



Taxation Laws Amendment (Venture Capital) Act 2002

No. 136, 2002

An Act to amend the law relating to taxation, and for related purposes

Note: An electronic version of this Act is available in SCALEplus (<http://scaleplus.law.gov.au/html/comact/browse/TOCN.htm>)

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No. 136, 2002

An Act to amend the law relating to taxation, and for related purposes

[Assented to 19 December 2002]

The Parliament of Australia enacts:

1 Short title

This Act may be cited as the *Taxation Laws Amendment (Venture Capital) Act 2002*.

2 Commencement

- (1) Each provision of this Act specified in column 1 of the table commences, or is taken to have commenced, on the day or at the time specified in column 2 of the table.

Commencement information		
Column 1	Column 2	Column 3
Provision(s)	Commencement	Date/Details
1. Sections 1 to 3 and anything in this Act not elsewhere covered by this table	The day on which this Act receives the Royal Assent	19 December 2002
2. Schedule 1, item 1	Immediately after the commencement of item 2 of Schedule 2 to the <i>Taxation Laws Amendment Act (No. 2) 2000</i>	31 May 2000
3. Schedule 1, items 2 to 4	The day on which this Act receives the Royal Assent	19 December 2002
4. Schedule 1, item 5	Immediately after the commencement of item 3 of Schedule 2 to the <i>Taxation Laws Amendment Act (No. 2) 2000</i>	31 May 2000
5. Schedule 1, items 6 to 27	The day on which this Act receives the Royal Assent	19 December 2002
6. Schedules 2, 3 and 4	The day on which this Act receives the Royal Assent	19 December 2002

Note: This table relates only to the provisions of this Act as originally passed by the Parliament and assented to. It will not be expanded to deal with provisions inserted in this Act after assent.

- (2) Column 3 of the table is for additional information that is not part of this Act. This information may be included in any published version of this Act.

3 Schedule(s)

Each Act that is specified in a Schedule to this Act is amended or repealed as set out in the applicable items in the Schedule concerned, and any other item in a Schedule to this Act has effect according to its terms.

Schedule 1—Capital gains and capital losses, and related matters

Income Tax Assessment Act 1997

1 Section 11-10 (table item headed “interest”)

Omit “51-55”, substitute “51-57”.

2 Section 11-15 (table item headed “foreign investment”)

Before:

gain or profit from realisation of venture capital equity 51-55

insert:

gain or profit from realisation of eligible venture capital
investments 51-54

3 After section 26-65

Insert:

26-68 Loss from disposal of eligible venture capital investments

Partners in VCLPs

- (1) You cannot deduct under this Act your share of a loss made from the disposal or other realisation of an *eligible venture capital investment if:
 - (a) it is made by a *VCLP that is *unconditionally registered; and
 - (b) were that disposal or other realisation to be a *disposal of a *CGT asset, your share of any *capital gain or *capital loss would be disregarded under section 118-405.

Partners in AFOFs

- (2) You cannot deduct under this Act your share of a loss made from the disposal or other realisation of an *eligible venture capital investment if:
 - (a) it is made by:
 - (i) an *AFOF that is *unconditionally registered; or

- (ii) a *VCLP that is unconditionally registered and in which an AFOF that is *unconditionally registered is a partner; and
- (b) were that disposal or other realisation to be a *disposal of a *CGT asset, your share of any *capital gain or *capital loss would be disregarded under section 118-410.

Eligible venture capital investors

- (3) You cannot deduct under this Act a loss made from the disposal or other realisation of an *eligible venture capital investment if:
 - (a) you are an *eligible venture capital investor; and
 - (b) were that disposal or other realisation to be a *disposal of a *CGT asset, any *capital gain or *capital loss would be disregarded under section 118-415.

4 Before section 51-55 (first occurring)

Insert:

51-54 Gain or profit from disposal of eligible venture capital investments

Partners in VCLPs

- (1) An entity's share of any gain or profit made from the disposal or other realisation of an *eligible venture capital investment is exempt from income tax if:
 - (a) it is made by a *VCLP that is *unconditionally registered; and
 - (b) were that disposal or other realisation to be a *disposal of a *CGT asset, the entity's share of any *capital gain or *capital loss would be disregarded under section 118-405.

Partners in AFOFs

- (2) An entity's share of any gain or profit made from the disposal or other realisation of an *eligible venture capital investment is exempt from income tax if:
 - (a) it is made by:
 - (i) an *AFOF that is *unconditionally registered; or

- (ii) a *VCLP that is unconditionally registered and in which an AFOF that is *unconditionally registered is a partner; and
- (b) were that disposal or other realisation to be a *disposal of a *CGT asset, the entity's share of any *capital gain or *capital loss would be disregarded under section 118-410.

Eligible venture capital investors

- (3) Any gain or profit made from the disposal or other realisation of an *eligible venture capital investment is exempt from income tax if:
 - (a) you are an *eligible venture capital investor; and
 - (b) were that disposal or other realisation to be a *disposal of a *CGT asset, any *capital gain or *capital loss would be disregarded under section 118-415.

5 Section 51-55 (second occurring)

Renumber as section 51-57.

6 After Subdivision 118-E

Insert:

Subdivision 118-F—Venture capital investment

Guide to Subdivision 118-F

118-400 What this Subdivision is about

Some foreign residents disregard capital gains and capital losses from CGT events that relate to investments, in Australian companies (and in some cases foreign holding companies), that meet the requirements of this Subdivision.

These investments are made:

- (a) through limited partnerships, known as venture capital limited partnerships, that are unconditionally registered under Part 2 of the *Venture Capital Act 2002*; or

- (b) through limited partnerships, known as Australian venture capital funds of funds, that are unconditionally registered under that Part; or
- (c) directly by foreign residents who are registered under Part 3 of that Act.

Note: Registration of a limited partnership under Part 2 of that Act also leads to its income and losses being assessed under Division 5 of Part III of the *Income Tax Assessment Act 1936* on the basis that it is a partnership.

This is an exception to the general rule, under Division 5A of that Part, that limited partnerships are assessed as companies. For this purpose, registration does not need to be unconditional.

Table of sections

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- 118-445 Meaning of *committed capital*

[This is the end of the Guide.]

