AUSTRALIAN INVESTMENT COUNCIL

17 April 2020

Senator Andrew Bragg
Chair
Select Committee on Financial Technology and Regulatory Technology
Po Box 6100
Parliament House
Canberra ACT 2600

Email: fintech.sen@aph.gov.au

Dear Senator Bragg,

Senate Select Committee Inquiry into Financial Technology and Regulatory Technology

The Australian Investment Council welcomes the opportunity to provide further input to the Senate Select Committee's Inquiry on Financial Technology and Regulatory Technology on the short, medium and long-term solutions for government to deliver to the FinTech and RegTech sectors during, and post the COVID-19 pandemic.

In the current environment, venture capital **(VC)** firms are closely engaging with their portfolio companies as they assess the impact of the economic downturn and the future viability of their investments. Unfortunately, some innovative and worthwhile companies that will be important for Australia's economic growth in the post COVID-19 era, will not survive. This has occurred at a time when an increasing number of FinTech and RegTech firms are reaching out to VC funds for assistance.

There is evidence, however, that VC funds are starting to have the capacity to consider new deals and new projects. In assessing which entrepreneurs and businesses to partner with, it is likely that VC funds will continue to be cautious with deploying their dry powder for some time to come. This is due to ongoing uncertainties in the funding environment, exacerbated by changes to the foreign investment regime, and uncertainties regarding government assistance, for example regarding the JobKeeper program.

The points below outline initiatives for the government to consider to help the FinTech and RegTech sectors navigate unexpected changes during the current environment and to support growth in the sectors after the pandemic comes to an end.

JobKeeper payments

The Australian Investment Council commends the government's JobKeeper payments as a short-term solution to help FinTech and RegTech start-ups survive over the next few months. While the policy is welcomed by the startup sector, a number of businesses will not meet the eligibility criteria. This particularly applies to the fast-growing businesses that have been hit hard by the economic slowdown. While companies in this category may have doubled or tripled revenue in the year since March 2019, they may have also taken a significant drop in revenue compared to the previous year, but not at the rate of 30 per cent or more that is required to access the JobKeeper arrangement.

It is these fast growth companies that will be critical in providing employment opportunities when the downturn comes to an end. We are able to provide further information regarding these issues if it is of assistance to the Committee.

Recommendation 1
Ensure fast-growth venture capital-backed Australian businesses can access the JobKeeper Program
The Australian Investment Council recommends the eligibility criteria for the JobKeeper Program be amended to consider "fast growth" companies to ensure venture capital-backed Australian businesses are not disadvantaged.

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The UK Approach
The UK government is considering a package of financial support for start-up companies as many are not eligible for the new government-backed loan scheme as they are in the loss-making, early stage of development. One approach being considered by UK Treasury is co-investment where the government would offer convertible loans which could either be repaid by the business after the crisis, or turned into equity owned by the government. This could be in the form of co-investment where VC firms match the funding provided by the government.

Recommendation 2
Introduce co-investment funding for early stage FinTech and RegTech start-ups
The Australian Investment Council recommends the government introduces co-investment measures to assist early stage FinTech and RegTech companies with funding during the crisis period.

Research and Development
A supportive R&D regime is increasingly important in a downturn or in times of heightened uncertainty, when markets and investors typically become increasingly risk adverse, and investment in innovation typically reduces.[1] OECD research has found that during such times, "firms face difficulties in tapping into external sources of funding to support their investments in R&D" and that R&D investment is "reoriented towards short-term, low-risk innovations, while longer term, high risk innovation projects are… cut first.[1, 2]

On 5 December 2019, the Research and Development Tax Incentive Bill was tabled in parliament. While it marked an important step forward in providing certainty to businesses about the future direction of Australia's R&D tax incentive, certain definitions used in the legislation are likely to continue to create uncertainty on the eligibility criteria for R&D tax incentives. This Bill is yet to be passed and uncertainty continues. We are able to provide further information regarding these issues if it is of assistance to the Committee.

Introducing changes that disincentivise Australia's R&D investment at this point in the economic cycle would, in our opinion, be harmful to the Australian economy. Given the current economic conditions and challenges, we should be incentivising Australian SMEs to expand their investment in R&D, which will lead directly to our nation's future productivity and employment growth.

We also note that other nations in our region have more supportive programs, such as New Zealand and Singapore.[3] Rather than creating uncertainty or inhibiting innovation, we should be leveraging our R&D regime to support Australian businesses and to position Australia as a stable and attractive destination for offshore investors in the period ahead.

Recommendation 3
Clarify definitions in R&D legislation
The Australian Investment Council recommends the government address recent uncertainty around the future settings of the R&D program. Steps should be taken to broaden the definition of "experiments" to encompass businesses that innovate on top of existing infrastructure and to provide clarity on which R&D claims are eligible to avoid potential disputes with the ATO.

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[1] Guellec, D. and S. Wunsch-Vincent (2009), Policy Responses to the Economic Crisis: Investing in Innovation for Long-Term Growth, OECD Digital Economy Papers, No. 159, OECD

[2] *ibid.*

[3] We are able to provide further information regarding offshore regimes if this would be useful to the Committee.

In recognition that start-up businesses are essential for innovation, employment and productivity growth, the UK government is also considering tax credits for venture capital companies. This recognises the importance of R&D investment in fuelling a recovery. Unless specific support is implemented in Australia, there is a risk our national recovery will be hampered unnecessarily by a reduction in R&D activity.

Recommendation 4
Introduce R&D incentives for FinTech and RegTech companies
The Australian Investment Council recommends the government considers incentives, such as tax credits, for FinTech and RegTech companies to invest in R&D during the crisis period.

Continued access to finance
While some FinTech and RegTech companies may be sustainable in the short term, potentially, the real impact of COVID-19 on the viability of businesses may not be seen until the second or third quarter of FY2021. By that stage, many businesses may no longer exist and it is likely that funding, such as that provided for SMEs by the COVID-19 SME guarantee scheme, will not be as readily available as it is today, or available at all. It is therefore critical that government considers funding options to assist the industry in the longer term.

Recommendation 5
Funding options for the longer term
The Australian Investment Council recommends the government explores options for providing funding assistance that extends beyond the COVID-19 SME guarantee scheme to sustain FinTech and RegTech companies through and post the pandemic.

If you have any questions about the recommendations or any specific points outlined in this letter, please do not hesitate to contact me or Brendon Harper, the Australian Investment Council's Head of Policy and Research,

Yours sincerely,

Yasser El-Ansary
Chief Executive