Partnership Amendment (Venture Capital Funds) Bill.

Second Reading

Mr NEVILLE NEWELL (Tweed—Parliamentary Secretary) [10.03 a.m.], on behalf of Mr Bob Debus: I move:

That this bill be now read a second time.

The Government is pleased to introduce the Partnership Amendment (Venture Capital Funds) Bill. This bill amends the Partnership Act 1892 to allow for a new form of corporate entity, the Incorporated Limited Partnership, for use as a structure for venture capital investment funds. This will align New South Wales with the dominant position structure internationally in respect of venture capital investment funds. Research conducted by the Australian Venture Capital Association Limited indicates that New South Wales will financially benefit from these reforms. Introducing this structure to complement the Commonwealth's recent venture capital tax reforms, it is anticipated that more than $1 billion will be invested in Australian growth companies, $350 million will be added to Australian gross domestic product and $120 million will be added to net exports each year.

Through incorporated limited partnerships, New South Wales will be able to more readily attract both domestic and foreign capital for investment in New South Wales growth companies. Venture capital is an important source of funds for start-up companies, expanding businesses and restructuring businesses. By its nature, venture capital investment is high risk as it provides funding to companies at difficult stages in their development and, consequently, at stages where there is the greatest risk of failure. The venture capital process attempts to prevent this failure by working with the management of investee companies through the growth phase. This applies in key areas of economic activity that often require years of research and development before investors may see returns. Medical technology and biotechnology are two such activities. In fact, the joint New South Wales, Queensland and Victorian "Australian Biotechnology Alliance" project is likely to benefit from an enhanced venture capital investment regime.

The introduction of the incorporated limited partnership is intended to complement the recent Commonwealth venture capital tax legislation. The Commonwealth legislation is designed to align the Australian tax regime applicable to venture capital investment structures with that of most other developed countries. The Commonwealth's tax reforms apply in respect of three forms of limited partnership: venture capital limited partnerships, which are limited partnerships investing directly in companies; Australian funds of funds, which diversify investment risk by investing across a range of venture capital limited partnerships; and venture capital management partnerships, which, under the Income Tax Assessment Act 1936, can only be involved in the management of these other bodies.

Since 1992, limited partnerships have been taxed as if they were companies. The Commonwealth Taxation Laws Amendment (Venture Capital) Act 2002 entitles limited partnerships registered as venture capital limited partnerships or Australian funds of funds to flow through taxation treatment. That is, partners in these types of limited partnerships are taxed on their share of the income, profits, gains and losses of the partnership, according to the partner's tax status. Under the Commonwealth's Venture Capital Act 2002 the Commonwealth is responsible for the registration and reporting process of venture capital limited partnerships and Australian funds of funds.

Registration requires the partnership to be in existence for more than five years and have capital commitments of more than $20 million. The Commonwealth registration requirements, and allowing the formation of incorporated limited partnerships, will help ensure that New South Wales gets long-term economic investment in innovative companies. Although limited partnership structures exist in Australia, they do not presently provide venture capital investors with the certainty required in respect of liability protection. This bill amends the Partnership Act to allow formation of a new type of partnership, the incorporated limited partnership, which addresses the issue of liability and provides a structure that is internationally preferred for venture capital investment.

Currently, a partnership in New South Wales is not a separate legal entity from its partners. Principles associated with these partnerships, such as joint and several liability, mutual agency and beneficial ownership of partnership assets, do not readily apply to a partnership that is a separate legal entity. To overcome this, proposed section 1C of the bill states the general law of partnership does not apply to incorporated limited partnerships, except as provided by the Act. An incorporated limited partnership will be a separate legal entity and for the purposes of the Corporations Act 2001, a body corporate. Therefore, in most cases, the firm will be subject to those provisions of the Corporations Act relating to bodies corporate, such as directors' duties and the prohibition on disqualified persons being involved in management.

Under proposed section 51, an incorporated limited partnership must have at least one general partner but not more than 20, and at least one limited partner. The general partners are responsible for the management of the partnership, while limited partners are investors. Rights and duties between the partners must be set out in a partnership agreement in accordance with proposed section 53B. This agreement has effect as a contract between the incorporated limited partnership and the partners. Under proposed section 53C, an agency relationship exists between the general partners

and between each general partner and the incorporated limited partnership. However, no agency relationship exists between a limited partner and either the general partners or the incorporated limited partnership.