Operative provisions

118-405 Exemption for certain foreign venture capital investments through venture capital limited partnerships

General

- (1) All of your share in a *capital gain or a *capital loss from a *CGT event is disregarded if:

- (a) you are an *eligible venture capital partner in a *limited partnership; and
- (b) the CGT event relates to an investment that the partnership made that is an *eligible venture capital investment; and
- (c) when the partnership made the investment, the partnership:
 - (i) was a *venture capital limited partnership that was *unconditionally registered; and
 - (ii) met all of the *registration requirements of a VCLP that are not *investment registration requirements; and
- (d) at the time of the CGT event, the partnership:
 - (i) owned the investment; and
 - (ii) had owned the investment for at least 12 months; and
 - (iii) was a venture capital limited partnership that was unconditionally registered; and
 - (iv) in the case of a capital gain—met all of the registration requirements of a VCLP that are not investment registration requirements.

Note: The registration requirements of a VCLP are set out in section 9-1 of the *Venture Capital Act 2002*. It is important to understand that this is a separate requirement from registration under Part 2 of that Act (which effectively determines whether an entity is a VCLP).

It is technically possible to be registered under Part 2 of that Act without meeting the registration requirements of a VCLP, but you might still not be entitled to exemption under this section.

Meaning of venture capital limited partnership

- (2) A *limited partnership is a ***venture capital limited partnership*** at a particular time if, at that time, the partnership's registration as a venture capital limited partnership under Part 2 of the *Venture Capital Act 2002* is, or is taken to have been, in force.

For when the registration is, or is taken to have been, in force, see section 13-10 of the *Venture Capital Act 2002*.

Note: In this Act and the *Venture Capital Act 2002*, the term “venture capital limited partnership” is usually abbreviated to “VCLP”.

Shares acquired by converting convertible notes

- (3) A partnership that acquired a *share in a company by converting a *convertible note, or a convertible preference share, issued by the company is treated, for the purposes of subparagraph (1)(d)(ii), as

having owned the share from the time when it last acquired the convertible note or convertible preference share.

118-410 Exemption for certain foreign venture capital investments through Australian venture capital funds of funds

Gains or losses as a partner in a VCLP

- (1) All of your share in a *capital gain or a *capital loss from a *CGT event is disregarded if:
- (a) you are an *eligible venture capital partner in a *limited partnership; and
 - (b) the CGT event relates to an *eligible venture capital investment made by a *VCLP in which the partnership is a partner; and
 - (c) when the investment was made, the partnership:
 - (i) was an *Australian venture capital fund of funds that was *unconditionally registered; and
 - (ii) met all of the *registration requirements of an AFOF that are not *investment registration requirements; and
 - (d) when the investment was made, the VCLP:
 - (i) was unconditionally registered; and
 - (ii) met all of the *registration requirements of a VCLP that are not investment registration requirements; and
 - (e) at the time of the CGT event, the partnership:
 - (i) was an Australian venture capital fund of funds that was unconditionally registered; and
 - (ii) in the case of a capital gain—met all of the registration requirements of an AFOF that are not investment registration requirements; and
 - (f) at the time of the CGT event, the VCLP:
 - (i) owned the investment; and
 - (ii) had owned the investment for at least 12 months; and
 - (iii) was unconditionally registered; and
 - (iv) in the case of a capital gain—met all of the registration requirements of a VCLP that are not investment registration requirements.

Note: The registration requirements of an AFOF are set out in section 9-5 of the *Venture Capital Act 2002*. It is important to understand that this is

a separate requirement from registration under Part 2 of that Act (which effectively determines whether an entity is an AFOF).

It is technically possible to be registered under Part 2 of that Act without meeting the registration requirements of an AFOF, but you might still not be entitled to exemption under this section.

Gains or losses from direct investments

- (2) All of your share in a *capital gain or a *capital loss from a *CGT event is disregarded if:
- (a) you are an *eligible venture capital partner in a *limited partnership; and
 - (b) in the case of a capital gain—the CGT event relates to an *eligible venture capital investment that the partnership made in a company in which a *VCLP, of which the partnership is a partner, owns one or more eligible venture capital investments; and
 - (c) when the investment was made, the partnership:
 - (i) was an *Australian venture capital fund of funds that was *unconditionally registered; and
 - (ii) met all of the *registration requirements of an AFOF that are not *investment registration requirements; and
 - (d) when the investment was made, the VCLP owned one or more eligible venture capital investments in the company referred to in paragraph (b); and
 - (e) at the time of the CGT event, the partnership:
 - (i) owned the investment; and
 - (ii) had owned the investment for at least 12 months; and
 - (iii) was an Australian venture capital fund of funds that was unconditionally registered; and
 - (iv) in the case of a capital gain—met all of the registration requirements of an AFOF that are not investment registration requirements.

Note: The registration requirements of an AFOF are set out in section 9-5 of the *Venture Capital Act 2002*. It is important to understand that this is a separate requirement from registration under Part 2 of that Act (which effectively determines whether an entity is an AFOF).

It is technically possible to be registered under Part 2 of that Act without meeting the registration requirements of an AFOF, but you might still not be entitled to exemption under this section.

Meaning of Australian venture capital fund of funds

- (3) A *limited partnership is an **Australian venture capital fund of funds** at a particular time if, at that time, the partnership's registration as an Australian venture capital fund under Part 2 of the *Venture Capital Act 2002* is, or is taken to have been, in force.

For when the registration is, or is taken to have been, in force, see section 13-10 of the *Venture Capital Act 2002*.

Note: In this Act and the *Venture Capital Act 2002*, the term "Australian venture capital fund of funds" is usually abbreviated to "AFOF".

Shares acquired by converting convertible notes

- (4) A partnership that acquired a *share in a company by converting a *convertible note, or a convertible preference share, issued by the company is treated, for the purposes of subparagraphs (1)(f)(ii) and (2)(e)(ii), as having owned the share from the time when it last acquired the convertible note or convertible preference share.

118-415 Exemption for certain venture capital investments by foreign residents

General

- (1) A *capital gain or a *capital loss from a *CGT event is disregarded if:
- (a) the CGT event relates to an investment that you made that is an *eligible venture capital investment; and
 - (b) you were an *eligible venture capital investor when you made the investment; and
 - (c) at the time of the CGT event:
 - (i) you owned the investment; and
 - (ii) you had owned the investment for at least 12 months; and
 - (iii) you were an eligible venture capital investor.

