature of the intervention powers could prevent some legitimate fintech products from going to market and stifle the innovation and growth potential of some businesses.

Early intervention by ASIC to provide FinTech and RegTech companies with clarity on any perceived issues in the early stage development of their products would be beneficial.

3. Opportunity Zones

How do the opportunity zones work in the USA?

Opportunity Zones (OZs) are defined as "economically-distressed communities where new investments, under certain conditions, may be eligible for preferential tax treatment." First conceived in April of 2018, OZ plans are now in place for communities in all 50 states in the USA this year.

Each state nominates blocks of low-income areas by census tract, which are then certified by the Secretary of the U.S. Treasury via his delegation of authority to the Internal Revenue Service. Through the IRS, investors can file a Form 8896 to create a Qualified Opportunity Fund — vehicles structured as either a partnership or corporation for the purpose of investing in an OZ census track, whether in real estate or directly in businesses through equity. The fund is required to hold at least 90% of its assets in that qualifying OZ area.

To qualify, the Opportunity Fund must invest more than 90% of its assets in a Qualified Opportunity Zone Property located in an Opportunity Zone. The property must be significantly improved, which means it must be an original use, or the basis of the property must be double the basis of the non-land assets. Capital gain taxes are deferred for investments reinvested into investments in these zones and, if the investment is held for ten years, all capital gains on the new investment are waived. Opportunity Zones are census tracts designated by state authorities.

An investor must invest in an Opportunity Fund by the end of 2019 to meet the seven-year holding period and be able to exclude 15% of the deferred capital gain. An investor may exclude 10% of the deferred capital gain by investing in an Opportunity Fund by the end of 2021 to meet the five-year holding period.

An investor who realises certain capital gain income may reinvest the capital gain in an Opportunity Fund within 180 days.

Capital has moved in a predictable fashion, to serve certain regions and populations which is why certain groups and places continue to be left behind. OZs are simply an incentive to move capital across America in a more inclusive fashion; more quickly and to more places where it just naturally wouldn't end up.

How has the program been received?

Understanding the mechanisms of the OZs has created a barrier to entry for more socially-minded investors.

To make a profit, essentially a taxpayer must sell an asset and generate a capital gain. The taxpayer then puts the capital gain into a Qualified OZ fund. There is ultimately delay and reduction of taxes owed to the government — if held for 10 years, that taxpayer can pay zero capital gains tax on the new investment in the fund.

Can you provide evidence of its success?

While the program is relatively new, there are two key benefits.

The first is that it provides equity by lending to minority business owners, lending to get affordable housing and student loans for those trying to pay back these loans and navigate out of debt with no cushion or family support.

The second is that this program compared to others really reaches broadly. Most folks live within the proximity of opportunity zones. It touches everyone in a lot of ways which is a positive impact of capital working on a big problem.

4. Regional investment

What needs to be done in Australia to encourage regional investment?

There is currently a lack of capability and investment capacity to support new ventures and innovative businesses located in regional and rural areas of Australia, despite the fact that regional Australia contributes one third of our national output and is home to 8.8 million people.

With the establishment of the Biomedical Translation Fund and overseas schemes such as the Opportunity Zones program in the US, the government has a blueprint for launching programs which couple government funding and private capital and direct it towards specific areas of need.

As an example, the need for investment in new technologies to make farming more viable and sustainable, can be seen in the growing number of AgTech start-ups that are progressing through incubator and accelerator programs with help from seed and early stage capital.

In the next few years, these new businesses will need further funding support, particularly from VC investment, to get to their next stages of growth. These businesses' innovative products and services have the potential to revolutionise Australia's AgTech sector which is predicted to be Australia's next $100 billion industry by 2030.

Recommendation 3: *Launch a Regional Innovation Fund*

A Regional Innovation Fund be introduced to stimulate and support the establishment and growth of startups, news businesses and industry sectors to catalyse economic growth of FinTech and RegTech in regional and rural areas of Australia.

5. Facts, figures and examples.

One area where Australia has a natural advantage is in the agricultural technology (Agtech) sector, which covers everything from farm management software, robotics, bioenergy and biotechnology, to innovative food and 3D food printers.

According to Austrade, global investment in Agtech in 2017 was $14.6 billion, an increase of almost 30 per cent on the previous year. While investment in Agtech in Australia is 50 per cent less per capita than in the USA, it is predicted to become Australia's next $100 billion industry by 2030.

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6. Case Studies

Agerris

Agerris is an Agtech startup company that has developed autonomous robotic solutions to improve agricultural productivity and environmental sustainability.

These have been developed by Agerris CEO, Salah Sukkarieh, who is also professor of Robotics and Intelligent Systems at the University of Sydney.

Professor Sukkarieh has translated his research into the production of farm equipment that combines artificial intelligence and robotics, deploying drones and self-driving farmbots that can collect data, herd animals, undertake precision seeding, intelligent spraying and chemical free weeding.

AgriDigital

Another development in the sector has combined Fintech with Agtech to enhance the efficiency of logistics and payment platforms.

AgriDigital developed a block-chain enabled agricultural platform to generate more efficient movement of commodities into markets. The platform uses a single source of records through which traceability, financing and real-time payment can be achieved.

Since its first deal in 2016, two and a half million tonnes in grain and $500 million in payments have been transacted through the AgriDigital platform. In 2018, Square Peg Capital and a private family investment office invested $5.5 million in the startup to help it expand into North America.

Yours sincerely

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