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A Review of Stephen Barkoczy, Don Maloney and Wayne Ngo, Pooled Development Funds Handbook

Primrose Mroczkowski
Monash University

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Abstract

Book Review of Stephen Barkoczy, Don Maloney and Wayne Ngo, *Pooled Development Funds Handbook* 2001 Australian Tax Practice, ISBN 0864602952, 305pp

BOOK REVIEW

Stephen Barkoczy, Don Maloney and Wayne Ngo, *Pooled Development Funds Handbook*

2001 Australian Tax Practice, ISBN 0864602952, 305pp

It has almost been a decade since the Australian Government introduced the Pooled Development Funds ('PDF') program. Its introduction was a reflection of the Government's recognition that certain small and medium-sized Australian enterprises (referred to as 'SMEs') are important contributors to the Australian economy and that some form of incentive to encourage greater investment in these entities was warranted. It is well established that, for a multitude of reasons, SMEs traditionally experience difficulties in effectively accessing finance for expansion and growth. The PDF program, at a simple level, involves a regime whereby the funding of SMEs via equity capital is encouraged, through entitlement to a series of tax incentives. Ten years on, in an increasingly competitive global economy, the significance of the PDF program and what it seeks to achieve has only been enhanced. Interestingly, however, not very much has been written on this program and, until recently, there was a vacuum in terms of comprehensive literature on this area. This state of affairs has now changed with the publication of the *Pooled Development Funds Handbook* ('*PDF Handbook*') by Barkoczy, Maloney and Ngo, (an ATP publication), the first definitive treatise of the PDF program.

The operational rules and regulations which facilitate the PDF program, contained within the *Pooled Development Funds Act 1992* (Cth) and the *Pooled Development Funds Regulations*, are highly intricate. Indeed, some commentators have attributed the initial, modest private sector interest in the PDF program, at least partly, to the fact that the regime is complex in nature and onerous in the qualifications and conditions that it imposes. It is notable that a raft of amendments was recently enacted with the aim of liberalising the rules and making the PDF program more attractive. Further, as a consequence of the Ralph Review of Business Taxation, related venture capital tax concessions have also been introduced. In the light of these developments, it appears that there has been a surge of interest in the PDF program.

Given the increasing practical significance of the PDF regime, and particularly also, given its level of complexity, there has been a need for a published scholarly work that provides not only a meaningful and an in-depth analysis of both the regulatory framework of the PDF program and the associated PDF tax concessions, but also a work that critically evaluates the regime as a whole. So far, there has arguably been an absence of such a work. The items of literature that do exist on this area, largely in the form of published articles, have generally had their focus on examining only aspects of the program. Further,

although most leading tax textbooks deal with the program, the coverage is usually brief and limited to the fundamentals. The gap in the literature has now been filled admirably with the *PDF Handbook*.

Before exploring the merits of the *PDF Handbook*, it is appropriate to briefly outline what the PDF program entails. In simple terms, the program facilitates the creation and operation of certain venture capital investment vehicles (PDFs) which are only permitted to invest, inter alia, in eligible companies (companies whose total asset values do not exceed \$50m and which do not have, as their primary activity, retail sale operations or acquisitions or disposals of interests in land). To ensure that PDFs operate in a manner consistent with the objectives of the program, PDFs are subject to a range of restrictions. There are, for example, limitations relating to both the capital structure of a PDF and the range of activities that could be undertaken by a PDF.

What motivates participation in the PDF program? Essentially, entitlement to a range of tax concessions under the *Income Tax Assessment Act 1936* (Cth) and *Income Tax Assessment Act 1997* (Cth). The key beneficiaries of these concessions are both the PDF and its shareholders. Some of the main tax concessions for PDF shareholders are exemption from tax on the gains made from the sale of PDF shares, and a choice (where the shareholder is resident) on whether to be exempt from income tax in respect of franked dividends. From the perspective of the PDFs, income and capital gains are sheltered at concessional tax rates (15% on income and gains from investments in SMEs, and 25% on other income and gains). A PDF is also able to credit its franking account for tax paid at the general corporate tax rate of 30%. PDFs are therefore able to pass on greater franking benefits to its shareholders than would otherwise be warranted by the rate of tax it pays.

With the publication of the *PDF Handbook*, there is now a treatise that provides an economically written, well-structured and comprehensive examination of the two main aspects to this area, the complex regulatory framework that governs the PDF program, and the special tax treatment of PDFs and their investors.

The chapters in the *PDF Handbook* are ordered in a logical sequence and, overall, the book can be divided up into four parts. The first part (Chapters 1 and 2) comprises an overview and an exploration of the historical context for the PDF regime. The second part (Chapters 3 to 7) examines the various aspects of the regulatory framework of the PDF program, such as the PDF Board, the registration of PDFs, capital raisings by PDFs and the management of PDFs. The third part of the book (Chapters 8 to 10) explores the PDF tax concessions for the PDF and its shareholders; and the last part (Chapters 11 and 12) provides an evaluation of these tax concessions and of the PDF

program as well. The book also contains a series of Appendices which provide useful material, from the PDF legislation and Regulations to a list of registered PDFs as at a particular date.

The wealth of experience of the authors of the *PDF Handbook* in PDFs is evident. All three authors are experienced tax practitioners and the subject matter of the book is explored very much from a practical perspective. There are, for instance, useful numerical and factual examples provided in the book to illustrate the effects of the PDF tax concessions. As they are largely the key to the success of the whole regime, there is a particular focus on the tax concessions. The authors not only articulate tax-planning issues for investors, but also identify deficiencies with the concessions. This information, although not a substitute for specific legal or tax advice, is at least a useful starting point for any potential investor interested in the PDF scheme. Further, the authors provide a critical evaluation of the operation of the program as a whole and make suggestions on how the regime might be further improved. Specific recommendations on how the tax rules might be reformed to make the program more attractive to potential investors are also detailed. Perhaps these recommendations will have some impact on the future shape of the PDF program itself. It is expected that there will be a review of the program before the end of 2003 (Explanatory Memorandum to the *Pooled Development Funds Amendment Bill 1999*) and it is not inconceivable that further amendments to the program may be made.

The *PDF Handbook* is well written and has a distinctive style that deals with complex issues in a comprehensible manner. It certainly makes information about an otherwise difficult area of the law more accessible. It will be of immense value to investors, legal practitioners, accountants, venture capitalists and other potential 'players' in the PDF scheme, not only because the book is an invaluable aid in the navigation of the PDF statutory regime, but also because it has the potential of assisting these entities in the making of more informed decisions.

Primrose Mroczkowski*

* Lecturer (Taxation Law), Department of Business Law and Taxation, Faculty of Business and Economics, Monash University.