Meaning of eligible venture capital investor

- (2) An entity is an **eligible venture capital investor** at a particular time if, at that time, the entity:
- (a) is a *tax-exempt non-resident; and

(b) is registered under Part 3 of the *Venture Capital Act 2002*.

Shares acquired by converting convertible notes

- (3) An entity that acquired a *share in a company by converting a *convertible note, or a convertible preference share, issued by the company is treated, for the purposes of subparagraph (1)(c)(ii), as having owned the share from the time when it last acquired the convertible note or convertible preference share.

118-420 Meaning of *eligible venture capital partner* etc.

- (1) A partner in a *limited partnership is an ***eligible venture capital partner*** if:
- (a) the partner is a *tax-exempt non-resident; or
 - (b) the partner is a *foreign venture capital fund of funds, and the sum of:
 - (i) the partner's *committed capital in the partnership; and
 - (ii) the sum of the amounts of committed capital in the partnership of any entities that are *connected entities of the partner;does not exceed 30% of the partnership's committed capital; or
 - (c) the partner meets the requirements set out in subsection (6), and the sum of:
 - (i) the partner's committed capital in the partnership; and
 - (ii) the sum of the amounts of committed capital in the partnership of any entities that are connected entities of the partner;is less than 10% of the partnership's committed capital.
- Note: Subsection (7) prevents some trusts from being eligible venture capital partners.
- (2) An entity that is an *associate of the partner only because the entity is a partner in the partnership in question is taken not to be a *connected entity of the partner for the purposes of subparagraphs (1)(b)(ii) and (c)(ii).
- (3) An entity is a ***tax-exempt non-resident*** if:
- (a) the entity is a foreign resident; and
 - (b) the entity is a resident of:

- (i) Canada; or
 - (ii) France; or
 - (iii) Germany; or
 - (iv) Japan; or
 - (v) the United Kingdom; or
 - (vi) the United States of America; or
 - (vii) any other foreign country prescribed by the regulations;
and
- (c) the entity's income is exempt, or effectively exempt, from taxation in the entity's country of residence.
- (4) An entity that is a *limited partnership is a ***foreign venture capital fund of funds*** if:
- (a) the partnership was established by or under a law in force in, or in a part of:
 - (i) Canada; or
 - (ii) France; or
 - (iii) Germany; or
 - (iv) Japan; or
 - (v) the United Kingdom; or
 - (vi) the United States of America; or
 - (vii) any other foreign country prescribed by the regulations;
and
 - (b) every partner who is a *general partner is a resident of a country referred to in paragraph (a); and
 - (c) the partnership is not a general partner of a *VCLP.
- (5) An entity that is not a *limited partnership is a ***foreign venture capital fund of funds*** if:
- (a) whether by operation of law or by election, the entity is not taxed as an entity in its country of residence, but the entity's income is taxed to its members according to their interests in the entity; and
 - (b) the entity was established by or under a law in force in, or in a part of:
 - (i) Canada; or
 - (ii) France; or
 - (iii) Germany; or
 - (iv) Japan; or

- (v) the United Kingdom; or
 - (vi) the United States of America; or
 - (vii) any other foreign country prescribed by the regulations;
and
 - (c) the entity is a resident of a country referred to in paragraph (b); and
 - (d) the entity is not a *general partner of a *VCLP.
- (6) The requirements that a partner must meet for the purposes of paragraph (1)(c) are that:
- (a) the partner must be a resident of:
 - (i) Canada; or
 - (ii) Finland; or
 - (iii) France; or
 - (iv) Germany; or
 - (v) Italy; or
 - (vi) Japan; or
 - (vii) the Netherlands (excluding the Netherlands Antilles); or
 - (viii) New Zealand; or
 - (ix) Norway; or
 - (x) Sweden; or
 - (xi) Taiwan; or
 - (xii) the United Kingdom; or
 - (xiii) the United States of America; or
 - (xiv) any other foreign country prescribed by the regulations;
and
 - (b) the partner must not be:
 - (i) a *general partner of a *VCLP; or
 - (ii) a *tax-exempt non-resident; or
 - (iii) a *foreign venture capital fund of funds.
- (7) A trust is not an eligible venture capital partner if an Australian resident:
- (a) is or is likely to become presently entitled, for the purposes of Division 6 of Part III of the *Income Tax Assessment Act 1936*, to; or

- (b) has or is likely to have an individual interest, for the purposes of Division 5 of Part III of the *Income Tax Assessment Act 1936*, in;
a share of income of the trust, either directly or indirectly through one or more interposed partnerships or trusts.

118-425 Meaning of *eligible venture capital investment*

Requirements for an eligible venture capital investment

- (1) An investment is an *eligible venture capital investment* if:
- (a) it is *at risk; and
 - (b) it is either:
 - (i) an acquisition of *shares in a company; or
 - (ii) an acquisition of options (including warrants) originally issued by a company to acquire shares in the company; and
 - (c) the company meets the requirements of subsections (2) to (7); and
 - (d) the sum of:
 - (i) the total amount that the partnership has invested in all the *equity interests and *debt interests that the partnership owns in the company; and
 - (ii) the total amount that the partnership has invested in all the equity interests and debt interests that the partnership owns in any entities that are *connected entities of the company;does not exceed 30% of the partnership's *committed capital.

Location within Australia

- (2) The company:
- (a) must, at the time the investment is made, be an Australian resident; and
 - (b) if at that time the entity making the investment does not own any other investments in the company—must meet the following requirements:
 - (i) more than 50% of the people who are currently engaged by the company to perform services must perform those services primarily in Australia;

(ii) more than 50% of its assets (determined by value) must be situated in Australia;

during the whole of the period of 12 months, or such shorter period as the *PDF Board determines under section 25-5 of the *Venture Capital Act 2002*, starting from the time the investment is made.

However, subparagraph (b)(i) or (ii) does not apply to the company if the PDF Board so determines under section 25-10 of the *Venture Capital Act 2002*.

See subsection (10) for the value of assets.