An incorporated limited partnership is formed when registered with the Registrar for Incorporated Limited Partnerships, who is currently the Director-General of the Department of Commerce. In addition, an incorporated limited partnership wishing to qualify as either a venture capital limited partnership or an Australian fund of funds will need to register with the Commonwealth's Pooled Development Fund Board. This board ensures that the firm meets the Commonwealth's requirements for these two forms of venture capital fund.

An application to form an incorporated limited partnership may be made by a partnership, or by the natural persons, corporations, and other partnerships that are to be partners in the firm. The incorporated limited partnership must register as, or satisfy the requirements applicable to, one of the three authorised venture capital bodies. To avoid any doubt, the bill extends the limited liability status to limited partnerships enacted under similar legislation in another jurisdiction by virtue of proposed section 66D. Where a statute in another jurisdiction is not similar to this bill, it can, for the avoidance of doubt, be proscribed in regulations to ensure recognition of those partnerships in New South Wales. A reciprocal relationship exists under section 66C, which explicitly allows New South Wales registered incorporated limited partnerships to operate in other jurisdictions while maintaining their incorporation and limited liability status.

A limited partner in an incorporated limited partnership has a limitation on their liability under proposed section 66A. Under this section, a limited partner has no liability for the liabilities of the incorporated limited partnership or of the general partners. This does not affect a limited partner's obligation to contribute capital or property to the firm. The bill sets out that the firm is primarily liable for the debts of the partnership, but that the general partners are personally liable to the extent that the firm cannot satisfy the debt.

The limitation on liability is balanced by a prohibition on limited partners taking part in the management of the incorporated limited partnership. However, certain 'safe harbour' provisions are prescribed in section 67A within which a limited partner is able to participate in the management of the incorporated limited partnership. These provisions essentially allow a limited partner to oversee their investment, assist the growth of the enterprise and ensure that the incorporated limited partnership is being managed effectively. A limited partner who breaches this provision and engages in wrongful conduct will be personally liable for loss or injury caused directly to a third party as a result of that conduct where that third party reasonably believed that the limited partner was a general partner.

The bill also ensures that the safe harbour provisions provide for conduct by a person acting on behalf of the limited partner. This extends to conduct not only directly in respect of an incorporated limited partnership and its general partner, but also in respect of associated entities functions. It is understood, for example, that in practice certain functions, such as those requiring an Australian financial services licence, may be undertaken by a different entity associated with the incorporated limited partnership.

Proposed sections 73C and 73D outline assumptions that a person is entitled to make when dealing with an incorporated limited partnership. These include an assumption that the partnership has title to property, and that a person acting on behalf of the firm has complied with the partnership agreement. These provisions were included in the Victorian Partnership (Venture Capital Funds) Act 2003, and similar provisions exist in the Corporations Act 2001. As an incorporated limited partnership is a body corporate for the purposes of the Corporations Act, it is necessary to include proposed section 81A, which allows certain provisions of the Corporations Act not to be applied. This will ensure that both Acts work in tandem and do not cause confusion or inconvenience for those operating or dealing with incorporated limited partnerships.

Schedule 1 to the bill provides the provisions for winding up an incorporated limited partnership. This can be done either voluntarily or by a certificate of the registrar. Where it is done by certificate, any person aggrieved may appeal the application to the Supreme Court. Before issuing a certificate the registrar may ask an incorporated limited partnership to show cause before being wound up. This provision is important due to the interaction with the Commonwealth's venture capital legislation, as it may be that the partnership must take certain steps to comply with the requirements of the Commonwealth legislation.

While incorporated limited partnerships are not designed to raise funds from the public, any proposal to do so will be subject to the fundraising provisions in section 6D of the Corporations Act. This bill aligns the liability regime for limited partners in venture capital funds with the international preferred vehicle for venture capital investment. In addition to providing separate legal entity status to venture capital limited partnerships, Australian funds of funds and venture capital management partnerships, the bill recognises that the unique nature of venture capital investment demands certainty in respect of the liability of investors.

The bill provides that limited partners should have protection against involuntary entanglement in legal actions against the incorporated limited partnership. It also recognises that while limited partners have an active role in overseeing and assisting the investments of the partnership, and in ensuring that the incorporated limited partnership is being managed effectively, this role should not, of itself, expose the limited partner to liability. Providing that a limited partner stays inside the safe harbour provisions in the bill, their liability will remain limited.

This bill will help ensure that New South Wales attracts long-term economic investment by providing a structure that will allow investors to access Australian markets and invest in small, innovative enterprises. This will help to ensure that

Australian initiatives are developed and commercialised within Australia and, in particular, New South Wales. I commend the bill to the House.