Primary activity

- (3) The company must not have as its primary activity any of the following:
- (a) property development or land ownership;
 - (b) finance, to the extent that it is any of the following:
 - (i) banking;
 - (ii) providing capital to others;
 - (iii) leasing;
 - (iv) factoring;
 - (v) securitisation;
 - (c) insurance;
 - (d) construction (including extension, improvement or up-grading) or acquisition of infrastructure facilities (within the meaning of section 93L of the *Development Allowance Authority Act 1992*) or related activities (within the meaning of section 93M of that Act), or both;
 - (e) making investments, whether made directly or indirectly, that are directed to deriving income in the nature of interest, rents, dividends, royalties or lease payments.

For the purposes of this subsection, activities that are ancillary or incidental to a particular activity are taken to form part of that activity.

Note: This requirement is ongoing. It is not limited to the circumstances at the time the investment was made.

Investment in other entities etc.

- (4) The company must not:
-

- (a) invest, in another entity, any part of the amount invested, unless the other entity:
 - (i) is *connected with the company; and
 - (ii) meets the requirements of subsections (3) to (7); or
- (b) in the capacity of a trustee, use any part of the amount invested.

However, this subsection does not prevent the company from depositing money with an *ADI, or with a body authorised by or under a law of a foreign country to carry on banking business in that country.

Note: This requirement is ongoing. It is not limited to the circumstances at the time the investment was made.

Registered auditor

- (5) The company must have as its auditor a person registered as a company auditor under a law in force in a State or a Territory.

Note: This requirement is ongoing. It is not limited to the circumstances at the time the investment was made.

Permitted entity value

- (6) The company must not, immediately before the investment is made, exceed the *permitted entity value.

Listing

- (7) The company must be a company whose *shares:
 - (a) are, at the time the investment is made, not listed for quotation in the official list of a stock exchange in Australia or a foreign country; or
 - (b) are so listed at that time, but cease to be so listed at any time during the 12 months after the investment is made.

Scrip for scrip investments

- (8) However, a company is taken to meet the requirements of subsections (2) to (7) if:
 - (a) the investment is an acquisition of *shares in that company in exchange for shares in another company; and
 - (b) at the time that the *VCLP, *AFOF or *eligible venture capital investor in question acquired the shares being

exchanged, the other company meets the requirements of subsections (2) to (7), but not only because this subsection applies to the other company; and

- (c) the shares in the other company that are being exchanged are all of the shares in the other company that the entity making the investment owned at the time of the exchange.

Debt interests

- (9) To avoid doubt, a *debt interest (including a *convertible note) cannot be an eligible venture capital investment.

The value of an asset

- (10) The value of an asset of an entity for the purposes of paragraph (2)(b) is the value of the asset as shown in:
 - (a) the last audited accounts prepared for the entity for the purposes of the *Corporations Act 2001* that relates to a period ending less than 18 months before that time; or
 - (b) if there are no such audited accounts—a statement, prepared in accordance with the *accounting standards and audited by the entity’s auditor, showing that value as at a time no longer than 12 months before that time.

118-430 Meaning of *at risk*

An *eligible venture capital investment is ***at risk*** if the entity that owns the investment had no *arrangement as to:

- (a) the maintenance of the value of the shares; or
- (b) the maintenance of any earnings or other return that might be made from owning the shares.

118-435 Special rule relating to investment in non-resident holding companies

- (1) A company that meets the requirements of subsections 118-425(6) and (7) is treated as also meeting the requirements of subsections 118-425(2), (3), (4) and (5) if:
 - (a) it is a resident of:
 - (i) Canada; or
 - (ii) France; or

- (iii) Germany; or
 - (iv) Japan; or
 - (v) the United Kingdom; or
 - (vi) the United States of America; or
 - (vii) any other foreign country prescribed by the regulations;
and
 - (b) it beneficially owns all the *shares in another company; and
 - (c) it does not carry on any *business other than to support the primary activity of the other company; and
 - (d) the other company meets the requirements of subsections 118-425(2) to (7).
- (2) However, if:
- (a) the company is so treated as meeting those requirements; and
 - (b) the other company ceases to be an Australian resident at any time within the period of 12 months after the day on which the first *eligible venture capital investment was made in the company;
- then:
- (c) any eligible venture capital investments already made in the company cease to be eligible venture capital investments; and
 - (d) any further investments made in the company are not eligible venture capital investments.

118-440 Meaning of *permitted entity value*

- (1) An entity exceeds the *permitted entity value* immediately before a proposed investment is made in the entity if, at that time, the sum of the following exceeds \$250 million:
 - (a) the total value of the entity's assets;
 - (b) the total value of the assets of any other entity *connected with the entity to the extent that they are not reflected in the value of any assets referred to in paragraph (a).
- (2) The total value of the assets of an entity is the total value of its assets (both current and non-current) as shown in:
 - (a) the last audited accounts prepared for the entity for the purposes of the *Corporations Act 2001* that relates to a period ending less than 18 months before that time; or

- (b) if there are no such audited accounts—a statement, prepared in accordance with the *accounting standards and audited by the entity’s auditor, showing that value as at a time no longer than 12 months before that time.

118-445 Meaning of *committed capital*

- (1) A partner’s *committed capital* in a partnership is the sum of the amounts that the partner may, under the partnership agreement establishing the partnership, become obliged to contribute to the partnership.
- (2) It does not matter whether:
- (a) the partner contributes all of those amounts; or
 - (b) any amounts contributed are subsequently returned to the partner; or
 - (c) the contributions give rise to *equity interests or *debt interests in the partnership, or both.
- (3) A partnership’s *committed capital* is the sum of the committed capital of all of the partnership’s partners.

7 Subdivision 118-G (heading)

Repeal the heading, substitute:

Subdivision 118-G—Venture capital: investment by foreign superannuation funds

8 Subsection 995-1(1)

Insert:

AFOF means an *Australian venture capital fund of funds.

9 Subsection 995-1(1)

Insert:

at risk has the meaning given by section 118-430.

10 Subsection 995-1(1)

Insert:

Australian venture capital fund of funds has the meaning given by subsection 118-410(3).

11 Subsection 995-1(1)

Insert:

committed capital of a partnership has the meaning given by section 118-445.

12 Subsection 995-1(1)

Insert:

eligible venture capital investment has the meaning given by section 118-425.

Note: This meaning is also affected by subsection 118-435(2).

13 Subsection 995-1(1)

Insert:

eligible venture capital investor has the meaning given by subsection 118-415(2).

14 Subsection 995-1(1)

Insert:

eligible venture capital partner has the meaning given by section 118-420.

15 Subsection 995-1(1)

Insert:

foreign venture capital fund of funds has the meaning given by subsections 118-420(4) and (5).

16 Subsection 995-1(1) (definition of *general partner*)

Omit “*corporate limited partnership”, substitute “*limited partnership”.

17 Subsection 995-1(1)

Insert:

investment registration requirement:

- (a) in relation to a *VCLP—has the meaning given by subsection 9-1(2) of the *Venture Capital Act 2002*; and
- (b) in relation to an *AFOF—has the meaning given by subsection 9-5(2) of the *Venture Capital Act 2002*.

18 Subsection 995-1(1)

Insert:

limited partner means a partner of a *limited partnership whose liability in relation to the partnership is limited.

19 Subsection 995-1(1)

Insert:

PDF Board means the PDF Registration Board established under section 5 of the *Pooled Development Funds Act 1992*.

20 Subsection 995-1(1)

Insert:

permitted entity value has the meaning given by section 118-440.

21 Subsection 995-1(1)

Insert:

registration requirements of an AFOF has the meaning given by subsection 9-5(1) of the *Venture Capital Act 2002*.

22 Subsection 995-1(1)

Insert:

registration requirements of a VCLP has the meaning given by subsection 9-1(1) of the *Venture Capital Act 2002*.

23 Subsection 995-1(1)

Insert:

tax-exempt non-resident has the meaning given by subsection 118-420(3).

24 Subsection 995-1(1)

Insert:

unconditionally registered: a *VCLP or *AFOF is unconditionally registered if its registration under the *Venture Capital Act 2002* is not based, or is no longer based, on its conditional registration under section 13-5 of that Act.

25 Subsection 995-1(1)

Insert:

VCLP means a *venture capital limited partnership.

26 Subsection 995-1(1)

Insert:

venture capital limited partnership has the meaning given by subsection 118-405(2).

27 Application

The amendments made by this Schedule apply, and are taken to have applied, to CGT events relating to investments made on or after 1 July 2002.

Schedule 2—“Flow-through” treatment, and related matters

Income Tax Assessment Act 1936

1 Subsection 6(1)

Insert:

AFOF means an Australian venture capital fund of funds within the meaning of subsection 118-410(3) of the *Income Tax Assessment Act 1997*.

2 Subsection 6(1)

Insert:

general partner means a partner of a limited partnership whose liability in relation to the partnership is not limited.

3 Subsection 6(1)

Insert:

limited partner means a partner of a limited partnership whose liability in relation to the partnership is limited.

4 Subsection 6(1)

Insert:

limited partnership means a partnership where the liability of at least one of the partners is limited.

5 Subsection 6(1)

Insert:

VCLP means a venture capital limited partnership within the meaning of subsection 118-405(2) of the *Income Tax Assessment Act 1997*.

6 Subsection 6(1)

Insert:

VCMP means a venture capital management partnership.

7 Subsection 6(1)

Insert:

venture capital management partnership has the meaning given by subsection 94D(3).

8 Subsection 6(1) (paragraph (b) of the definition of year of income)

Repeal the paragraph, substitute:

- (b) in relation to any other person:
 - (i) the financial year for which income tax is levied; or
 - (ii) if an accounting period is adopted under this Act in lieu of that financial year and subparagraph (iii) does not apply—that accounting period; or
 - (iii) an accounting period that commences or ends under section 18A, if that accounting period would (but for that section) have formed part of the financial year referred to in subparagraph (i) or the accounting period referred to in subparagraph (ii).

9 Subsection 6(2)

Omit “a reference to that accounting period”, substitute:

a reference to:

- (a) the adopted accounting period; or
- (b) if the adopted accounting period ends under section 18A:
 - (i) in relation to the commencing of the year of income—the adopted accounting period (as ending under that section); or
 - (ii) in relation to the ending of the year of income—the accounting period ending under that section on the day on which the adopted accounting period would (but for that section) have ended.

10 After subsection 6(2)

Insert:

- (2AA) A reference in this Act (other than subsection (2) of this section) to an accounting period adopted in lieu of a year of income includes a reference to an accounting period:
- (a) that commences or ends under section 18A; and
 - (b) that would, but for that section, form part of an accounting period so adopted.
- (2AB) The Commissioner may make a determination modifying the operation of one or more provisions of this Act in relation to limited partnerships whose accounting periods commence or end under section 18A of the *Income Tax Assessment Act 1936*.
- (2AC) A determination can only be made under subsection (2AB) in order to take account of the fact that such accounting periods are of less than 12 months’ duration.
- (2AD) A determination under subsection (2AB) is a disallowable instrument for the purposes of section 46A of the *Acts Interpretation Act 1901*.

11 Subsection 18(1)

Omit “unless with the leave of the Commissioner some other date is adopted”, substitute:

unless:

- (a) with the leave of the Commissioner some other date is adopted; or
- (b) the accounting period ends earlier under section 18A.

12 After section 18

Insert:

18A Accounting periods for VCLPs, AFOFs and VCMPs

- (1) If a partnership becomes, or ceases to be, a VCLP, an AFOF or a VCMP on a particular day:
 - (a) the accounting period during which that day occurs (the *first accounting period*) is taken to have ended immediately before that day; and
 - (b) another accounting period is taken to have commenced at the beginning of that day.

The other accounting period ends on the day on which the first accounting period would have ended if this section did not apply.

Example: A partnership whose accounting periods ended on 30 June becomes a VCLP on 1 October 2002, and ceases to be a VCLP on 1 April 2003.

The effect of becoming a VCLP: the accounting period that commenced on 1 July 2002 is taken under this section to end on 30 September 2002, and a second accounting period commences on 1 October 2002. The second accounting period is scheduled to end on 30 June 2003.

The effect of ceasing to be a VCLP: the second accounting period is now taken under this section to end on 31 March 2003, and a third accounting period commences on 1 April 2003. The third accounting period is to end on 30 June 2003.

- (2) This section does not apply in relation to a partnership becoming, or ceasing to be, a VCLP, an AFOF or a VCMP on the day on which an accounting period commences.

13 After subsection 92(2)

Insert:

(2AA) However, if:

- (a) the partner is a limited partner in a partnership; and
- (b) the partnership is a VCLP, an AFOF or a VCMP during the year of income;

the amount allowable under subsection (2), in respect of the year of income, as a deduction must not exceed the amount worked out as follows:

Method statement

Step 1. Work out the sum of the amounts that the partner has contributed (the *partner’s contribution*) to the partnership.

Step 2. Subtract the sum of all the amounts (if any) of the partner’s contribution that are repaid to the partner.

Step 3. Subtract the sum of all deductions allowed to the partner for losses of the partnership in previous years of income.

Step 4. Subtract the sum of the amounts of all the debt interests issued by the partner to the extent that they are secured by the partner’s interest in the partnership.

Example: A limited partner contributes \$100,000 to a VCLP, having borrowed \$80,000. Because the lender values the partner’s interest in the partnership at \$70,000, the partner also provides, as additional security, other assets valued at \$10,000.

If none of the partner’s contribution has been repaid and the partner has not been allowed deductions for partnership losses in previous years of income, the amount allowable to the partner for a partnership loss cannot exceed \$30,000.

14 After section 92

Insert:

92A Deductions in respect of outstanding subsection 92(2AA) amounts

- (1) If:
- (a) the partner is a limited partner in a partnership; and
 - (b) the partnership is a VCLP, an AFOF or a VCMP during the year of income; and
 - (c) the amount allowable under subsection 92(2) as a deduction to the partner for partnership losses incurred by the partnership in the year of income is not reduced because of subsection 92(2AA); and
 - (d) the partner has an outstanding subsection 92(2AA) amount for the year of income;

there is allowable as a deduction to the partnership an amount worked out as follows:

Method statement

Step 1. Subtract the amount allowable under subsection 92(2) as a deduction to the partner for partnership losses incurred by the partnership in the year of income from the amount worked out using the method statement in subsection 92(2AA).

Step 2. If the amount worked out under step 1 is greater than or equal to the outstanding subsection 92(2AA) amount for the year of income, the amount of the deduction allowable under this section is the outstanding subsection 92(2AA) amount.

Step 3. If the amount worked out under step 1 is less than the outstanding subsection 92(2AA) amount for the year of income, the amount of the deduction allowable under this section is the amount worked out under step 1.

- (2) The partner has an outstanding subsection 92(2AA) amount for a year of income if:
- (a) an amount allowable under subsection 92(2) as a deduction to the partner for partnership losses incurred by the partnership in a previous year of income was reduced because of subsection 92(2AA); and
 - (b) the difference between:
 - (i) the sum of all reductions made under subsection 92(2AA) to amounts allowable under subsection 92(2) as deductions to the partner for partnership losses incurred by the partnership in previous years of income; and
 - (ii) the sum of all amounts allowable under this section, in respect of previous years of income, as deductions to the partner in relation to those reductions;is greater than zero.
- The amount of that difference is the partner’s ***outstanding subsection 92(2AA) amount*** for the year of income.
- (3) To avoid doubt, a partner’s outstanding subsection 92(2AA) amount for a year of income cannot form part of a tax loss for the purposes of Division 36 of the *Income Tax Assessment Act 1997*.

15 Section 94B (definition of *limited partnership*)

Repeal the definition.

16 At the end of section 94D

Add:

- (2) However, a partnership that is a VCLP, an AFOF or a venture capital management partnership cannot be a corporate limited partnership.

Note 1: This subsection can apply without the partnership meeting the applicable registration requirements under the *Venture Capital Act 2002*. It must be registered under that Act in order to be a VCLP or an AFOF, but it is possible for it to remain registered while the requirements are not met.

Note 2: VCLPs, AFOFs and VCMPs are taxed as ordinary partnerships under Division 5.

Note 3: If the partnership’s registration as a VCLP or AFOF is unconditional, some partners’ share in capital gains and losses from CGT events relating to some investments may be disregarded: see Subdivision 118-F of the *Income Tax Assessment Act 1997*.

- (3) A **venture capital management partnership** is a limited partnership that:

(a) is a general partner of either or both of the following:

- (i) one or more VCLPs;
- (ii) one or more AFOFs; and

(b) only carries on activities that are related to being such a general partner.

A limited partnership ceases to be a venture capital management partnership if it ceases to meet the requirements of paragraphs (a) and (b).

Note: In this Act, the term “venture capital management partnership” is usually abbreviated to “VCMP”.

17 Paragraph 160APH(1)(a)

After “different accounting period”, insert “, or has an accounting period that commences or ends under section 18A”.

Income Tax Assessment Act 1997

18 Paragraph 4-10(2)(b)

Repeal the paragraph, substitute:

- (b) if you have an accounting period that is not the same as the financial year, each such accounting period or, for a company, each previous accounting period is an income year.

19 Subsection 4-10(2) (note)

Repeal the note, substitute:

- Note 1: The Commissioner can allow you to adopt an accounting period ending on a day other than 30 June. See section 18 of the *Income Tax Assessment Act 1936*.
- Note 2: An accounting period ends, and a new accounting period starts, when a partnership becomes, or ceases to be, a VCLP, an AFOF or a VCMP. See section 18A of the *Income Tax Assessment Act 1936*.

20 Paragraph 9-5(2)(b)

Repeal the paragraph, substitute:

- (b) if an entity has an accounting period that is not the same as the financial year, each such accounting period or, for a company, each previous accounting period is an income year.

21 Subsection 9-5(2) (note)

Repeal the note, substitute:

- Note 1: The Commissioner can allow an entity to adopt an accounting period ending on a day other than 30 June. See section 18 of the *Income Tax Assessment Act 1936*.
- Note 2: An accounting period ends, and a new accounting period starts, when a partnership becomes, or ceases to be, a VCLP, an AFOF or a VCMP. See section 18A of the *Income Tax Assessment Act 1936*.

22 Section 36-25 (after the table headed “Tax losses of pooled development funds (PDFs)”)

Insert:

Tax losses of VCLPs, AFOFs and VCMPs

Item	For the special rules about this situation...	See:
1.	A limited partnership that has a tax loss becomes a VCLP, an AFOF or a VCMP: it cannot deduct the loss while it is a VCLP, an AFOF or a VCMP.	Subdivision 195-B

23 At the end of Division 195

Add:

Subdivision 195-B—Limited partnerships

Guide to Subdivision 195-B

195-60 What this Subdivision is about

This Subdivision contains rules about the income tax treatment of limited partnerships that become, or cease to be, venture capital limited partnerships, Australian venture capital funds of funds or venture capital management partnerships.

It also allows the Commissioner to determine how to take account of limited partnerships having income years of less than 12 months when they become, or cease to be, venture capital limited partnerships, Australian venture capital funds of funds or venture capital management partnerships.

Table of sections

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[This is the end of the Guide.]

Operative provisions

195-65 Tax losses cannot be transferred to a VCLP, an AFOF or a VCMP

A *limited partnership's *tax loss for a *loss year cannot be deducted in a later income year during which the partnership is a *VCLP, an *AFOF or a *VCMP.

195-70 Previous tax losses can be deducted after ceasing to be a VCLP, an AFOF or a VCMP

This Subdivision does not prevent a *limited partnership that has ceased to be a *VCLP, an *AFOF or a *VCMP from deducting, in an income year, a *tax loss for a *loss year that occurred before the partnership was a VCLP, AFOF or VCMP.

195-75 Determinations to take account of income years of less than 12 months

- (1) The Commissioner may make a determination modifying the operation of one or more provisions of this Act in relation to limited partnerships whose accounting periods commence or end under section 18A of the *Income Tax Assessment Act 1936*.
- (2) A determination can only be made in order to take account of the fact that such accounting periods are of less than 12 months’ duration.
- (3) A determination under this section is a disallowable instrument for the purposes of section 46A of the *Acts Interpretation Act 1901*.

24 Subsection 995-1(1) (definition of *income year*)

Omit “includes that accounting period”, substitute:

includes:

- (a) the adopted accounting period; or
- (b) if the adopted accounting period ends under section 18A of the *Income Tax Assessment Act 1936*:
 - (i) in relation to the commencing of the income year—the adopted accounting period (as ending under that section); or
 - (ii) in relation to the ending of the income year—the accounting period ending under that section on the day on which the adopted accounting period would (but for that section) have ended.

25 Subsection 995-1(1) (note at the end of the definition of *income year*)

Repeal the note, substitute:

Note 1: The Commissioner can allow you to adopt an accounting period ending on a day other than 30 June. See section 18 of the *Income Tax Assessment Act 1936*.

Note 2: An accounting period ends, and a new accounting period starts, when a partnership becomes, or ceases to be, a VCLP, an AFOF or a VCMP. See section 18A of the *Income Tax Assessment Act 1936*.

26 Subsection 995-1(1) (definition of *limited partnership*)

Omit “section 94B”, substitute “subsection 6(1)”.

27 Subsection 995-1(1)

Insert:

VCMP means a venture capital management partnership within the meaning of subsection 94D(3) of the *Income Tax Assessment Act 1936*.

28 Application

The amendments made by this Schedule apply, and are taken to have applied, to the 2002-2003 income year and later income years.

Schedule 3—Capital gains tax treatment of “carried interests”

Fringe Benefits Tax Assessment Act 1986

1 Subsection 136(1) (after paragraph (m) of the definition of fringe benefit)

Insert:

- (ma) a payment, within the meaning of subsection 104-255(7) of the *Income Tax Assessment Act 1997*, of a carried interest of a kind referred to in subsection 104-255(1) of that Act; or
- (mb) a grant or acquisition of such a carried interest, or of an entitlement to such a payment; or

Income Tax Assessment Act 1997

2 Section 10-5 (after table item headed “car expenses”)

Insert:

carried interests

carried interests, not ordinary income 118-21

3 Section 12-5 (after table item headed “car expenses of employee”)

Insert:

carried interests

carried interests, no deduction for 118-21

4 Section 104-5 (after table row relating to event number K8)

Insert:

K9 Entitlement to receive payment of a carried interest	when you become entitled to receive payment	capital proceeds from entitlement	<i>no capital loss</i>
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[See section 104-255]

5 At the end of Subdivision 104-K

Add:

104-255 Carried interests: CGT event K9

- (1) **CGT event K9** happens if you become entitled to receive a payment of a *carried interest of a *general partner in a *VCLP or an *AFOF or a *limited partner in a *VCMP.
- (2) The time of the event is the time you become entitled to receive the payment.
- (3) You make a **capital gain** equal to the *capital proceeds from the *CGT event.

Note: You cannot make a capital loss.

Meaning of carried interest

- (4) The **carried interest** of a *general partner in a *VCLP or an *AFOF is the partner’s entitlement to a distribution from the VCLP or AFOF, to the extent that the distribution is contingent upon the attainment of profits for the *limited partners in the VCLP or AFOF.
- (5) The **carried interest** of a *limited partner in a *VCMP is the partner’s entitlement to a distribution from the VCMP, to the extent that the distribution is contingent upon the attainment of profits for the *limited partners in the VCLP or AFOF in which the VCMP is a *general partner.
- (6) The *carried interest does not include:
 - (a) any part of the partner’s entitlement to that distribution that is attributable to a fee (by whatever name called) for the management of the *VCLP, *AFOF or *VCMP; or
 - (b) any part of the partner’s entitlement to that distribution that is attributable to the partner’s *equity interest in the VCLP, AFOF or VCMP.

Meaning of payment of carried interest

- (7) **Payment**, of a *carried interest, includes:
 - (a) a payment that is attributable to the carried interest; or
 - (b) the giving of property in satisfaction of the carried interest: see section 103-5; or

(c) the giving of property in satisfaction of an entitlement that is attributable to the carried interest: see section 103-5.

6 Section 110-10 (after table row relating to event number K7)

Insert:

K9	Carried interests	104-255
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7 At the end of section 115-20

Add:

(3) This section does not apply to a *capital gain worked out under subsection 104-255(3) (about carried interests).

8 After subsection 115-25(2)

Insert:

(2A) If the *capital gain results from a *CGT event K9 happening:

- (a) subsection (1) does not apply; and
- (b) to be a *discount capital gain, the *carried interest to which the CGT event relates must arise under a partnership agreement entered into at least 12 months before the CGT event.

9 Subsection 116-20(2)

Omit “and H2”, substitute “, H2 and K9”.

10 Subsection 116-20(2) (after table row relating to event number H2)

Insert:

K9	Entitlement to receive payment of a *carried interest	The amount of the payment, to the extent that it is a payment of the *carried interest
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11 Section 116-25 (at the end of the table)

Add:

K9	Entitlement to receive payment of a *carried interest	2, 3, 4	None
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12 At the end of section 116-30

Add:

Carried interests

- (5) This section does not apply to *CGT event A1 or C2 to the extent that the CGT event is constituted by ceasing to own:
- (a) the *carried interest of a *general partner in a *VCLP or an *AFOF or a *limited partner in a *VCMP; or
 - (b) an entitlement to receive a payment of such a carried interest.

13 After section 118-20

Insert:

118-21 Carried interests

CGT events relating to carried interests not to be treated as income

- (1) The modifications in subsections (2) and (3) apply if *CGT event K9 happens in relation to your entitlement to receive a payment of the *carried interest of a *general partner in a *VCLP or an *AFOF or a *limited partner in a *VCMP.
- (2) These provisions do not apply to the CGT event:
- (a) sections 6-5 (about *ordinary income), 8-1 (about amounts you can deduct), 15-15 and 25-40 (about profit-making undertakings or plans) and 118-20 (reducing capital gains if amount otherwise assessable);
 - (b) sections 25A and 52 of the *Income Tax Assessment Act 1936* (about profit-making undertakings or schemes).
- (3) Section 6-10 (about *statutory income) does not apply to the *CGT event except so far as that section applies in relation to section 102-5 (about net capital gains).

14 Section 136-15 (heading)

Repeal the heading, substitute:

136-15 Making a capital gain or loss from CGT events D1, E9 and K9

15 At the end of section 136-15

Add:

- (3) You make a *capital gain from *CGT event K9 (about carried interests) only if one of the items in this table is satisfied.

CGT event K9		
Item	In this situation:	This requirement is satisfied:
1	The *capital proceeds from the event would have been your *ordinary income if section 118-21 did not apply	The proceeds are *derived from an *Australian source
2	The *capital proceeds from the event would <i>not</i> have been your *ordinary income even if section 118-21 did not apply	If the proceeds <i>were</i> your *ordinary income, they <i>would</i> have been *derived from an *Australian source

16 Subsection 995-1(1)

Insert:

carried interest:

- (a) of a *general partner in a *VCLP or an *AFOF—has the meaning given by subsections 104-255(4) and (6); and
- (b) of a *limited partner in a *VCMP—has the meaning given by subsections 104-255(5) and (6).

17 Subsection 995-1(1)

Insert:

payment, of a *carried interest, includes the meanings given in subsection 104-255(7).

18 Application

The amendments made by this Schedule apply, and are taken to have applied, to the 2002-2003 income year and later income years.

Schedule 4—Consequential amendments relating to the Venture Capital Act 2002

Income Tax Assessment Act 1997

1 Subsection 995(1)

Insert:

form approved by the PDF Board has the same meaning as in section 33-5 of the *Venture Capital Act 2002*.

2 Subsection 995-1(1)

Insert:

permitted loan has the same meaning as in section 9-10 of the *Venture Capital Act 2002*.

Pooled Development Funds Act 1992

3 Subsection 4(1)

Insert:

AFOF means an Australian venture capital fund of funds within the meaning of subsection 118-410(3) of the *Income Tax Assessment Act 1997*.

4 Subsection 4(1)

Insert:

limited partnership has the same meaning as in the *Income Tax Assessment Act 1997*.

5 Subsection 4(1)

Insert:

VCLP means a venture capital limited partnership within the meaning of subsection 118-405(2) of the *Income Tax Assessment Act 1997*.

6 At the end of section 6

Add:

- (3) The Board also has the functions of:
- (a) registering limited partnerships as VCLPs or AFOFs under Part 2 of the *Venture Capital Act 2002*; and
 - (b) registering entities as eligible venture capital investors under Part 3 of that Act; and
 - (c) making determinations under Part 4 of that Act; and
 - (d) giving information it obtains under those Parts to the Commissioner of Taxation for the purposes of implementing and administering the taxation law (within the meaning of the *Taxation Administration Act 1953*).

7 Paragraph 71(1)(d)

After “Act”, insert “or the *Venture Capital Act 2002*”.

8 Subsection 71(5) (at the end of the definition of *tax law*)

Add “and includes the *Venture Capital Act 2002*”.

9 At the end of subsection 72(1)

Add:

- ; and (c) the Board’s powers to register limited partnerships as VCLPs or AFOFs or revoke registration under Part 2 of the *Venture Capital Act 2002*; and
- (d) the Board’s powers to register entities as eligible venture capital investors or revoke registration under Part 3 of the *Venture Capital Act 2002*; and
- (e) the Board’s powers to make determinations under Part 4 of the *Venture Capital Act 2002*.

10 At the end of subsection 73(1)

Add:

- ; and (c) the Board’s powers to register limited partnerships as VCLPs or AFOFs or revoke registration under Part 2 of the *Venture Capital Act 2002*; and
- (d) the Board’s powers to register entities as eligible venture capital investors or revoke registration under Part 3 of the *Venture Capital Act 2002*; and

- (e) the Board's powers to make determinations under Part 4 of the *Venture Capital Act 2002*.

11 At the end of subsection 74(2)

Add:

- ; or (c) registering limited partnerships as VCLPs or AFOFs or revoking registration under Part 2 of the *Venture Capital Act 2002*; or
- (d) registering entities as eligible venture capital investors or revoking registration under Part 3 of the *Venture Capital Act 2002*; or
- (e) making determinations under Part 4 of the *Venture Capital Act 2002*.

[Minister's second reading speech made in—
House of Representatives on 14 November 2002
Senate on 9 December 2002]

(242/02)